

Edgar Filing: DYNATRONICS CORP - Form 10QSB

DYNATRONICS CORP  
Form 10QSB  
May 14, 2008

=====

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934

For the quarterly period ended March 31, 2008.

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 0-12697

Dynatronics Corporation

-----

(Exact name of small business issuer as specified in its charter)

Utah  
-----

87-0398434  
-----

(State or other jurisdiction of  
incorporation or organization)

(IRS Employer  
Identification No.)

7030 Park Centre Drive, Salt Lake City, UT 84121  
-----

(Address of principal executive offices)

(801) 568-7000  
-----

(Issuer's telephone number, including Area Code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No \_\_\_

Indicate by check mark whether the registrant is a shell company (as defined in rule 12b-2 of the Exchange Act). Yes \_\_\_ No X

The number of shares outstanding of the issuer's common stock, no par value, as of May 12, 2008 is approximately 13.7 million.

Transitional Small Business Disclosure Format (Check one): Yes \_\_\_ No X  
-----

# Edgar Filing: DYNATRONICS CORP - Form 10QSB

DYNATRONICS CORPORATION  
FORM 10-QSB  
MARCH 31, 2008  
TABLE OF CONTENTS

	Page Number -----
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements.....	1
Condensed Consolidated Balance Sheets	
March 31, 2008 and June 30, 2007 .....	1
Condensed Consolidated Statements of Operations	
Three and Nine Months Ended March 31, 2008 and 2007.....	2
Condensed Consolidated Statements of Cash Flows	
Nine Months Ended March 31, 2008 and 2007.....	3
Notes to Condensed Consolidated Financial Statements.....	4
Item 2. Management's Discussion and Analysis or Plan of Operation.....	9
Item 3. Controls and Procedures.....	18
PART II. OTHER INFORMATION	
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.....	18
Item 6. Exhibits.....	19

ii

DYNATRONICS CORPORATION  
Condensed Consolidated Balance Sheets  
(Unaudited)

Assets	March 31, 2008 -----	June 30, 2007 -----
Current assets:		
Cash	\$ 212,670	1,301,105
Trade accounts receivable, less allowance for doubtful accounts of \$181,990 at March 31, 2008 and \$330,857 at June 30, 2007	5,513,805	3,757,484
Other receivables	65,427	282,741
Inventories, net	6,952,979	5,313,984
Prepaid expenses	899,787	507,755
Prepaid income taxes	106,412	92,702

Edgar Filing: DYNATRONICS CORP - Form 10QSB

Deferred tax asset - current	408,429	396,156
	-----	-----
Total current assets	14,159,509	11,651,927
Property and equipment, net	3,617,687	3,453,495
Goodwill, net	6,623,596	2,758,572
Intangible asset, net	653,509	356,792
Deferred tax asset - noncurrent	495,058	-
Other assets	354,154	346,830
	-----	-----
	\$ 25,903,513	18,567,616
	=====	=====

Liabilities and Stockholders' Equity

Current liabilities:

Current installments of long-term debt	\$ 318,632	271,979
Line of credit	5,704,823	250,000
Warranty reserve	208,000	208,000
Accounts payable	2,380,281	1,241,030
Accrued expenses	395,275	287,773
Accrued payroll and benefit expenses	422,796	276,754
Acquisition cash obligations	-	1,000,000
	-----	-----
Total current liabilities	9,429,807	3,535,536

Long-term debt, excluding current installments	3,110,160	3,251,631
Deferred compensation	444,635	420,470
Deferred tax liability - noncurrent	-	289,335
	-----	-----
Total liabilities	12,984,602	7,496,972
	-----	-----

Commitments and contingencies

Stockholders' equity:

Common stock, no par value.		
Authorized 50,000,000 shares;		
issued 13,540,736 shares at		
March 31, 2008 and 10,308,522		
shares at June 30, 2007	7,755,184	4,227,147
Retained earnings	5,163,727	6,843,497
	-----	-----
Total stockholders' equity	12,918,911	11,070,644
	-----	-----
	\$ 25,903,513	18,567,616
	=====	=====

See accompanying notes to condensed consolidated financial statements.

Edgar Filing: DYNATRONICS CORP - Form 10QSB

	Three Months Ended March 31		Nine Months Ended March 31	
	2008	2007	2008	2007
Net sales	\$ 7,781,871	\$ 4,330,440	\$ 24,534,934	\$ 12,897,679
Cost of sales	4,946,912	2,719,548	15,428,447	8,163,440
Gross profit	2,834,959	1,610,892	9,106,487	4,734,239
Selling, general, and administrative expenses	3,325,765	1,368,680	10,240,809	3,938,693
Research and development expenses	368,994	328,980	1,070,993	1,153,736
Operating income (loss)	(859,800)	(86,768)	(2,205,315)	(358,190)
Other income (expense):				
Interest income	3,823	7,381	9,210	18,726
Interest expense	(165,613)	(54,870)	(463,216)	(155,640)
Other income, net	2,033	1,919	8,865	7,326
Net other income (expense)	(159,757)	(45,570)	(445,141)	(129,588)
Income (loss) before income taxes	(1,019,557)	(132,338)	(2,650,456)	(487,778)
Income tax expense (benefit)	(390,782)	(50,949)	(970,686)	(187,794)
Net income (loss)	\$ (628,775)	\$ (81,389)	\$ (1,679,770)	\$ (299,984)
Basic and diluted net income (loss) per common share	\$ (0.05)	\$ (0.01)	\$ (0.12)	\$ (0.03)
Weighted average basic and diluted common shares outstanding (note 2)				
Basic	13,579,328	8,881,534	13,616,237	8,936,425
Diluted	13,579,328	8,881,534	13,616,237	8,936,425

Edgar Filing: DYNATRONICS CORP - Form 10QSB

See accompanying notes to condensed consolidated financial statements.

2

DYNATRONICS CORPORATION  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

	Nine Months Ended March 31	
	2008	2007
	-----	-----
Cash flows from operating activities:		
Net loss	\$ (1,679,770)	(299,984)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization of property and equipment	276,844	266,108
Amortization of intangible assets	69,683	5,493
Stock based compensation expense	292,365	6,374
Provision for doubtful accounts	190,000	24,000
Provision for inventory obsolescence	126,000	126,000
Provision for deferred income taxes	(971,854)	-
Provision for warranty reserve	209,137	198,792
Provision for deferred compensation	24,165	24,165
Change in operating assets and liabilities:		
Receivables	(360,468)	(109,726)
Inventories	(572,356)	(154,519)
Prepaid expenses and other assets	(394,574)	144,232
Accounts payable and accrued expenses	(313,142)	(651,136)
Prepaid income taxes	(13,710)	(196,402)
	-----	-----
Net cash used in operating activities	(3,117,680)	(616,603)
	-----	-----
Cash flows from investing activities:		
Capital expenditures	(238,138)	(68,009)
Business acquisitions	(1,839,794)	-
	-----	-----
Net cash used in investing activities	(2,077,932)	(68,009)
	-----	-----
Cash flows from financing activities:		
Principal payments on long-term debt	(184,952)	(193,281)
Net change in line of credit	4,454,823	1,090,786
Proceeds from issuance of common stock	49,225	23,664
Redemption of common stock	(211,919)	(192,444)
	-----	-----
Net cash provided by financing activities	4,107,177	728,725
	-----	-----
Net change in cash	(1,088,435)	44,113

Edgar Filing: DYNATRONICS CORP - Form 10QSB

Cash at beginning of period	1,301,105	423,184
	-----	-----
Cash at end of period	\$ 212,670	467,297
	=====	=====
Supplemental disclosures of cash flow information:		
Cash paid for interest	\$ 438,872	152,215
Cash paid for income taxes	8,700	8,608
Supplemental disclosure of non-cash investing and financing activities:		
Stock based compensation - see note 3 for details		
Business acquisition disclosure - see note 9 for details		
Capital expenditures financed by long term debt	90,134	-
Acquisition cash obligation financed by line of credit	1,000,000	-

See accompanying notes to condensed consolidated financial statements.

3

DYNATRONICS CORPORATION  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
March 31, 2008  
(Unaudited)

NOTE 1. PRESENTATION

The condensed consolidated balance sheet as of March 31, 2008 and condensed consolidated statements of operations and cash flows for the three and nine months ended March 31, 2008 and 2007 were prepared by Dynatronics Corporation without audit pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, all necessary adjustments, which consist only of normal recurring adjustments, to the financial statements have been made to present fairly the financial position and results of operations and cash flows. The results of operations for the respective periods presented are not necessarily indicative of the results for the respective complete years. The Company has previously filed with the SEC an annual report on Form 10-KSB which included audited financial statements for the two years ended June 30, 2007 and 2006. It is suggested that the financial statements contained in this filing be read in conjunction with the statements and notes thereto contained in the Company's form 10-KSB filing.

NOTE 2. NET INCOME PER COMMON SHARE

Net income (loss) per common share is computed based on the weighted-average number of common shares and, as appropriate, dilutive common stock equivalents outstanding during the period. Stock options are considered to be common stock equivalents. The computation of diluted earnings per share does not assume

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

exercise or conversion of securities that would have an anti-dilutive effect.

Basic net income (loss) per common share is the amount of net income (loss) for the period available to each share of common stock outstanding during the reporting period. Diluted net income (loss) per common share is the amount of net income (loss) for the period available to each share of common stock outstanding during the reporting period and to each common stock equivalent outstanding during the period, unless inclusion of common stock equivalents would have an anti-dilutive effect.

In calculating net income (loss) per common share, the net income (loss) was the same for both the basic and diluted calculation for the three and nine months ended March 31, 2008 and 2007. A reconciliation between the basic and diluted weighted-average number of common shares for the three and nine months ended March 31, 2008 and 2007 is summarized as follows:

	(Unaudited) Three Months Ended March 31,		(Unaudited) Nine Months Ended March 31,	
	2008	2007	2008	2007
Basic weighted average number of common shares outstanding during the period	13,579,328	8,881,534	13,616,237	8,936,425
Weighted average number of dilutive common stock options outstanding during the period	-0-	-0-	-0-	-0-
Diluted weighted average number of common and common equivalent shares outstanding during the period	13,579,328	8,881,534	13,616,237	8,936,425
	=====	=====	=====	=====

4

Outstanding options not included in the computation of diluted net loss per share for the three month periods ended March 31, 2008 and 2007 total 1,323,464 and 830,757 and for the nine month periods ended March 31, 2008 and 2007 total 730,646 shares and 810,193 respectively, because to do so would have been anti-dilutive.

### NOTE 3. STOCK BASED COMPENSATION

Stock-based compensation cost is measured at grant date, based on the fair value of the award, and is recognized over the employee requisite service period. The Company recognized \$18,390 and \$2,374 in stock-based compensation during the three months ended March 31, 2008 and 2007, respectively, and recognized \$292,365 and \$6,374 in stock-based compensation during the nine months ended March 31, 2008 and 2007, respectively, as selling, general, and administrative expenses in the condensed consolidated statements of operations.

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

On July 1, 2007, the Company granted 220,000 shares of common stock to employees with an estimated value of \$1.08 per share. This stock had a ninety day vesting period. On July 1, 2007, the Company also granted 80,000 shares of common stock with an estimated value of \$1.08 per share, which vested over a four-year period in annual installments of 20,000 shares per year. The Company recognized \$11,250 and \$272,700 in stock-based compensation during the three and nine month periods ended March 31, 2008, respectively, from these shares. As of March 31, 2008, \$52,650 in unrecognized stock-based compensation from the unvested shares is expected to be recognized over the remainder of the four-year period.

### NOTE 4. COMPREHENSIVE INCOME

For the periods ended March 31, 2008 and 2007, comprehensive income was equal to the net income as presented in the accompanying condensed consolidated statements of operations.

### NOTE 5. INVENTORIES

Inventories consisted of the following:

	March 31, 2008	June 30, 2007
	-----	-----
Raw material	\$ 3,278,192	2,961,653
Finished goods	4,060,410	2,646,141
Inventory reserve		
	(385,623)	(293,810)
	-----	-----
	\$ 6,952,979	5,313,984
	=====	=====

### NOTE 6. PROPERTY AND EQUIPMENT

Property and equipment were as follows:

	March 31, 2008	June 30, 2007
	-----	-----
Land	\$ 354,743	354,743
Buildings	3,682,504	3,603,380
Machinery and equipment	1,656,230	1,521,601
Office equipment	1,281,926	1,147,667
Vehicles	188,148	95,124
	-----	-----
	7,163,551	6,722,515
Less accumulated depreciation and amortization	3,545,864	3,269,020
	-----	-----
	\$ 3,617,687	3,453,495
	=====	=====

### NOTE 7. PRODUCT WARRANTY RESERVE

The Company accrues the estimated costs to be incurred in connection with its



## Edgar Filing: DYNATRONICS CORP - Form 10QSB

product warranty programs as products are sold based on historical warranty rates. A reconciliation of the changes in the warranty liability is as follows:

	Three months ended March 31, 2008	Three months ended March 31, 2007
	-----	-----
Beginning product warranty reserve balance	\$ 208,000	208,000
Warranty repairs	(81,962)	(64,235)
Warranties issued	117,848	62,157
Changes in estimated warranty costs	(35,886)	2,078
	-----	-----
Ending product warranty liability balance	\$ 208,000	208,000
	=====	=====
	Nine months ended March 31, 2008	Nine months ended March 31, 2007
	-----	-----
Beginning product warranty reserve balance	\$ 208,000	208,000
Warranty repairs	(209,137)	(198,792)
Warranties issued	371,556	185,128
Changes in estimated warranty costs	(162,419)	13,664
	-----	-----
Ending product warranty liability balance	\$ 208,000	208,000
	=====	=====

### NOTE 8. COMMON STOCK.

The Company received proceeds of \$49,225 during the nine months ended March 31, 2008 for 47,499 shares of common stock that were issued upon the exercise of options for services.

### NOTE 9. ACQUISITION AND NON-CASH DISCLOSURE

On July 2, 2007, the Company completed the acquisition of a 100% interest in five of its key independent distributors, Responsive Providers, Inc. of Houston, Texas, Therapy and Health Care Products, Inc. of Youngstown, Ohio, Cyman Therapy, Inc. of Detroit, Michigan, Al Rice and Associates, Inc. of Jeffersonville, Indiana and Theratech Inc. of Minneapolis, Minnesota. The total consideration paid for the five separately-negotiated acquisitions was approximately \$5.6 million comprised of approximately \$2.3 million in cash and 3,061,591 shares of common stock.

The acquisition value of the five dealers acquired was accounted for using the purchase method of accounting. Accordingly, the purchase price was assigned to the assets acquired and the liabilities assumed based on fair values at the purchase date. The following table reflects the unaudited estimated fair values of the assets acquired and the liabilities assumed as of the acquisition date:

Cash	\$	651,828
Trade accounts receivable		1,160,976
Inventories		1,192,639
Prepaid expenses		4,782

Edgar Filing: DYNATRONICS CORP - Form 10QSB

Property and equipment	112,764
Cash surrender value of life insurance	207,563
Intangible assets - weighted average 9 years	366,400
Goodwill	3,512,779
	-----
Total assets acquired	7,209,731
Accounts payable and accrued expenses	(1,496,800)
	-----
Net assets acquired	5,712,931
	=====

The acquisition resulted in a \$175,188 deferred income tax liability and a corresponding increase to goodwill of \$175,188.

Unaudited pro forma results of operations for the three and nine months ended March 31, 2008 and 2007, as though the five dealers had been acquired as of July 1, 2006, are as follows:

	Three months ended March 31, 2008	Three months ended March 31, 2007
	-----	-----
Net sales	\$ 7,781,871	6,542,337
Net loss	(628,775)	(46,906)
Basic and diluted net loss per common share	(.05)	(.00)

	Nine months ended March 31, 2008	Nine months ended March 31, 2007
	-----	-----
Net sales	\$ 24,534,934	19,472,975
Net loss	(1,679,770)	(196,534)
Basic and diluted net loss per common share	(.12)	(.02)

NOTE 10. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill. The cost of the acquired companies in excess of the fair value of the net assets and purchased intangible assets at acquisition date is recorded as goodwill. As of March 31, 2008 the Company had net goodwill of \$6,646,481 arising from various acquisitions. Goodwill is subject to annual specified impairment tests or more frequently if events or changes in circumstances indicate that goodwill might be impaired. There were no goodwill impairment losses recorded during the three and nine month periods ended March 31, 2008.

Identifiable Intangibles. Identifiable intangibles assets consists of the following:

	As of March 31, 2008	As of June 30, 2007
	-----	-----
Trade name - 15 years	\$ 339,400	118,000
Domain name - 15 years	5,400	1,200
Non-compete covenant - 4 years	149,400	114,000
Customer relationships - 7-15 years	120,000	89,000
Trademark licensing agreement - 20 years	45,000	-0-
Backlog of orders - 3 months	2,700	2,700
Customer database - 7 years	38,100	8,700
License agreement - 10 years	73,240	73,240

Edgar Filing: DYNATRONICS CORP - Form 10QSB

Total identifiable intangibles	773,240	406,840
Accumulated amortization	119,731	50,048
Net carrying amount	\$ 653,509	356,792

7

NOTE 11. RECENT ACCOUNTING PRONOUNCEMENTS

On July 13, 2006, FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes - An Interpretation of FASB No. 109, was issued. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006. Accordingly, the Company adopted the revised standard during the quarter ended September 30, 2007. The adoption of this standard had no material impact on the Company's financial statements.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS 157 defines fair value, establishes a framework for measuring fair value, and expands disclosure requirements regarding fair value measurement. Where applicable, this statement simplifies and codifies fair value related guidance previously issued within United States of America generally accepted accounting principles. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 for financial assets and November 15, 2008 for non-financial assets, and interim periods within those fiscal years. The Company is currently reviewing SFAS 157 and has not yet determined the impact that the adoption of SFAS 157 will have on its results of operations or financial condition.

In December 2007, the FASB Statement 141R, "Business Combinations" ("SFAS 141R") was issued. SFAS 141R replaces SFAS 141. SFAS 141R requires the acquirer of a business to recognize and measure the identifiable assets acquired, the liabilities assumed, and any non-controlling interest of the acquired company at fair value. SFAS 141R also requires transactions costs related to the business combination to be expensed as incurred. SFAS 141R applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The effective date for the Company will be January 1, 2009. We have not yet determined the impact of SFAS 141R related to future acquisitions, if any, on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 160, "Non-controlling Interests in Consolidated Financial Statements - An Amendment of ARB No. 51," which establishes accounting and reporting standards to improve the relevance, comparability, and transparency of financial information in its consolidated financial statements. This is accomplished by requiring all entities, except not-for-profit organizations, that prepare consolidated financial statements to (a) clearly identify, label, and present ownership interests in subsidiaries held by parties other than the parent in the consolidated statement of financial position within equity, but separate from the parent's equity, (b) clearly identify and present both the parent's and the non-controlling's interest attributable consolidated net income on the face of the consolidated statement of income, (c) consistently account for changes in parent's ownership interest while the parent retains it controlling financial interest in subsidiary and for all transactions that are economically similar to be accounted for similarly, (d) measure of any gain, loss or retained non-controlling equity at fair value

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

after a subsidiary is deconsolidated, and (e) provide sufficient disclosures that clearly identify and distinguish between the interests of the parent and the interests of the non-controlling owners. This Statement also clarifies that a non-controlling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. SFAS No. 160 is effective for fiscal years, and interim periods on or after December 15, 2008. The management of the Company does not expect the adoption of this pronouncement to have a material impact on its financial statements.

In June 2007, the FASB ratified Emerging Issues Task Force (EITF) Issue No. 06-11, "Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards." EITF06-11 requires companies to recognize the income tax benefit realized from dividends or dividend equivalents that are charged to retained earnings and paid to employees for non-vested equity-classified employee share-based payment awards as an increase to additional paid-in capital. EITF 06-11 is effective for fiscal years beginning after September 15, 2007. The Company does not expect EITF 06-11 will have a material impact on its financial statements.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities - an amendment of FASB Statement No. 133, ("SFAS No. 161"), which requires companies to provide additional disclosures about its objectives and strategies for using derivative instruments, how the derivative instruments and related hedged items are accounted for under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, and related interpretations, and how the derivative instruments and related hedged items affect the Company's financial statements. SFAS No. 161 also requires companies to disclose information about credit risk-related contingent features in their hedged positions. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008. Although the Company will continue to evaluate the application of SFAS No. 161, management does not currently believe adoption will have a material impact on the Company's financial condition or operating results.

8

### Item 2. Management's Discussion and Analysis or Plan of Operation

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the Financial Statements (unaudited) and Notes thereto appearing in Part I, Item 1 of this report on Form 10-QSB.

#### Results of Operations

-----

The Company's fiscal year ends on June 30th. This report covers the three and nine months ended March 31, 2008, for the Company's fiscal year ending June 30, 2008.

#### Net Sales

During the quarter ended March 31, 2008, the Company's sales increased 79.7% to \$7,781,871, compared to \$4,330,440 in the quarter ended March 31, 2007. For the nine months ended March 31, 2008, the Company's sales increased 90.2% to

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

\$24,534,934, compared to \$12,897,679 in the nine month period ended March 31, 2007. The increase in sales is the result of the addition of revenues from the Company's acquisition of six of its distributors of physical medicine products completed on June 30, 2007 and July 2, 2007. On June 30, 2007, we acquired our largest independent distributor, Rajala Therapy Sales Associates of Pleasanton, California. On July 2, 2007, Dynatronics acquired five additional independent distributors: Responsive Providers, Inc. of Houston, Texas; Therapy and Health Care Products, Inc. of Girard, Ohio; Cyman Therapy, Inc. of Detroit, Michigan; Al Rice and Associates, Inc. of Jeffersonville, Indiana; and Theratech, Inc. of Minneapolis, Minnesota. The vertical integration of these distributors is a key strategic step toward strengthening our distribution channels. We believe that these acquisitions, as they are fully assimilated into our business operations, will provide Dynatronics with more effective direct distribution of our products and result in better margins on each product sold at the retail level compared to the wholesale level. Subsequent to these acquisitions, we added twelve new direct sales persons in other territories including Southern California, Louisiana, Kansas, Oklahoma, and Missouri, expanding our direct sales force to 40 sales representatives covering 30 states.

The acquired distributors sell products from many manufacturers, including Dynatronics. As a result of the transactions described above, the mix between Company's sales of manufactured and distributed products during the quarter covered by this report shifted toward distributed products with 42% of sales attributed to sales of distributed products and the remaining 58% being manufactured products. By comparison, during the same period in fiscal year 2007, the mix between manufactured and distributed products was 71% and 29%, respectively. We anticipate the mix between manufactured and distributed products in future periods will be similar to the mix experienced during the first three quarters of fiscal year 2008.

### Gross Profit

During the quarter ended March 31, 2008, gross profit increased 76% to \$2,834,959, or 36.4% of net sales, compared to \$1,610,892, or 37.2% of net sales, in the quarter ended March 31, 2007. For the nine months ended March 31, 2008, gross profit increased 92.4% to \$9,106,487, or 37.1% of net sales, compared to \$4,734,239, or 36.7% of net sales, in the nine months ended March 31, 2007. The increase in gross profit in the three and nine month periods was primarily a result of the sales added by the recent acquisitions. For the quarter ended March 31, 2008, gross profit as a percent of sales decreased 0.8 percentage point to 36.4% due to a shift in product mix toward sales of medical supplies and distributed items which generate lower margins as a percent of sales compared to the Company's manufactured medical devices and products.

### Selling, general and administrative expenses

Selling, general and administrative ("SG&A") expenses for the quarter ended March 31, 2008 increased \$1,957,085 to \$3,325,765, or 42.7% of net sales, compared to \$1,368,680, or 31.6% of net sales in the prior year period. SG&A expenses for the nine months ended March 31, 2008 increased \$6,302,116 to \$10,240,809, or 41.7% of net sales, compared to \$3,938,693, or 30.5% of net sales in the prior year period. Substantially all of the increase in SG&A expenses for the nine months ended March 31, 2008 is related to the recent acquisitions and includes the following:

- o \$3,315,500 in higher selling expenses primarily related to the new direct sales force
- o \$1,878,400 in higher labor and operating costs to support the higher sales volume
- o \$1,360,700 in higher general and administrative expenses associated with the acquired companies

With the assimilation of the six acquisitions substantially completed, during the quarter ended March 31, 2008, management implemented measures designed to reduce annual operating expenses by an estimated \$1.9 million. These cost savings are expected to be achieved by a reduction of approximately 20 percent of the Company's workforce and the elimination of duplicative overhead expense. In addition, we consolidated operations from eight distribution points to three. Many of these reductions had been contemplated as part of the planning for the acquisition and assimilation of the distributors in 2007. We believe these reductions in expenses will not negatively impact the Company's sales or operations. The implementation of the cost reductions caused us to incur severance costs of approximately \$102,000 that were expensed in the quarter ended March 31, 2008; we expect to see the benefit of those reductions in our operating results commencing in the fourth quarter 2008.

#### Research and Development

Research and Development ("R&D") expense during the quarter ended March 31, 2008 increased to \$368,994, compared to \$328,980 in the prior year period. The increase in the current quarter is attributable to the final stages of completing the new Synergie Elite line of products. R&D expense during the nine months ended March 31, 2008 decreased to \$1,070,993 compared to \$1,153,736 in the prior year period. R&D expense represented approximately 4.7% and 7.6% of the net sales of the Company in the quarters ended March 31, 2008 and 2007, respectively. R&D expenditures as a percentage of sales were lower due to the additional sales during the quarter and nine month periods ended March 31, 2008 due to the acquisitions, compared to the prior year periods which predated the acquisitions. R&D costs are expensed as incurred. Dynatronics intends to continue its commitment to developing innovative products for the physical medicine market in fiscal year 2008 and beyond in order to position the Company for growth.

#### Pre-tax Loss

Pre-tax loss for the quarter ended March 31, 2008 was \$1,019,557 compared to a pre-tax loss of \$132,338 in the quarter ended March 31, 2007. Pre-tax loss for the nine months ended March 31, 2008 was \$2,650,456 compared to a pre-tax loss of \$487,778 in the similar period ended March 31, 2007. Included in the pre-tax loss in the quarter ended March 31, 2008 was approximately \$100,000 of severance costs related to the reduction in force completed during the quarter, as well as approximately \$450,000 in costs management believes have been eliminated through the cost cutting measures implemented at the end of the quarter.

#### Income Tax Benefit

Income tax benefit for the quarter ended March 31, 2008 was \$390,782 compared to income tax benefit of \$50,949 in the quarter ended March 31, 2007. Income tax benefit for the nine months ended March 31, 2008 was \$970,686 compared to income tax benefit of \$187,794 in the nine months ended March 31, 2007. The effective tax rate for the quarter ended March 31, 2008 was 38.3% compared to 38.5% for the prior year period. The effective tax rate for the nine months ended March 31, 2008 was 36.6% compared to 38.5% for the prior year period. The lower tax rate for this quarter and nine month period ended March 31, 2008 reflects the assumption of certain anticipated tax benefits that will be earned during the year.

#### Net Loss

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

Net loss for the quarter ended March 31, 2008 was \$628,775 (\$.05 per share), compared to net loss of \$81,389 (\$.01 per share) in the quarter ended March 31, 2007. Net loss for the nine months ended March 31, 2008 was \$1,679,770 (\$.12 per share), compared to a net loss of \$299,984 (\$.03 per share) in the nine months ended March 31, 2007.

### Recent Developments

On April 17, 2008, Dynatronics announced the introduction of the DynaPro Spinal Health System, a non-surgical treatment for back and neck pain. This innovative system combines the benefits of decompression and light therapy with core-stabilization exercises and nutrition, together forming a very effective tool for reducing pain.

Another new product introduced on April 17, 2008 was the new Dynatron X5 "Turbo" soft-tissue oscillation therapy unit. The new X5 "Turbo" is three times more powerful than the original X5 device and is a highly effective treatment for acute as well as chronic pain.

10

In April 2008, we began shipments of the new "Synergie Elite" line of aesthetic treatment devices. This new line is comprised of cellulite treatment devices, microdermabrasion units and bio-stimulation light therapy equipment. These new products represent the first time in 10 years the Synergie line of products have been updated. Initial response to the new Synergie Elite equipment at trade shows has been promising. The new updated design and additional features make the Synergie Elite products not only visually attractive, but functionally enhanced positioning us to better compete in the aesthetic markets.

### Liquidity and Capital Resources

-----

The Company has financed its operations through available cash reserves and borrowings under its line of credit. The Company had working capital of \$4,729,702 at March 31, 2008, inclusive of the current portion of long-term obligations and credit facilities, compared to working capital of \$8,116,391 at June 30, 2007. The \$3.4 million decrease in working capital over the nine month period is a direct result of a \$5,455,000 increase in the line of credit that was required in part to finance a \$3,400,000 increase in accounts receivable and inventory and to finance a portion of the \$3.3 million in cash expended in the acquisitions in June and July 2007. The remaining reduction in working capital is accounted for by increased accounts payable and lower cash balances.

### Accounts Receivable

Trade accounts receivable, net of allowance for doubtful accounts, increased \$1,756,321 to \$5,513,805 at March 31, 2008, compared to \$3,757,484 at June 30, 2007. The majority of this increase in trade accounts receivable was a result of increased sales associated with the recent acquisitions. During the first eight months following the acquisitions, new billing paradigms were implemented to accommodate large orders from certain retail customers. These billing paradigms allowed extended terms for payment until complete orders had been delivered. These extended terms significantly delayed collection on some orders that had components delivered over a three to four month period of time. We are modifying these arrangements to require that all products subject to special term orders will be delivered within a specific 30 day period or the customer will be required to pay monthly for product shipped. As these accounts are collected and the new policy implemented, we expect accounts receivable to decrease in coming

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

quarters.

Trade accounts receivable represent amounts due from the Company's dealer network, from medical practitioners and clinics. We estimate that the allowance for doubtful accounts is adequate based on our historical knowledge and relationship with these customers. Except for those special accounts described above, accounts receivable are generally due within 30 days of the agreed terms. However, as a result of the recent acquisitions, the character of the accounts receivable and collection patterns have changed and will be carefully monitored over the coming year to ensure the allowance estimates are adequate. Allowances for the retail accounts assumed in the acquisitions are currently calculated based on the historical experience of the acquired companies.

### Inventories

Inventories, net of reserves, at March 31, 2008 increased \$1,638,995 to \$6,952,979 compared to \$5,313,984 at June 30, 2007. This increase is primarily a result of the inventories acquired in connection with the acquisitions. Inventories are expected to reduce modestly now that we have consolidated eight distribution points to three central distribution facilities.

### Goodwill

Goodwill at March 31, 2008 increased to \$6,623,596, compared to \$2,758,572 at June 30, 2007. This increase in goodwill is attributable to the acquisitions completed on July 2, 2007.

In compliance with Statement of Financial Accounting Standard ("SFAS") No. 142, management utilized standard principles of financial analysis and valuation including: transaction value, market value and income value methods to arrive at a reasonable estimate of the fair value of the Company in comparison to its book value. The Company has determined it has one reporting unit. As of July 1, 2002 and June 30, 2007, management believes the fair value of the Company exceeded the book value of the Company. Therefore, there was no indication of impairment at June 30, 2007. Management is primarily responsible for the SFAS No. 142 valuation determination and performed the annual impairment assessment during the Company's fourth quarter.

11

### Accounts Payable

Accounts payable increased \$1,139,251 to \$2,380,281 at March 31, 2008, compared to \$1,241,030 at June 30, 2007, primarily as a result of the recent acquisitions and the increased level of sales associated with those acquisitions. Accounts payable are generally within term with the exception of disputed or inadequately documented payables that are associated with the transition and assimilation of the acquired dealers. We attempt to take advantage of available early payment discounts when offered.

### Accrued Expenses and Acquisition Cash Obligation

Accrued expenses increased \$107,502 to \$395,275 at March 31, 2008, compared to \$287,773 at June 30, 2007, primarily as a result of increased sales at the retail level which generate higher sales tax liabilities in the 30 states where we now sell on a direct basis.

Acquisition cash obligations decreased to \$0 at March 31, 2008, compared to \$1,000,000 at June 30, 2007. This obligation at June 30 reflected the cash



## Edgar Filing: DYNATRONICS CORP - Form 10QSB

amount that was placed into escrow in conjunction with the acquisition made on June 30, 2007, which was paid subsequently.

### Accrued Payroll and Benefit Expenses

Accrued payroll and benefit expenses increased \$146,042 to \$422,796 at March 31, 2008, compared to \$276,754 at June 30, 2007. The increase in accrued payroll and benefit expenses is related to timing differences as well as increased number of employees resulting in higher accrued payroll at March 31, 2008 compared to June 30, 2007.

### Cash

The Company's cash position decreased to \$212,670, compared to \$1,301,105 at June 30, 2007, as a result of payments related to the acquisitions made on June 30, 2007 and July 2, 2007. The Company had deposited the financing proceeds in anticipation of the acquisitions, which temporarily increased cash balances at June 30, 2007. The Company believes that improved cash flow from operations through improving management of accounts receivable, maintaining current inventory levels and the recently implemented reductions in expenses will further minimize operating losses and expedite a return to profitability. This improved cash flow combined with balances under available lines of credit is expected to be sufficient to cover operating needs in the ordinary course of business for the next twelve months. If we experience an adverse operating environment or unusual capital expenditure requirements, additional financing may be required. However, no assurance can be given that additional financing, if required, would be available on favorable terms.

### Line of Credit

In March 2008, the Company temporarily increased its revolving line of credit with a commercial bank from \$6,500,000 to \$8,000,000. At March 31, 2008, the Company owed \$5,704,823 compared to \$250,000 at June 30, 2007. The increase in the line of credit was the result of the following factors:

- o The Company used approximately \$3.3 million under the line of credit to finance the acquisitions after June 30, 2007.
- o Receivables and inventory increased \$3,400,000, while payables increased approximately \$1,139,000. This imbalance of slower collections while maintaining payables more current required additional financing demands on the line of credit.
- o Operating losses and capital expenditures, mostly associated with the acquisitions, required additional financing provided by the line of credit.

Interest on the line of credit is based on the bank's prime rate plus 1%, which at March 31, 2008, equaled 6.25%. The line of credit is collateralized by accounts receivable and inventories of the Company. Borrowing limitations are based on approximately 45% of eligible inventory and up to 80% of eligible accounts receivable. Interest payments on the line are due monthly. The line of credit is renewable biennially on December 15th and includes covenants requiring the Company to maintain certain financial ratios. As of March 31, 2008, the Company was in compliance with all loan covenants or had received waivers of any noncompliance.

The current ratio was 1.5 to 1 at March 31, 2008 compared to 3.3 to 1 at June 30, 2007. Current assets represented 55% of total assets at March 31, 2008, compared to 63% at June 30, 2007.

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

### Debt

Long-term debt excluding current installments totaled \$3,110,160 at March 31, 2008, compared to \$3,251,631 at June 30, 2007. In June 2007, we obtained \$1.5 million of long-term mortgage financing used to finance our acquisitions in June and July 2007. The funding of this loan temporarily increased our cash balances at the end of June 2007. Long-term debt is comprised primarily of the mortgage loans on our office and manufacturing facilities in Utah and Tennessee. The principal balance on the mortgage loans is approximately \$3.4 million with monthly principal and interest payments of \$40,707.

### Inflation and Seasonality

The Company's revenues and net income from continuing operations have not been unusually affected by inflation or price increases for raw materials and parts from vendors.

The Company's business operations are not materially affected by seasonality factors.

### Critical Accounting Policies

We have identified the policies below as critical to our business operations and an understanding of our results of operations. The impact and risks related to these policies on our business operations are discussed where such policies affect our reported and expected financial results. In all material respects, management believes that the accounting principles that are utilized conform to accounting principles generally accepted in the United States of America.

The preparation of this quarterly report requires us to make significant estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses reported in our unaudited financial statements. By their nature, these judgments are subject to an inherent degree of uncertainty. On an on-going basis, we evaluate these estimates, including those related to bad debts, inventories, and revenue recognition. We base our estimates on historical experience and other facts and circumstances that are believed to be reasonable, and the results form the basis for making judgments about the carrying value of assets and liabilities. The actual results may differ from these estimates under different assumptions or conditions.

### Inventory Reserves

The nature of our business requires that we maintain sufficient inventory on hand at all times to meet the requirements of our customers. We record finished goods inventory at the lower of standard cost, which approximates actual costs (first-in, first-out) or market. Raw materials are recorded at the lower of cost (first-in, first-out) or market. Inventory valuation reserves are maintained for the estimated impairment of the inventory. Impairment may be a result of slow moving or excess inventory, product obsolescence or changes in the valuation of the inventory. In determining the adequacy of reserves, we analyze the following, among other things:

- o Current inventory quantities on hand.
- o Product acceptance in the marketplace.
- o Customer demand.
- o Historical sales.
- o Forecast sales.
- o Product obsolescence.
- o Technological innovations.
- o Character of the inventory whether it is a distributed item,

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

finished manufactured item or raw material.

Any modifications to estimates of inventory valuation reserves are reflected in the cost of goods sold within the statements of income during the period in which such modifications are determined necessary by management. At March 31, 2008 and June 30, 2007, our inventory valuation reserve balance, which established a new cost basis, was \$385,623 and \$293,810, respectively, and our inventory balance was \$6,952,979 and \$5,313,984 net of reserves, respectively.

### Revenue Recognition

The majority of our product sales for the fiscal year ended June 30, 2007, were to customers who are independent distributors. Beginning in the fiscal first quarter ended September 30, 2007, a significant portion of our sales were generated through our new direct sales force. Our sales force and distributors sell our products to end users, including physical therapists, professional trainers, athletic trainers, chiropractors, medical doctors and aestheticians. With the acquisition of key distributors, we effectively reduced our dependence

13

on sales by independent distributors. Sales revenues are recorded when products are shipped FOB shipping point under an agreement with a customer, risk of loss and title have passed to the customer, and collection of any resulting receivable is reasonably assured. Amounts billed for shipping and handling of products are recorded as sales revenue. Costs for shipping and handling of products to customers are recorded as cost of sales.

### Allowance for Doubtful Accounts

We must make estimates of the collectibility of accounts receivable. In doing so, we analyze historical bad debt trends, customer credit worthiness, current economic trends and changes in customer payment patterns when evaluating the adequacy of the allowance for doubtful accounts. Our accounts receivable balance was \$5,513,805 and \$3,757,484, net of allowance for doubtful accounts of \$181,990 and \$330,857, at March 31, 2008 and June 30, 2007, respectively. The expansion of our customer base associated with more direct sales will spread bad debt risk over a broader base of customers and reduce the concentration of large dealer balances. At the same time, the management of more customer accounts presents a higher risk. These risks will be evaluated over the coming year to determine if current estimate policies are still applicable. In the meantime, allowance for doubtful accounts associated with these acquired customers is being based on the historical experience of the dealers acquired.

### Business Plan and Outlook

During fiscal year 2008, we will continue to implement a four-fold strategy to improve overall operations. This strategy focuses on (1) strengthening in-house distribution channels; (2) developing new, state-of-the-art products for future growth; (3) refining operations associated with the acquired companies and reducing overhead costs; and (4) enhancing product profit margins through improved manufacturing processes. Our goal in implementing this four-fold strategy is to enable the Company to address short-term profitability without jeopardizing long-term growth.

Our primary market, the physical medicine marketplace, has experienced significant change over the past few years, most notably with consolidation among manufacturers and distributors. In order to compete more favorably and effectively, we moved aggressively to strengthen our channels of distribution by acquiring key distributors. We identified six key distributors with operations

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

in 20 states. On June 30, 2007, we acquired our largest independent distributor headquartered in California. On July 2, 2007, we acquired five additional key independent distributors headquartered in Texas, Ohio, Michigan, Indiana and Minnesota. We also began hiring direct sales representatives in key locations around the country resulting in direct sales representatives now in 30 states. The creation of a direct distribution channel through these key acquisitions and hiring direct sales representatives provides Dynatronics with expanded ability to sell at the retail level, which we believe will improve gross profit margins and enhance the Company's control over the distribution process. We expect these changes will open new opportunities for improving future sales as we continue to pursue our strategy of strengthening our distribution channels through consideration of additional acquisitions, the expansion of our direct sales force, and maximizing our relationships with strong independent dealers.

In the fiscal year ended June 30, 2007, Dynatronics introduced many new products including the following:

- o Dynatron X3 - A powerful light therapy device capable of powering a light probe and two light pads simultaneously was introduced in August 2006.
- o Dynatron DX2 - Dynatronics' first proprietary traction device that offers not only decompression therapy, but also light therapy was introduced in December 2006.
- o Dynatron T4 Table - This motorized treatment table was introduced in March 2007 and is designed to be used in decompression and traction therapy.
- o Dynatron T3 Table - This motorized treatment table was introduced in July 2007 and was an enhancement of the company's popular HLT3 treatment table.
- o Dynatron X5 - A unique modality providing Oscillation Therapy for the reduction of pain using electrostatic fields that combine concepts from electrotherapy and therapeutic massage was introduced in June 2007.

Fiscal 2007 was an important year for introduction of new devices and technology. Significant investments were made in research and development to bring these products to market. That commitment to bringing new products to market has continued in the current fiscal year. Though our investment in research and development has not been as intense during the current fiscal year, the new product introductions have not diminished thus supporting our objective of bringing new, state of the art products to market to enhance growth.

In April 2008, Dynatronics introduced the DynaPro Spinal Health System, a non-surgical treatment for back and neck pain. This innovative system combines the benefits of decompression and light therapy with core-stabilization exercises and nutrition forming a very effective tool for reducing pain.

Decompression therapy has been shown effective in relieving pain associated with a host of back problems including herniated discs, degenerative disc disease, sciatica and pinched nerves. In addition to offering the most comprehensive approach to the effective treatment of many of the most common causes of back and neck pain, the DynaPro Spinal Health System features the company's Dynatron DX2, T4 treatment table and other packaged accessories incorporating a state-of-the-art marketing and patient-awareness program to help practitioners promote this proven, non-surgical pain relief treatment.

Another new product introduced in April 2008 is the new Dynatron X5 "Turbo" soft-tissue oscillation therapy unit. The new X5 "Turbo" is three times more

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

powerful than the original X5 device and is a highly effective treatment for various orthopedic and sports injuries, and is gaining popularity in sports medicine.

Also introduced in April 2008 is the new "Synergie Elite" product line. The new "Synergie Elite" line of aesthetic treatment devices is comprised of cellulite treatment devices, microdermabrasion units and bio-stimulation light therapy equipment. These new products represent the first major redesign of the Synergie AMS cellulite reduction device and MDA microdermabrasion device since their introduction almost a decade ago. Initial response to the new Synergie Elite equipment at trade shows has been promising. The new updated design and additional features make the Synergie Elite products not only visually attractive, but functionally enhanced positioning us to better compete in the aesthetic markets. By including proven treatment procedures that have made Synergie aesthetic devices the most effective with the new design this line continues to be the best value on the market. In addition, we plan to develop and introduce additional products for the aesthetic market. Strategic partnerships, both domestic and international, are currently under consideration that would help maintain the sales momentum that is being initiated by the introduction of this revised product line.

With all these products being introduced in April 2008, we expect to receive revenue from sales of the new products during the fiscal fourth quarter ending June 30, 2008.

Since the acquisitions were completed in July 2007, Dynatronics has consolidated operations from eight distribution points to three facilities: our existing facilities in Tennessee and Utah as well as a new facility established in California that was formerly associated with Rajala Therapy Sales Associates, one of the acquired companies. The ability to timely service west coast customers was deemed a critical point of service and warranted the continuance of the Rajala operations. We believe that other areas of the country can be adequately served from these three warehouse operations.

With the assimilation of the six acquisitions now substantially completed, management has taken measures designed to reduce expenses by an estimated \$1.9 million annually. These cost savings are expected to be achieved primarily by a reduction of approximately 20 percent of the Company's workforce and the elimination of duplicative overhead expense. Many of these reductions had been contemplated as part of the successful assimilation of the acquired distributors; however, implementation of the planned reductions took longer to realize than expected. The implementation of these cost reductions and further refinements that should be achieved over the coming months are expected to contribute significantly to our profitability objectives in the coming quarters.

In addition to reducing operating costs through better assimilation of the acquired dealers, sales strategies are being implemented to capitalize on our new direct sales force. While we continue to look for opportunities to add to our direct sales force, we also are working with strong, independent dealers who are well established in their territories. The combination of strong dealers and a direct sales force will allow us to continue to expand our sales network. In support of that effort, we plan to introduce the most comprehensive product catalog in the Company's history in September 2008. We expect that the expanded catalog and new sales initiatives will provide additional impetus to sales. In addition, we are currently negotiating strategic partnerships that we expect will give us greater access to segments of the market not previously pursued by Dynatronics.

We have long believed that international sales present an untapped potential for growth and expansion, particularly given the current exchange rates which favor foreign currencies over the dollar. Adding new distributors in several countries will be the key to this expansion effort. Our past efforts to improve

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

international marketing have yielded only marginal improvements. We remain committed, however, to finding the most cost effective ways to expand our markets internationally. Our Salt Lake City facilities, where all electrotherapy, ultrasound, traction, STS devices, light therapy and Synergie products are manufactured, are certified to ISO 13485, an internationally recognized standard of excellence in medical device manufacturing. This designation is an important requirement in obtaining the CE Mark certification, which allows us to market our products in the European Union and other foreign countries.

Fiscal year 2008 thus far has been a year of transformation. Dynatronics has changed its business model from being primarily a manufacturer of products distributed through a network of independent dealers to a manufacturer and

15

distributor of products through primarily a direct sales force as well as key independent dealers. This change in our business model comes in response to the changes occurring in our industry. Consolidation efforts have resulted in a much more competitive environment. These consolidation efforts are occurring in both manufacturing and distribution. The consolidation in manufacturing is being led by DJO, Inc. (formerly Re-able or Encore Medical). Over the past few years DJO, Inc. has acquired such companies as Chattanooga Group, Saunders, Iomed, Empi, and Rehabilicare. In addition it has acquired distributors, including Performance Modalities and Endeavor Medical. The consolidation in distribution is being led primarily by Patterson Medical. During the same period of time, Patterson Medical has acquired distributors including Sammons-Preston, Theraquip, Dale Surgical, W.S. Medical and Goldsmith Medical. These consolidation efforts have created both challenges and opportunities for Dynatronics.

In order to strategically protect distribution channels, Dynatronics acquired the six independent distributors previously discussed. Since that time, Dynatronics has continued to add direct sales personnel as well as strengthen relationships with key independent distributors. We believe that through these direct sales reps and independent distributor relationships, we have the premier distribution network of seasoned and trained equipment sales personnel in the industry. The consolidation efforts in manufacturing by DJO and in distribution by Patterson are having a polarizing effect and compelling independent distributors and sales reps to choose an affiliation. We believe many of the best of these have become affiliated with Dynatronics because of our innovative quality products and proven history of strong customer service and loyalty to our distribution network. The quality of our products, the breadth of our product line, and the strength of our distribution channel we believe enable us to effectively compete in servicing our core market of private clinical practitioners and professional, collegiate, and other athletic teams.

As a manufacturer of many of the products we sell, we also have the ability to be competitive in our pricing schemes - particularly when compared to large consolidated or independent distributors.

Dynatronics' management acknowledges that the transition in our business model has taken longer than anticipated and the losses incurred have been higher than expected. Sales during the quarter ended March 31, 2008, did not meet our expectations. Nevertheless, the strategic decisions to change our business model were mandated by our desire to be responsive to the consolidations occurring within our industry. While it has been a more expensive proposition than originally projected, we believe the worst is behind us. With the reduction in expenses already implemented, the new products recently introduced, the sales tools anticipated for introduction in the next two quarters, including the new

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

catalog, and ongoing efforts to further streamline operations, we believe our goal of returning to profitability is achievable in the coming quarters.

Based on our defined strategic initiatives, we are focusing our resources in the following areas:

- o Reinforcing our position in the physical medicine market by securing channels of distribution through a strategy of acquiring dealers, recruiting direct sales representatives and working closely with the most successful dealers of capital equipment.
- o Improving sales by focusing on development of new sales strategies and promotional programs including the introduction of the most comprehensive catalog in our history.
- o Continuing development of new, state-of-the-art products, both high tech and commodity, in fiscal year 2008, for both the rehabilitation and aesthetic markets.
- o Further improving efficiencies in conjunction with the assimilation of the companies acquired.
- o Improving distribution of aesthetic products domestically and exploring the opportunities to introduce more products into the aesthetics market.
- o Expanding distribution of both rehabilitation and aesthetic products internationally.
- o Exploring strategic business alliances that will leverage and complement the Company's competitive strengths.
- o Exploring strategic relationships that would increase market reach and capital resources.

16

### Cautionary Statement Concerning Forward-Looking Statements

-----

The statements contained in this report on Form 10-QSB, particularly the foregoing discussion in Part I Item 2, Management's Discussion and Analysis or Plan of Operation, that are not purely historical, are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These statements refer to our expectations, hopes, beliefs, anticipations, commitments, intentions and strategies regarding the future. They may be identified by the use of the words or phrases "believes," "expects," "anticipates," "should," "plans," "estimates," "intends," and "potential," among others. Forward-looking statements include, but are not limited to, statements contained in Management's Discussion and Analysis or Plan of Operation regarding product development, market acceptance, financial performance, revenue and expense levels in the future and the sufficiency of its existing assets to fund future operations and capital spending needs. Actual results could differ materially from the anticipated results or other expectations expressed in such forward-looking statements for the reasons detailed in our Annual Report on Form 10-KSB under the headings "Description of Business" and "Risk Factors." The fact that some of the risk factors may be the same or similar to past reports filed with the SEC means only that the risks are present in multiple periods. We believe that many of the

## Edgar Filing: DYNATRONICS CORP - Form 10QSB

risks detailed here and in our other SEC filings are part of doing business in the industry in which we operate and compete and will likely be present in all periods reported. The fact that certain risks are endemic to the industry does not lessen their significance.

The forward-looking statements contained in this report are made as of the date of this report and we assume no obligation to update them or to update the reasons why actual results could differ from those projected in such forward-looking statements. Among others, risks and uncertainties that may affect the business, financial condition, performance, development, and results of operations include:

- o Assimilating acquired companies in a timely and effective manner including specific risks of:
  - o Failure to realize expected economies of scale and efficiencies of operations
  - o Inability to achieve sales targets
  - o Loss of key sales personnel
  - o Inefficiencies in management of receivables
  - o Lack of controlling inventories and consolidation of inventories
  - o Operational inefficiencies resulting in unmet customer expectations
- o market acceptance of our technologies, particularly our core therapy devices, Synergie AMS/MDA product line, and the Solaris infrared light therapy products;
- o lack of available financing through lines of credit or other financing sources to fully fund operating losses, expansion in working capital, and necessary capital expenditures to support the planned strategic initiatives.
- o failure to timely release new products against market expectations;
- o the ability to hire and retain the services of trained personnel at cost-effective rates;
- o rigorous government scrutiny or the possibility of additional government regulation of the industry in which we market our products;
- o reliance on key management personnel;
- o foreign government regulation of our products and manufacturing practices that may bar or significantly increase the expense of expanding to foreign markets;
- o economic and political risks related to expansion into international markets;
- o failure to sustain or manage growth, including the failure to continue to develop new products or to meet demand for existing products;
- o reliance on information technology;
- o the timing and extent of research and development expenses;
- o the ability to keep pace with technological advances, which can



## Edgar Filing: DYNATRONICS CORP - Form 10QSB

occur rapidly;

17

- o the loss of product market share to competitors;
- o potential adverse effect of taxation;
- o additional terrorist attacks on U.S. interests and businesses;
- o escalating costs of raw materials, particularly steel and petroleum based materials; and
- o increased competition from a consolidating market that could put pressure on pricing and margin realization.

As a public company, we are subject to the reporting requirements of the Exchange Act and the Sarbanes-Oxley Act of 2002. These requirements may place a strain on our systems and resources. The Exchange Act requires, among other things, that we file annual, quarterly and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires, among other things, that we maintain effective disclosure controls and procedures and internal controls over financial reporting. We are currently reviewing and further documenting our internal control procedures. However, the guidelines for the evaluation and attestation of internal control systems for small companies continue to evolve. Therefore, we can give no assurances that our systems will satisfy the new regulatory requirements. In addition, in order to maintain and improve the effectiveness of our disclosure controls and procedures and internal controls over financial reporting, significant resources and management oversight will be required.

### Item 3. Controls and Procedures

Based on evaluation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Exchange Act), as of the end of the period covered by this Report, our principal executive and principal financial officers have concluded that our disclosure controls and procedures are effective at the reasonable assurance level. There were no changes in our internal control over financial reporting that occurred during the quarter ended March 31, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Repurchases of Equity Securities. The following table summarizes purchases of Dynatronics common stock made by the Company during the quarter ended March 31, 2008, under a stock repurchase program approved by the board of directors of the Company in September 2003.

#### Small Business Issuer Purchases of Equity Securities\*

Period	Total # of Shares Purchased	Average Price Paid per Share	Total # of Shares Purchased as part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet be Purchased Under Plan/Program
--------	-----------------------------------	---------------------------------	---	---

Edgar Filing: DYNATRONICS CORP - Form 10QSB

1/1/08 to 1/31/08	39,000	\$1.04	39,000	\$201,756
2/1/08 to 2/29/08	35,014	\$1.07	35,014	\$164,336
3/1/08 to 3/31/08	18,500	\$1.05	18,500	\$144,950

\* The Company's repurchase program was announced on September 3, 2003. At that time, the Company approved repurchases aggregating \$500,000. In November 2007, the Company added an additional \$250,000 to the repurchase plan.

18

Item 6. Exhibits

(a) Exhibits

- 
- 3.1 Articles of Incorporation and Bylaws of Dynatronics Laser Corporation. Incorporated by reference to a Registration Statement on Form S-1 (No. 2-85045) filed with the SEC and effective November 2, 1984
  - 3.2 Articles of Amendment dated November 21, 1988 (previously filed)
  - 3.3 Articles of Amendment dated November 18, 1993 (previously filed)
  - 10.1 Employment contract with Kelvyn H. Cullimore, Jr. (previously filed)
  - 10.2 Employment contract with Larry K. Beardall (previously filed)
  - 10.3 Loan Agreement with Zions Bank (previously filed)
  - 10.5 Amended Loan Agreement with Zions Bank (previously filed)
  - 10.6 1992 Amended and Restated Stock Option Plan (previously filed)
  - 10.7 Dynatronics Corporation 2006 Equity Incentive Award Plan (previously filed as Annex A to the Company's Definitive Proxy Statement on Schedule 14A filed on October 27, 2006)
  - 10.8 Form of Option Agreement for the 2006 Equity Incentive Plan for incentive stock options (previously filed as Exhibit 10.8 to the Company's Annual Report on Form 10-KSB for the fiscal year ended June 30, 2006)
  - 10.9 Form of Option Agreement for the 2006 Equity Incentive Plan for non-qualified options (previously filed as Exhibit 10.9 to the Company's Annual Report on Form 10-KSB for the fiscal year

Edgar Filing: DYNATRONICS CORP - Form 10QSB

ended June 30, 2006)

- 11 Computation of Net Income per Share (included in Notes to Consolidated Financial Statements)
- 31.1 Certification under Rule 13a-14(a)/15d-14(a) of principal executive officer (filed herewith)
- 31.2 Certification under Rule 13a-14(a)/15d-14(a) of principal financial officer (filed herewith)
- 32 Certifications under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. SECTION 1350) (filed herewith)

19

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

DYNATRONICS CORPORATION  
Registrant

Date 5/13/08 /s/ Kelvyn H. Cullimore, Jr.  
-----  
Kelvyn H. Cullimore, Jr.  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)

Date 5/13/08 /s/ Terry M. Atkinson, CPA  
-----  
Terry M. Atkinson, CPA  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

20

-----