DYNATRONICS CORP
Form 10QSB
November 14, 2005

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

FORM 10-QSB

(Mark One)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2005.

[ ] 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)

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 ___

The number of shares outstanding of the issuer's common stock, no par value, as of November 9, 2005 is 9,020,339.

Transitional Small Business Disclosure Format (Check one): Yes __ No X

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DYNATRONICS CORPORATION
Balance Sheets

Assets		September 30, 2005 (Unaudited)
Current assets:		
Cash	$	411,066
Trade accounts receivable, less allowance for doubtful accounts of $250,101 at September 30, 2005 and $252,509 at June 30, 2005		3,177,811
Other receivables		99,663
Inventories, net		4,575,441
Prepaid expenses		573,337
Prepaid income taxes		36,674
Deferred tax asset-current		384,077
Total current assets		9,258,069
Property and equipment, net		3,163,196
Goodwill, net of accumulated amortization of $649,792 at September 30, 2005 and at June 30, 2005		789,422
Other assets		353,293
	$	13,563,980

Liabilities and Stockholders' Equity

Current liabilities:	
Current installments of long-term debt	$ 224,453
Line of credit	868,755
Accounts payable	498,435
Accrued expenses	483,538
Accrued payroll and benefit expenses	126,495
Total current liabilities	2,201,676
Long-term debt, excluding current installments	1,274,051
Deferred compensation	367,451
Deferred tax liability - noncurrent	223,647
Total liabilities	4,066,825
Stockholders' equity:	
Common stock, no par value. Authorized 50,000,000 shares; issued 9,020,339 shares at September 30, 2005 and 9,015,128 shares at June 30, 2005	2,784,968
Retained earnings	6,712,187
Total stockholders' equity	9,497,155
	$ 13,563,980

See accompanying notes to financial statements.

DYNATRONICS CORPORATION
Condensed Statements Of Operations
(Unaudited)

	Three Months Ended September 30	
	2005	2004
Net sales	$ 4,358,428	$ 4,918,884
Cost of sales	2,769,844	2,907,405
Gross profit	1,588,584	2,011,479
Selling, general, and administrative expenses	1,243,125	1,487,314
Research and development expenses	413,605	253,792
Operating income (loss)	(68,146)	270,373

Other income (expense):		
Interest income	2,791	976
Interest expense	(30,189)	(35,789
Other income, net	59,250	7,283
Total other income (expense)	31,852	(27,530
Income (Loss) before income taxes	(36,294)	242,843
Income tax expense	(13,973)	93,495
Net income (loss)	$ (22,321)	$ 149,348
Basic and diluted net income (loss) per common share	$ (0.00)	$ 0.02
Weighted average basic and diluted common shares outstanding (note 2)		
Basic	9,017,771	8,957,876
Diluted	9,017,771	9,181,387

See accompanying notes to condensed financial statements.

DYNATRONICS CORPORATION
Statements of Cash Flows
(Unaudited)

	Three Months September 2005	
Cash flows from operating activities:		
Net income (loss)	$ (22,321)	$
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	84,544	
Other amortization	1,831	
Provision for doubtful accounts	12,000	
Provision for inventory obsolescence	63,000	
Provision for warranty reserve	59,451	
Provision for deferred compensation	6,933	
Change in operating assets and liabilities:		
Receivables	(192,030)	
Inventories	74,082	
Prepaid expenses and other assets	(168,748)	
Income tax receivable	(14,973)	
Accounts payable and accrued expenses	(496,878)	

Net cash (used in) provided by operating activities		(593,109)
Cash flows from investing activities:		
Capital expenditures		(27,296)
Proceeds from sale of assets		1,500
Net cash used in investing activities		(25,796)
Cash flows from financing activities:		
Principal payments on long-term debt		(52,890)
Net change in line of credit		603,994
Proceeds from issuance of common stock		5,968
Net cash provided by (used in) financing activities		557,072
Net change in cash		(61,833)
Cash at beginning of year		472,899
Cash at end of year	$	411,066 $
Supplemental disclosures of cash flow information:		
Cash paid for interest	$	27,516 $
Cash paid for income taxes	$	1,000 $

See accompanying notes to financial statements.

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DYNATRONICS CORPORATION
NOTES TO CONDENSED FINANCIAL STATEMENTS
September 30, 2005
(Unaudited)

NOTE 1. PRESENTATION

The financial statements as of September 30, 2005 (unaudited) were prepared by the Company 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, 2005 and 2004. 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 10-KSB filing.

NOTE 2. NET INCOME (LOSS) PER COMMON SHARE

Net income 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 EPS does not assume exercise or conversion of securities that would have an anti-dilutive effect.

Basic net income per common share is the amount of net income for the period available to each share of common stock outstanding during the reporting period. Diluted net income per common share is the amount of net income for the period available to each share of common stock outstanding during the reporting period and to each share that would have been outstanding assuming the issuance of common shares for all dilutive potential common shares outstanding during the period.

In calculating net income per common share, the net income was the same for both the basic and diluted calculation for the three months ended September 30, 2004. Stock options exercisable of 204,812 at September 30, 2005 were not included in the calculation of diluted net loss per share because their effect was anti-dilutive. A reconciliation between the basic and diluted weighted-average number of common shares for the three months ended September 30, 2005 and 2004 is summarized as follows:

	(Unaudited) Three Months Ended September 30, 2005	2004
Basic weighted average number of common shares outstanding during the period	9,017,771	8,957,876
Weighted average number of dilutive common stock options outstanding during the period	-	223,511
Diluted weighted average number of common and common equivalent shares outstanding during the period	9,017,771	9,181,387

NOTE 3. EMPLOYEE STOCK COMPENSATION

The Company employs the footnote disclosure provisions of Statement of Financial Accounting Standard (" SFAS") No. 123, Accounting for Stock-Based Compensation, as amended by SFAS No. 148, Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of SFAS Statement No. 123. SFAS No. 123 encourages entities to adopt a fair-value-based method of accounting for stock options or similar equity instruments. However, it also allows an entity to continue measuring compensation cost for stock-based compensation using the

intrinsic-value method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees (APB 25). The Company has elected to apply the provisions of APB 25; accordingly, no compensation expense has been recognized for the stock option plan. Had compensation expense for the Company's stock option plan been determined based on the fair value at the grant date for awards consistent with the provisions of SFAS No. 123, the Company's results of operations would have been reduced to the pro forma amounts indicated below:

	Three months ended September 30, 2005	Three months ended September 30, 2004
Net income (loss) as reported	$ (22,321)	$ 149,348
Less: pro forma adjustment for stock based Compensation, net of income tax	(173,562)	(8,752)
Pro forma net income (loss)	$ (195,883)	$ 140,596
Basic net income (loss) per share:		
As reported	$ -	$ 0.02
Effect of pro forma adjustment	(0.02)	-
Pro forma	$ (0.02)	$ 0.02
Diluted net income (loss) per share:		
As reported	$ -	$ 0.02
Effect of pro forma adjustment	(0.02)	-
Pro forma	$ (0.02)	$ 0.02

The per share weighted-average fair value of stock options granted for the three months ended September 30, 2005 and 2004 was $1.40 and $1.29 per share, respectively, on the date of grant using the Black-Scholes option pricing model with the following weighted-average assumptions:

	Three months ended September 30, 2005	Three months ended September 30, 2004
Expected dividend yield	0%	0%
Risk-free interest rate	4.14 - 4.20%	3.66 - 3.68%
Expected volatility	87 - 88%	87 - 88%
Expected life	5 & 7 years	5 & 7 years

NOTE 4. COMPREHENSIVE INCOME

For the periods ended September 30, 2005 and 2004, comprehensive income was equal to the net income (loss) as presented in the accompanying condensed statements of operations.

NOTE 5. INVENTORIES

Inventories consisted of the following:

	September 30, 2005	June 30, 2005
Raw Material	$ 2,626,849	2,671,255
Finished Goods	2,373,299	2,409,435
Inventory Reserve	(424,707)	(368,167)
	$ 4,575,441	4,712,523

NOTE 6. PROPERTY AND EQUIPMENT

Property and equipment were as follows:

	September 30, 2005	June 30, 2005
Land	$ 354,744	$ 354,743
Buildings	2,921,127	2,921,127
Machinery and equipment	1,570,817	1,560,010
Office equipment	1,026,089	1,011,101
Vehicles	94,290	94,290
	5,967,067	5,941,271
Less accumulated depreciation and amortization	2,803,871	2,719,327
	$ 3,163,196	$ 3,221,944

NOTE 7. GOODWILL AND INTANGIBLE ASSETS

Goodwill represents the excess of costs over fair value of assets of businesses acquired. The Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 142, Goodwill and Other Intangible Assets, as of July 1, 2002. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of SFAS No. 142. Management is primarily responsible for the SFAS No. 142 valuation determination. In compliance with SFAS No. 142, management utilizes 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, the fair value of the Company exceeded the book value of the Company. Therefore, there was not an indication of impairment upon adoption of SFAS No. 142. Management performed its annual impairment assessment during the Company's fourth quarter ending June 30, 2004 and determined there was not an indication of impairment. SFAS No. 142 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with SFAS No. 144, Accounting for Impairment or Disposal of Long-Lived Assets.

Goodwill. As of September 30, 2005, the Company had goodwill, net, of $789,422 from the acquisition of Superior Orthopaedic Supplies, Inc on May 1, 1996 and the exchange of Dynatronics Laser Corporation common stock for a minority interest in Dynatronics Marketing Corporation on June 30, 1983. Through June 30,

2002, goodwill from these transactions was amortized over a period of 15 and 30 years, respectively, on a straight-line basis.

License Agreement. Identifiable intangible assets consist of a license agreement entered into on August 16, 2000 for a certain concept and process relating to a patent. The license agreement is being amortized over ten years on a straight-line basis. The following table sets forth the gross carrying amount, accumulated amortization and net carrying amount of the license agreement:

	As of September 30, 2005	As of June 30, 2005
Gross carrying amount	$ 73,240	$ 73,240
Accumulated amortization	37,231	35,400
Net carrying amount	$ 36,009	$ 37,840

Amortization expense associated with the license agreement was $1,831 for both the three months ended September 30, 2005 and 2004. Estimated amortization expense for the existing license agreement is expected to be $7,324 for each of the fiscal years ending June 30, 2006 through June 30, 2010. The license agreement is included in other assets.

NOTE 8. PRODUCT WARRANTY RESERVE

The Company adopted the provisions of FASB Interpretation No. 45, Guarantors' Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, as of December 31, 2002. The Company accrues the estimated costs to be incurred in connection with its product warranty programs as products are sold based on historical warranty rates. The product warranty reserve is included in accrued expenses at September 30, 2005 and June 30, 2005. A reconciliation of the changes in the warranty liability is as follows:

	Three months ended September 30, 2005	Three months ended September 30, 2004
Beginning product warranty reserve balance	$ 208,000	$ 184,000
Warranty repairs	(59,451)	(29,472)
Warranties issued	31,041	51,153
Changes in estimated warranty costs	28,410	(15,681)
Ending product warranty liability balance	$ 208,000	$ 190,000

NOTE 9. COMMON STOCK.

The Company received proceeds of $5,968 during the three months ended September 30, 2005 for 5,211 shares of common stock that were issued upon the exercise of options by employees. During the three months ended September 30, 2004 the Company received proceeds of $2,633 for 2,250 shares of common stock that were issued upon the exercise of options by employees

NOTE 10. RECENT ACCOUNTING PRONOUNCEMENTS

On December 16, 2004, the Financial Accounting Standards Board ("FASB") published Statement of Financial Accounting Standards No. 123 (Revised 2004), Share Based Payment ("SFAS 123R"). SFAS 123R requires that compensation cost related to share-based payment transactions be recognized in the financial statements. Share-based payment transactions within the scope of SFAS 123R include stock options, restricted stock plans, performance-based awards, stock appreciation rights, and employee share purchase plans. The provisions of SFAS 123R are effective as of the first interim period that begins after December 15, 2005. Accordingly, the Company will implement the revised standard in the third quarter of fiscal year 2006. Currently, the Company accounts for its share-based payment transactions under the provisions of APB 25, which does not necessarily require the recognition of compensation cost in the financial statements. Management is assessing the implications of this revised standard and the effect of the adoption of SFAS 123R will have on our financial position, results of operations, or cash flow.

In March 2005, the Financial Accounting Standard Board ("FASB") issued FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" an interpretation of FASB No. 143 ("FIN No. 47"). FIN No. 47 addresses the obligation of a business enterprises to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. An entity is required to recognize a liability for the fair value of a conditional asset retirement obligation if the fair value of the liability can be reasonably estimated. The Company evaluated the criteria of this pronouncement and concluded that it has no conditional asset retirement obligation, and therefore the adoption of FIN No. 47 had no impact on the Company's financial statements.

In May 2005, the Financial Accounting Standard Board ("FASB") issued SFAS No. 154, "Accounting Changes and Error Corrections-a replacement of APB Opinion No. 20 and FASB Statement No. 3". This Statement requires retrospective application to prior periods' financial statements of changes in accounting principle, unless it is impracticable to determine the period-specific effects or the cumulative effect of the change. This pronouncement will be effective December 15, 2005. Currently, the Company does not have changes in accounting principle, the adoption of SFAS No. 154 will not have impact on the Company's financial position or results of operations.

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 elsewhere in this report on Form 10-QSB.

Results of Operations

The Company's fiscal year ends on June 30th. This report covers the first quarter ended September 30, 2005, for the Company's fiscal year ending June 30, 2006.

Net Sales

During the quarter ended September 30, 2005, the Company generated sales of $4,358,428, compared to $4,918,884 in the quarter ended September 30, 2004. The 11.4% decrease in revenue in this first quarter of fiscal 2006 compared to the same quarter last year is a direct result of delays in the release of previously announced new products. Dealers postponed purchases of existing Solaris and 50 Series combination devices anticipating the introduction of the new Dynatron Xp Light Pad, Dynatron X3 Light Therapy device and the Dynatron DX2 combination traction and light therapy device, as well as two new Solaris light therapy probes and proprietary treatment tables. Lower device sales during the quarter ended September 30, 2005 were partially offset by increased sales of the Company's wood and metal treatment tables during the reporting period.

The Dynatron Xp Light Pad was released in late October 2005 and release of the Dynatron X3 and DX1 are now anticipated in the third quarter of fiscal 2006.

Gross Profit

During the quarter ended September 30, 2005, total gross profit was $1,588,584, or 36.4% of net sales, compared to $2,011,479, or 40.9% of net sales, in the quarter ended September 30, 2004. This 4.5 percentage point decrease was primarily attributable to the reduced sales of above average margin products. The Company generated lower sales of therapy and aesthetic devices which carry above average margins while slightly increasing sales of below-average margin treatment tables during the reporting quarter. Another contributing factor was the update of labor and overhead cost allocations to cost of goods sold implemented during the quarter ended June 30, 2005. This adjustment allocated more SG&A costs to Cost of Goods Sold to more accurately reflect actual cost of manufacturing each product. The quarter ended September 30, 2005 was the first full quarter to reflect this change. The increase in Cost of Goods Sold attributable to this adjustment was offset by lower SG&A expenses.

Selling, general and administrative expenses

Selling, general and administrative (SG&A) expenses for the quarter ended September 30, 2005 were $1,243,125, or 28.5% of net sales, compared to $1,487,314, or 30.2% of net sales, in the prior year period. Total SG&A expenses in the 2005 quarter decreased by $244,189 or 16.4% compared to the similar quarter in 2004. The three primary components affecting SG&A expenses in the first quarter ended September 30, 2005 compared to 2004 were:

- Approximately $81,000 in lower labor expenses which is partly related to the reallocation of costs to cost of goods sold as explained above.
- Approximately $93,000 in decreased selling expenses including tradeshow activities, sales commissions, dealer incentive programs and advertising.
- Approximately $68,000 in lower incentive compensation expenses.

Research and Development

The Company has expanded its R&D capabilities by increasing its staff of engineers in order to develop new products at a more rapid pace. A record number of new products are currently under development. The first of these new products began shipping in October 2005. While this effort has increased short term costs, we believe it will also position the Company to generate future growth in both sales and profitability. R&D expenses during the quarter ended September 30, 2005 increased approximately $160,000 to $413,605, compared to $253,792 in the prior year period. R&D expenses represented approximately 9.5% and 5.2% of the net sales of the Company in the 2005 and 2004 quarterly periods,

respectively. R&D costs are expensed as incurred.

Pre-tax profit

Pre-tax loss for the quarter ended September 30, 2005 was $36,294 compared to pre-tax profit of $242,843 in the quarter ended September 30, 2004. Lower sales and margins generated during the reporting quarter, combined with higher R&D costs, account for the difference between the comparative periods.

Income Tax

Income tax benefit for the quarter ended September 30, 2005 was $13,973 compared to income tax expense of $93,495 in the quarter ended September 30, 2004. The effective tax rate for the quarters ended September 30, 2005 and September 30, 2004 was 38.5%.

Net Income

Net loss for the quarter ended September 30, 2005 was $22,321 (approximately $.00 per share), compared to net income of $149,348 (approximately $.02 per share) in the quarter ended September 30, 2004. The lower sales and margins generated during the reporting quarter, combined with higher R&D expenses, led to the reduction in net income compared to the prior year period.

Liquidity and Capital Resources

The Company has financed its operations through cash reserves, available borrowings under its line of credit, and from cash provided by operations. The Company had working capital of $7,056,393 at September 30, 2005, inclusive of the current portion of long-term obligations and credit facilities, as compared to working capital of $7,043,854 at June 30, 2005.

Accounts Receivable

Trade accounts receivable, net of allowance for doubtful accounts, increased $171,496 to $3,177,811 at September 30, 2005 compared to $3,006,315 at June 30, 2005. Management anticipates accounts receivable could increase in future periods due to the planned introduction of eight new products in fiscal year 2006 which are expected to increase sales.

Trade accounts receivable represent amounts due from the Company's dealer network and 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. Accounts receivable are generally collected within 30 days of the agreed terms.

Inventories

Inventories, net of reserves, at September 30, 2005 decreased $137,082 to $4,575,441 compared to $4,712,523 at June 30, 2005. Management expects that inventories will likely increase during the current fiscal year based on the Company's planned new product introductions.

Prepaid Expenses

Prepaid expenses increased $186,402 to $573,337 at September 30, 2005 compared

to $386,935 at June 30, 2005, due primarily to increases in advances made to suppliers for various component parts.

Goodwill

Goodwill at September 30, 2005 and June 30, 2005 was $789,422. Beginning July 1, 2002, the Company adopted the provisions of SFAS No. 142 Goodwill and other Intangible Assets. In compliance with SFAS 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, 2005, the fair value of the Company exceeded the book value of the Company. Therefore, there was no indication of impairment upon adoption of SFAS No. 142 or at June 30, 2005. Management is primarily responsible for the FAS 142 valuation determination and performed the annual impairment assessment during the Company's fourth quarter.

Accounts Payable

Accounts payable decreased by $107,353 to $498,435 at September 30, 2005 compared to $605,788 at June 30, 2005. The decrease in accounts payable is a result of the timing of our weekly payments to suppliers and the timing of purchases of product components. All accounts payable are within term. We continue to take advantage of available early payment discounts when offered.

Accrued Expenses

Accrued expenses decreased by $88,402 to $483,538 at September 30, 2005 compared to $571,940 at June 30, 2005. Accrued expenses at June 30, 2005 were higher due to the timing of our June 2005 national dealer meeting and accrued expenses for sales incentive programs.

Accrued Payroll & Benefit Expenses

Accrued payroll & benefit expenses decreased by $241,672 to $126,495 at September 30, 2005 compared to $368,167 at June 30, 2005. The decrease in accrued payroll & benefit expenses is related to lower accrued payroll and bonuses for employees, officers, and directors and corresponding payroll taxes.

Cash

The Company's cash position was $411,066 at September 30, 2005 compared to $472,899 at June 30, 2005. The Company believes that its current cash balances, amounts available under its line of credit and cash provided by operations will be sufficient to cover its 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

The Company maintains a revolving line of credit with a commercial bank in the amount of $4,500,000. The outstanding balance on our line of credit was $868,755 at September 30, 2005 compared to $264,761 at June 30, 2005. The $603,994 increase in the outstanding balance of the line of credit was attributable primarily to the payment of accounts payable and accrued expenses during the reporting quarter. Interest on the line of credit is based on the bank's prime

rate, which at September 30, 2005, equaled 6.75%. The line of credit is collateralized by accounts receivable and inventories. Borrowing limitations are based on 30% of eligible inventory and up to 80% of eligible accounts receivable. The line of credit is renewable annually on December 1st and includes covenants requiring the Company to maintain certain financial ratios. As of September 30, 2005, the Company was in compliance with all loan covenants.

The current ratio was 4.2 to 1 at September 30, 2005 compared to 4.5 to 1 at June 30, 2005. Current assets represent 68% of total assets at September 30, 2005.

Debt

Long-term debt excluding current installments totaled $1,274,051 at September 30, 2005 compared to $1,330,325 at June 30, 2005. 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 $1.5 million with monthly principal and interest payments of $21,370.

Stock Repurchase Program

On September 3, 2003, the Company announced a stock repurchase program. The Board of Directors authorized the expenditure of up to $500,000 to purchase the Company's common stock on the open market pursuant to regulatory restrictions governing such repurchases. During fiscal 2004, the Company purchased $89,000 of stock, leaving over $400,000 of authorized funds for future stock repurchases. The stock repurchase program is conducted pursuant to safe harbor regulations under Rule 10b-18 of the Exchange Act for the repurchase by an issuer of its own shares. No shares were repurchased during the quarter ended September 30, 2005.

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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 the understanding of our results of operations. The impact and risks related to these policies on our business operations are discussed in this Management's Discussion and Analysis where such policies affect our reported and expected financial results. For a detailed discussion of the application of these and other accounting policies, see Notes to the Audited Financial Statements contained in the Company's annual report on Form 10-KSB for the year ended June 30, 2005. 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, intangible assets, warranty obligations, product liability,

revenue, and income taxes. 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:

- Current inventory quantities on hand.
- Product acceptance in the marketplace.
- Customer demand.
- Historical sales.
- Forecast sales.
- Product obsolescence.
- Technological innovations.

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 September 30, 2005 and June 30, 2005, our inventory valuation reserve balance, which established a new cost basis, was $424,707 and $368,167, respectively, and our inventory balance was $4,575,441 and $4,712,523 net of reserves, respectively.

Revenue Recognition

Our products are sold primarily to customers who are independent distributors and equipment dealers. These distributors resell the products, typically to end users, including physical therapists, professional trainers, athletic trainers, chiropractors, medical doctors and aestheticians. 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 $3,177,811and $3,006,315, net of allowance for doubtful accounts of $250,101 and $252,509, at September 30, 2005 and June 30, 2005, respectively.

Business Plan and Outlook

Over the past seven years, annual net sales have grown from $12.6 million in fiscal year 1998 to $20.4 million in 2005. During fiscal year 2006, we will

continue to focus our efforts on fueling and sustaining growth through the development of new products for the rehabilitation and aesthetics markets while, at the same time, strengthening our channels of distribution and improving operating efficiencies.

The fruits of our focused R&D campaign begun in 2002 were initially manifest in September 2004 when we introduced the Solaris Series, a new product line of advanced technology electrotherapy/ultrasound products featuring an infrared light therapy probe. This new family of products has quickly become our top selling line, due largely to the popularity of light therapy. Light therapy is becoming widely recognized for its successful treatment of painful conditions.

In July 2005, we announced that we would be introducing eight new products over the coming months. The first of those products, the Dynatron Xp Infrared Light Pad and Dynatron XpB, or Booster Box, began shipping to customers in October 2005. The Dynatron Xp and XpB provide practitioners with a tool that allows unattended therapy of large segments of the body such as the back, thigh or shoulder.

The Dynatron XpB is an accessory that will allow the thousands of Solaris unit owners to add the new Xp Infrared Light Pad as an accessory to their existing Solaris device. This compatibility of technology not only opens a significant market segment for the new Xp Infrared Light Pad, but assures users of Dynatronics' products that we are working to make these technologies affordable for them.

In October 2005, we also began shipping the Dynatron iBox, a new transdermal drug delivery device for iontophoresis that we believe is the most technologically advanced product of its kind on the market. We intend to use this device to leverage sales of the iontophoresis electrodes we distribute.

In the third quarter of fiscal year 2006, we plan to begin shipping the Dynatron Solaris X3, a powerful unit offering multiple applications of light therapy. The original Solaris series devices offered light therapy as an added accessory to our popular combination electrotherapy/ultrasound technology. However, there has been increasing market demand for a stand-alone unit that expands light therapy capabilities. The X3 has been designed to provide the ability to operate two Xp Infrared Light Pads or two light therapy probes simultaneously.

The probes being offered with the X3 include not only the existing Dynatron 880 and 890 probes but also two new probes - one with a much higher output of infrared wavelength light and the other a combination infrared and blue wavelength output.

In the third quarter of fiscal year 2006, we also anticipate introducing the DX2 combination traction and light therapy device. We believe that combining the pain relieving characteristics of infrared light therapy as offered through our new Xp Light Pad, with the traditional benefits of decompression therapy through traction, will make our DX2 traction device one of the most unique devices of its kind on the market. It is designed to provide practitioners a more efficacious way to relieve pain using combination therapy. We anticipate this unique combination of modalities together with the benefits of touch screen technology will create significant demand for this product.

To support this product, we also plan to introduce a new traction therapy table, the Dynatron T4, which we expect to be one of the best value tables on the market for traction and decompression therapy. The T4 and DX2 will typically be sold together as a package.

The technological complexity of these new devices has delayed their introduction by 3-5 months. These delays are attributable to many factors including sourcing of critical parts & components, completing designs and operating software, and

complying fully with all internal quality processes for new product development and release. While the delays in release have diminished sales and profits for

the reporting quarter and will likely have a similar effect on the quarter ending December 31, 2005, demand for these products remain strong and we remain confident that once released these new products will be reliable and spark new growth in sales and profits during the last half of fiscal year 2006.

Another important part of our strategic plan is the further expansion of worldwide marketing efforts. Over the past two years, international sales have more than doubled and we continue to press forward seeking additional opportunities for international expansion. The Company's Salt Lake City operation, where all electrotherapy, ultrasound, STS devices, light therapy and Synergie products are manufactured, is 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.

We continue efforts to promote our line of aesthetic equipment which includes the Synergie AMS device for dermal massage, the Synergie MDA device for microdermabrasion, and the Synergie LT device, an infrared light therapy unit designed specifically for aesthetic applications. The introduction of the Synergie LT device is positioning Dynatronics to compete more fully in the spa and beauty market. We plan to develop and introduce additional light therapy probes for the aesthetic market using different wavelengths of light. Recent interest by medical spas in the use of other physical therapy modalities such as electrotherapy, ultrasound and light therapy in aesthetic applications has opened new potential for crossover of physical medicine modalities into the aesthetics market. This presents a unique opportunity for us to grow sales of new aesthetic products with little additional R&D effort since the products have already been developed for the physical medicine markets.

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

- Reinforcing our position in the physical medicine market through an aggressive research and development campaign that will result in the introduction of eight new products, both high tech and commodity, in fiscal year 2006.

- Increasing sales of Solaris devices through introduction of new light therapy accessories and by developing new markets for light therapy applications.

- Improving sales and distribution of rehabilitation products domestically through strengthened relationships with dealers, particularly the high-volume specialty dealers.

- Improving distribution of aesthetic products domestically and exploring the opportunities to introduce more light therapy devices and versions of our physical therapy modalities into the aesthetics market.

- Expanding distribution of both rehabilitation and aesthetic products internationally.

- Seeking strategic partnerships to further expand our presence in and market share of the physical rehabilitation and the aesthetics

markets.

Cautionary Statement Concerning Forward-Looking Statements

The statements contained in this report on Form 10-QSB, particularly the foregoing discussion in Part 1 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. 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 Securities and Exchange Commission means only that the risks are present in multiple periods. We believe that many of the 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:

- Market acceptance of our technologies, particularly our core therapy devices, Synergie AMS/MDA product line, and the Solaris infrared light therapy products;
- Failure to timely release new products against market expectations;
- The ability to hire and retain the services of trained personnel at cost-effective rates;
- Rigorous government scrutiny or the possibility of additional government regulation of the industry in which we market our products;
- Reliance on key management personnel;
- Foreign government regulation of our products and manufacturing practices that may bar or significantly increase the expense of expanding to foreign markets;
- Economic and political risks related to expansion into international markets;

- Failure to sustain or manage growth including the failure to continue to develop new products or to meet demand for existing products;
- Reliance on information technology;
- The timing and extent of research and development expenses;
- The ability to keep pace with technological advances, which can occur rapidly;
- The loss of product market share to competitors;
- Potential adverse effect of taxation;
- Additional terrorist attacks on U.S. interests and businesses;
- The ability to obtain required financing to meet changes or other risks; and
- Escalating costs of raw materials, particularly steel and petroleum based materials.
- As a public company, we are subject to the reporting requirements of the Securities Exchange Act of 1934 and the Sarbanes-Oxley Act of 2002. These requirements may place a strain on our systems and resources. The Securities 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 have only recently been finalized, and the evaluation and attestation processes are new and untested. 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 have been no significant changes in internal controls over financial reporting or in other factors that could significantly affect these controls subsequent to the date of their evaluation, including any corrective actions with regard to significant deficiencies or material weaknesses.

PART II. OTHER INFORMATION

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 Securities and Exchange Commission and effective November 2, 1984, as amended by Articles of Amendment dated November 18, 1993
3.2	Articles of Amendment dated November 21, 1988 (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 (December 2003)
10.6	1992 Amended and Restated Stock Option Plan (previously filed)
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	Certification under Section 906 of the Sarbanes-Oxley Act of 2002 (18 U.S.C. SECTION 1350) (filed herewith)

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 11/11/05 /s/ Kelvyn H. Cullimore, Jr.

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	Kelvyn H. Cullimore, Jr. Chairman, President and Chief Executive Officer (Duly Authorized Officer and Principal Executive Officer)
Date 11/11/05	/s/ Terry M. Atkinson, CPA
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	Terry M. Atkinson, CPA Chief Financial Officer (Principal Financial Officer)