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ALANCO TECHNOLOGIES INC  
Form 10KSB  
September 28, 2006

ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

FORM 10-KSB

Annual Report Pursuant to Section 13 or 15 (d) of  
The Securities Exchange Act of 1934  
For the fiscal year ended June 30, 2006  
Commission file number 0-9347

ALANCO TECHNOLOGIES, INC.  
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(Exact name of registrant as specified in its charter)

Arizona 86-0220694  
-----  
(State or other jurisdiction of (I.R.S. Employer  
Incorporation or organization) Identification No.)

15575 North 83rd Way, Suite 3, Scottsdale, AZ 85260  
-----  
(Address of principal executive offices) (Zip Code)

Registrant's Telephone Number: (480) 607-1010

Securities registered pursuant to Section 12(b) of the Act: None  
Securities registered pursuant to Section 12(g) of the Act

COMMON STOCK  
(Title of Class)

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  
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Check if disclosure of delinquent filers in response to Item 405 of  
Regulation S-B is not contained in this form, and no disclosure will be  
contained, to the best of registrant's knowledge, in definitive proxy or  
information statements incorporated by reference in Part III of this Form 10-KSB  
or any amendment to this Form 10-KSB.

Yes X No  
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The Registrant's revenues for the fiscal year ended June 30, 2006 were  
\$6,659,600.

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State the aggregate market value, based upon the closing bid price of the Common Stock as quoted on NASDAQ, of the voting stock held by non-affiliates of the registrant: \$18,006,500 as of September 22, 2006.

Indicate the number of shares outstanding of each of the registrant's classes of common stock: 38,163,700 shares of Class A Common Stock (net of treasury shares) and no shares of Class B Common Stock as of September 22, 2006.

### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Except for historical information, the statements contained herein are forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include statements concerning plans, objectives, goals, strategies, future events or performance, and underlying assumptions and other statements, which are other than statements of historical facts. From time to time, the Company may publish or otherwise make available forward-looking statements of this nature. All such forward-looking statements are based on the expectations of management when made and are subject to, and are qualified by, risks and uncertainties that could cause actual results to differ materially from those expressed or implied by those statements. These risks and uncertainties include, but are not limited to, the following factors, among others, that could affect the outcome of the Company's forward-looking statements: general economic and market conditions; reduced demand for information technology equipment; competitive pricing and difficulty managing product costs; development of new technologies which make the Company's products obsolete; rapid industry changes; failure by the Company's suppliers to meet quality or delivery requirements; the inability to attract, hire and retain key personnel; failure of an acquired business to further the Company's strategies; the difficulty of integrating an acquired business; undetected problems in the Company's products; the failure of the Company's intellectual property to be adequately protected; unforeseen litigation; unfavorable result of current pending litigation; the ability to maintain sufficient liquidity in order to support operations; the ability to maintain satisfactory relationships with lenders and to remain in compliance with financial loan covenants and other requirements under current banking agreements; the ability to maintain satisfactory relationships with suppliers; federal and/or state regulatory and legislative actions; customer preferences and spending patterns; the ability to implement or adjust to new technologies and the ability to secure and maintain key contracts and relationships.

#### PART 1

#### ITEM 1. BUSINESS

##### GENERAL DEVELOPMENT OF BUSINESS

Alanco Technologies, Inc. was incorporated in 1969 under the laws of the State of Arizona. Unless otherwise noted, the "Company" or "Alanco" refers to Alanco Technologies, Inc. and its wholly owned subsidiaries. Alanco (Nasdaq: ALAN) is a provider of advanced information technology solutions with the Company's operations for fiscal years ended June 30, 2006 and 2005 diversified into two reporting business segments including: (i) design, production, marketing and distribution of RFID (Radio Frequency Identification) tracking technology, and (ii) manufacturing, marketing and distribution of data storage products.

The Company acquired its RFID (Radio Frequency Identification) tracking technology known as the TSI PRISM system in May 2002 through the acquisition of the operations of Technology Systems International, Inc., a Nevada corporation

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("TSIN"). The Company continues to participate in the data storage market through two wholly-owned subsidiaries: Arraid, Inc., a manufacturer of proprietary storage products to upgrade older "legacy" computer systems; and Excel/Meridian Data, Inc., a manufacturer of Network Attached Storage ("NAS") systems and other storage related products for mid-range organizations.

The acquisition, effective June 30, 2006, of StarTrak Systems, LLC ("StarTrak"), located in Morris Plains, New Jersey, added Wireless Asset Management, a third reporting business segment described as a provider of wireless GPS tracking and monitoring services, which are offered on a monthly subscription basis to various industry segments. The company's primary focus is currently the refrigerated or "Reefer" segment of the transport industry, providing the dominant share of all wireless tracking, monitoring and control services to this market segment.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### RECENT BUSINESS DEVELOPMENTS

**New Product Announcement** - On September 7, 2006, the Company announced that StarTrak Systems, LLC, its wholly owned subsidiary, had commenced the initial commercial deployment of the new ReeferTrak(R) Scout RFID product line designed specifically for localized food distribution fleets, including fast food, dairy and grocery operations. Two Los Angeles-area food distributors have recently purchased and deployed the new ReeferTrak Scout units and base stations at their distribution centers.

ReeferTrak Scout is an RFID wireless communications system that gives users full two-way command and control capability of their refrigerated truck and trailer fleets when the units are within a several mile range of a base station-equipped distribution center. When the "reefers" are operating out of range of the distribution center, the Scout unit logs GPS, trip and refrigeration unit performance data and automatically downloads the information to StarTrak's central data center via the local base station upon return to the center. Customers use the data to immediately confirm temperature compliance of the shipment from origin to destination. The base stations' several mile RFID range provides excellent coverage of distribution facilities, allowing customers to achieve significant savings in yard operations, fuel usage and product quality.

**Material Definitive Agreement** - On August 28, 2006, the Company completed agreements whereby the Company raised \$1.3 million in debt financing from certain officers and members of the Company's Board of Directors. The funds were used for working capital requirements related primarily to the acquisition of StarTrak Systems, LLC, an acquisition that was effective on June 30, 2006.

**Contract for Wireless Tracking and Monitoring of Refrigerated Containers** - The Company announced on August 24, 2006 that its subsidiary, StarTrak Systems, LLC ("StarTrak"), had begun delivery on a single contract valued at greater than \$10 million for its GenTrak wireless tracking system and related monitoring services. The StarTrak contract represents one of the largest single industrial deployments of wireless tracking and monitoring systems on refrigerated assets anywhere.

GenTrak is a GPS-based, wireless monitoring and control system, initially deployed on marine gensets to monitor the location, operating condition, fuel levels, etc. of both the gensets and any connected refrigerated container. A marine genset is a portable generator temporarily connected to a refrigerated container to provide power during the land-based portion of the

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transport cycle. The GenTrak system provides significant operational savings and quality improvements to global shipping companies in their refrigerated container operations.

Nasdaq Listing Notification - In August of 2006, Alanco announced that it had received a staff determination letter from Nasdaq indicating that the Company failed to comply with the minimum bid price requirements for continued listing as set forth in Nasdaq Marketplace Rule 4310(c)(4), and that its securities may be subject to delisting from the Nasdaq Capital Market. The Company has appealed the Staff determination and requested a hearing before the Nasdaq Listing Qualifications Panel ("Panel"). Under Nasdaq Marketplace rules, a request for a hearing stays the delisting action pending the issuance of a written determination by the Panel. The hearing was held on September 14, 2006 in Washington, D.C. with representatives of the Company present. There can be no assurance that the Panel will grant the Company's request for continued listing. Pending a decision by the Panel, the Company's common stock will remain listed on the Nasdaq Capital Market.

Sale of Unregistered Securities - On July 14, 2006, the Company completed the sale, in a private offering to several private and institutional investors, of 240,000 Units consisting of one share of its Series A Convertible Preferred Stock together with a 5-year warrant to purchase three shares of the Company's Class A Common Stock at a price of \$.60 per share ("Unit") for a Unit price of \$1.71. The Company received \$410,400 from the offering. Twenty five percent of the Units, or 60,000 Units, were purchased by an institutional investor with the balance purchased by members of the Company's Board of Directors. Due to the structure of the offering and the Nasdaq stock market requirements, warrants issued in this offering to members of the Board of Directors are restricted from being exercised without shareholders' approval, which shall be requested at the next annual meeting of the Company's Shareholders.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### DESCRIPTION OF BUSINESS

##### RFID TECHNOLOGY SEGMENT

The Company acquired, in May 2002, the operations of Technology Systems International, Inc., a Nevada Corporation ("TSIN"). The technology consisted of the proprietary TSI PRISM(TM) wireless RFID tracking capabilities utilized primarily in correctional facilities, security management and personnel monitoring. The acquisition was effected through a wholly owned subsidiary, Technology Systems International, Inc., an Arizona corporation, by the issuance of Alanco Class A Common Stock to purchase TSIN's assets and assumption of specific liabilities of TSIN. During the fiscal year 2005, the Company changed the name of Technology Systems International, Inc. to Alanco/TSI PRISM, Inc. ("ATSI").

Marketing - ATSI markets its TSI PRISM(TM) RFID tracking system primarily in the United States, through the Company's direct sales representatives and a network of lobbyists. The primary focus of the marketing effort has been directed at the domestic state and federal correctional facilities and county jail markets. In addition, ATSI is providing transmitter technology for a project in the corrections market in Europe.

Raw Materials - The RFID Technology segment utilizes various domestic subcontractors for materials and parts used to manufacture its products. One domestic supplier represented approximately 34% of those purchases for fiscal year ended June 30, 2005. During fiscal year ended June 30, 2006, no

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subcontractor accounted for 10% or more of the business segment's purchases.

The Company anticipates continued concentration of vendor purchases; however, additional suppliers are readily available at competitive pricing levels. The Company does not foresee any future significant shortages or substantial price increases that cannot be recovered from its customers. See Competitive Conditions below for a discussion related to a new licensing agreement to provide new technology that may increase concentration of purchases in future years.

**Competitive Conditions** - The TSI PRISM(TM) system is the only known wireless RFID continuous real-time tracking technology currently available to the correctional facilities market. There are other companies attempting to introduce area location and monitoring technologies in the correctional facilities market, offering an area or zone detection system. However, at this time these technologies are not capable of providing continuous real-time tracking.

During fiscal year 2005, Alanco entered into a technology license agreement ("License") with a developer of RFID real-time location services technology utilizing 2.4 GHz wireless networking standards. The License grants to Alanco an exclusive five-year worldwide license for the corrections market, to acquire, modify or combine the 2.4 GHz technology with Alanco's 900 MHz TSI PRISM technology. The Company believes the 2.4 GHz technology has certain application advantages over the 900 MHz technology in international markets and in some segments of the U.S. corrections market. The License requires royalty payments on product sold and stipulates minimum annual purchase requirements starting in the second year of the License. As consideration for the License, Alanco agreed to make certain prepayments for future product purchases and granted a warrant to purchase 500,000 shares of Class A Common Stock at a price of \$1.00 per share.

**Employees** - The Company's RFID tracking segment employed eighteen full-time employees as of June 30, 2006 and 2005, respectively.

**Seasonality of Business** - Location and tracking products have minimal seasonality. However, many of the products in this segment are marketed to state and federal government customers that are affected by annual budget schedules and economic conditions.

**Dependence Upon Key Customers** - The RFID Technology segment is in an early stage of commercial market development. Targeted customers operate the majority of the prison facilities in the United States and include the 50 state governments, numerous county governments and the federal government. During the twelve months ended June 30, 2006, substantially all revenue was generated from four state governments. In fiscal year 2005, a substantial portion of revenues recognized were generated from two Midwestern state governments. The Company anticipates that as market penetration of its TSI PRISM(TM) technology accelerates, the Company will have numerous customers. However, due to the type of product sold by the RFID Technology segment, the size of each contract may continue to be significant.

**Backlog Orders** - The Company operates using system order contracts that it considers to be firm and non-cancelable and extended maintenance contracts not longer than twelve months. Under this method, the Company had an order backlog as of June 30, 2006 of approximately \$560,100, compared to \$76,200 at fiscal year end 2005.

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Research & Development - The Company estimated that the ATSI operation spent approximately \$200,000 and \$360,000 in research and development expenditures, recorded as selling, general and administrative expense, during fiscal years 2006 and 2005, respectively.

#### WIRELESS ASSET MANAGEMENT

The Company's Wireless Asset Management business segment was created by the acquisition, effective June 30, 2006, of StarTrak Systems, LLC ("StarTrak"), a privately held company located in Morris Plains, New Jersey. StarTrak is a leading provider of wireless GPS tracking and monitoring services which are offered on a monthly subscription basis to various industry segments. The company's primary focus is currently the refrigerated or "Reefer" segment of the transport industry. StarTrak provides the dominant share of all wireless tracking, monitoring and control services to this market segment.

Marketing - StarTrak markets its wireless tracking and wireless subscription data services in the United States, both through dealers and the company's direct sales representatives. The primary focus of the marketing effort has been directed at the domestic refrigerated transport market and the reefer equipment providers. The company also has limited international sales (Australia, Europe) and expects that segment to grow as well.

Raw Materials - The Company anticipates the Wireless Asset Management segment will utilize various domestic subcontractors for materials and parts used to manufacture its products; however certain vendors may represent more than 10% of total purchases for fiscal year 2007. Additional suppliers are available at competitive pricing levels and we anticipate concentration of purchases will decrease as new products are introduced and volumes increase. The Company does not foresee any future significant shortages or substantial price increases that cannot be recovered from its customers.

Competitive Conditions - StarTrak is the only known provider of wireless GPS tracking and monitoring services that offers a subscription program to the refrigerated or "Reefer" segment of the transport industry. There are other companies marketing GPS tracking services to the general transport industry; however, to our knowledge, none have the capability of providing integration with the major manufacturers' "Reefer" electronic systems that allows for the monitoring of various sensor data on a real time basis.

Employees - The Company's Wireless Asset Management segment employed thirty-three full-time employees and two part-time employees as of June 30, 2006.

Seasonality of Business - Location and tracking products have minimal seasonality. However, many of the products in this segment are marketed to commercial customers that are affected by annual budget schedules and economic conditions. Further, high asset utilization during the summer months can cause some seasonal effects on deployment of units.

Dependence Upon Key Customers - The company has numerous end customers, many of which chose to purchase StarTrak products from two primary OEM refrigerator equipment suppliers. StarTrak is the only vendor currently providing the two OEMs with tracking and monitoring products for the refrigerated or Reefer segment of the transport industry. Additionally, the company is currently delivering product and providing subscription services under a contract with a major customer that is expected to exceed 10% of fiscal year 2007 segment revenue.

Backlog Orders - The Company operates using order contracts that it considers to be firm and non-cancelable. Under this method, the Company had

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unfulfilled contracts as of June 30, 2006 of approximately \$11 million.

### COMPUTER DATA STORAGE SEGMENT

The Company's Computer Data Storage segment consists of two separate units, Arraid, Inc. ("Arraid") and Excel/Meridian Data, Inc. ("Excel"). Arraid is a Phoenix, Arizona-based manufacturer of legacy computer data storage products, and Excel is a Dallas, Texas-based provider of data storage networking products and services.

Arraid designs and manufactures proprietary data storage subsystems called "emulators" that serve as translators between older "legacy" computers and state-of-the-art storage devices and provides unique, cost-effective storage system solutions. Arraid's unique products are targeted at users of special application legacy computers, such as airplane flight simulators, nuclear power control systems, missile tracking computer systems, etc.

Excel is a manufacturer and marketer of data storage networking products and is recognized as a leading provider of optical storage devices, such as CD/DVD-ROM servers. Excel also markets a Network Attached Storage ("NAS") product line and other storage products incorporating state-of-the-art software technology.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Marketing - Arraid markets legacy storage products nationally and internationally through Company sales representatives and independent sales representatives and distributors. Excel markets optical storage and NAS products, primarily in the United States, through national advertising, telemarketing and Company sales representatives.

Raw Materials - The computer data storage operations have numerous domestic sources for materials and parts used to manufacture their products. For fiscal year 2006 and 2005, no supplier provided 10% or more of the Company's data storage material and parts purchases. The Company believes that it has an adequate supply of materials and parts and does not foresee any significant shortages or substantial price increases that cannot be passed on to the customers.

Competitive Conditions - There are numerous competitors in the computer data storage market, with no company dominating the market. Arraid principally provides unique storage products to a limited market with minimal direct competitors. Excel competes with many established companies in the general storage market and many of these companies may have substantially greater financial, marketing and technological resources, larger distribution capabilities, earlier access to customers and more opportunities to address customers' various information storage requirements than the Company. The Company also competes with many smaller, less established companies in specific storage product segments. Some of these companies may have earlier access to new technologies or products than the Company. The announcement or introduction of new products and/or implementation of effective marketing strategies by its competitors may have a materially adverse affect on the Company's business.

Employees - As of June 30, 2006 the Company's computer data storage business employed twenty-seven full-time employees, compared to twenty-four full-time employees as of June 30, 2005.

Seasonality of Business - Computer data storage products have minimal seasonality. However, many of the products in this segment are marketed to business customers, which in some cases can be significantly affected by budget

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restraints and economic conditions.

Dependence Upon Key Customers - During fiscal year ended June 30, 2006, no customer accounted for more than 10% of the reported Data Storage revenues. During fiscal year 2005, one customer accounted for 10.2% of revenues.

Backlog Orders - The Company operates using customer purchase orders that in some cases may not be considered firm and non-cancelable. Methods of defining a firm "Backlog Order" are being evaluated, and if the Company utilizes that information in evaluating sales activity, the information will be reported.

Research & Development - The Company estimates it spent approximately \$150,000 in research and development expenditures, recorded as selling, general and administrative expense, for both fiscal years 2006 and 2005.

### NET ASSETS HELD FOR SALE

The Company's reporting business segments for both fiscal years 2006 and 2005 are limited to the RFID Technology segment and Computer Data Storage segment discussed above. Assets classified on the Company's balance sheet at June 30, 2006 and 2005 as "net assets held for sale" consist of remaining Restaurant Equipment segment assets, which are being liquidated and are valued at the lower of cost or net realizable value. Income of the Restaurant Equipment liquidation activities are reported as "other income" for both the current and prior fiscal years.

### ITEM 2. PROPERTIES

The Company's corporate office and the ATSI operation are located in an approximate 9,300 square foot leased facility in Scottsdale, Arizona. The current lease expires on July 31, 2007.

In August 2003, Arraid entered into a three-year 5,200 square foot office/manufacturing space lease and moved to a new Phoenix, Arizona location. The three-year lease, scheduled to expire on August 31, 2006, was extended through August 2008.

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Excel/Meridian Data, Inc. entered into an office/manufacturing space lease during fiscal year 2001 for 11,328 square feet in Carrollton, Texas. The five-year lease, scheduled to expire on March 15, 2006 was extended through April 2009.

StarTrak Systems, LLC, is currently occupying an approximately 5,000 square foot office/manufacturing facility in Morris Plains, New Jersey under a lease scheduled to expire on September 30, 2007. Management is currently working with its landlord to obtain significant additional office/manufacturing space required due to business expansion.

### ITEM 3. LEGAL PROCEEDINGS

The Company is a party to litigation that relates to the acquisition, in May of 2002, of substantially all the assets of Technology Systems International, Inc., a Nevada Corporation ("TSIN"), to litigation arising out of Carolina Casualty Insurance Company's failure to pay a claim (relating to the TSIN litigation) pursuant to a Directors and Officers insurance policy, and to litigation arising from an expired property lease between the Company's subsidiary, Arraid, Inc., and Arraid Property L.L.C., an Arizona limited liability company. The actions are more fully described below:



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On January 30, 2003, a shareholder of TSIN filed a derivative suit naming as defendants the Company and its wholly owned subsidiary, ATSI. The venue for this action is the Arizona Superior Court in and for Maricopa County, Arizona, as case number CV2003-001937. The complaint sets forth various allegations and seeks damages arising out of the Company's acquisition of substantially all of the assets of TSIN. This derivative suit was terminated and the action converted into a direct action by TSIN by stipulation and court order in July 2003.

TSIN is currently in Chapter 7 bankruptcy. The Chapter 7 Trustee failed to prosecute the action timely and the state court dismissed the action for lack of prosecution, but allowed the Trustee to restart the action, which the Trustee has done as case number CV2006-007398. The Company is seeking its attorney's fees with respect to the dismissed action, and will appeal the court's order allowing the Trustee to restart the action. The Company's management, in consultation with legal counsel, believes the plaintiff's claims are without merit and the Company will continue to aggressively defend the action. In addition, the Company will pursue reimbursement of legal expenses incurred from TSIN.

The Company is the plaintiff in a lawsuit (U.S. District Court No. CV-04-0789-PHX-DGC) arising out of Carolina Casualty Insurance Company's ("Carolina") failure to pay a claim regarding the TSIN litigation, that the Company made pursuant to its Directors and Officers Insurance Policy ("Policy") issued by Carolina. The Company seeks payment for its legal expenses in the TSIN litigation and reimbursement of legal fees incurred in the Carolina litigation. The District Court granted summary judgment in favor of Carolina and the Company has filed an appeal with the Ninth Circuit Court of Appeals.

On July 18, 2003, Arraid Property L.L.C., an Arizona Limited Liability Company ("Arraid LLC"), filed a complaint in the Arizona Superior Court in and for Maricopa County, Arizona (case number CV 2003-13999) against the Company and its wholly owned subsidiary Arraid, Inc., alleging breach of lease and seeking substantial monetary damages. The suit relates to an expired lease agreement for property previously leased by Arraid. Following a trial, the Court found in favor of Arraid LLC against the Company with respect to certain factual findings resulting in damages owed by the Company in an amount currently undecided, but anticipated to be less than \$35,000. The prevailing party, which has not yet been determined by the court, will likely be awarded some attorney's fees. Based upon a determination of the amount of any final award against the Company, the Company's management, in consultation with legal counsel, will determine whether to appeal the decision of the court.

The Company may also, from time to time, be involved in litigation arising from the normal course of business. As of June 30, 2006, there was no such litigation pending deemed material by the Company.

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#### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of the Shareholders during the fourth quarter of fiscal year ended June 30, 2006.

#### ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Alanco's common stock is traded on the Nasdaq Small Cap Market under the symbol "ALAN."

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The following table sets forth high and low sale prices for each fiscal quarter for the last two fiscal years. Such quotations represent inter-dealer prices without retail mark-ups, markdowns, or commissions and, accordingly, may not represent actual transactions.

Quarter Ended	High	Low	High	Low
September 30	\$0.99	\$0.70	\$1.72	\$0.91
December 31	\$0.70	\$0.46	\$1.19	\$0.78
March 31	\$0.78	\$0.48	\$1.20	\$0.69
June 30	\$0.83	\$0.60	\$1.37	\$0.89

As of June 30, 2006, Alanco had approximately 1,300 holders of record of its Class A Common Stock. This does not include beneficial owners holding shares in street name.

During the fiscal year ended June 30, 2006, the Company issued 11,473,500 shares of its Class A Common Stock. Of those shares, 2,100,000 shares were issued in connection with exercise of employee stock options and warrants, 383,500 were issued for services and prepayments, 3,990,000 were issued pursuant to a private offering and 5,000,000 were issued in the StarTrak acquisition.

Alanco has paid no Common Stock cash dividends and has no current plans to do so. During fiscal years ended June 30, 2006 and 2005, holders of Series A Convertible Preferred Stock received "paid-in-kind" dividends of 341,700 shares valued at \$512,500 and 304,400 shares valued at \$456,600, respectively. Holders of Series B Convertible Preferred Stock received "paid-in-kind" dividends during fiscal years ended June 30, 2006 and 2005 of 7,000 shares, valued at \$70,200, and 6,500 shares, valued at \$64,500, respectively.

### ITEM 6. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### Critical Accounting Policies

"Management's Discussion and Analysis of Financial Condition and Results of Operations" discusses our consolidated financial statements that have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amount of assets and liabilities at the date of the financial statements, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. On an on-going basis, we evaluate our estimates and judgments, including those related to revenue recognition, valuation allowances for inventory and receivables, warranty and impairment of long-lived and intangible assets. We base our estimates and judgments on historical experience and on various other factors that are believed to be reasonable under the circumstances. The result of these estimates and judgments form the basis for making conclusions about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The SEC suggests that all registrants list their most "critical accounting policies" in Management's Discussion and Analysis. A critical accounting policy is one which is both important to the portrayal of the Company's financial condition and results and requires management's most

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difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Management has identified the critical accounting policies presented below as those accounting policies that affect its more significant judgments and estimates in the preparation of its consolidated financial statements. The Company's Audit Committee has reviewed and approved the critical accounting policies identified.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

These policies include, but are not limited to, the carrying value of goodwill and other intangible assets, estimates related to the valuation of inventory and receivables, the actual net realizable value of net assets held for sale and the ultimate resolution of the current litigation with TSIN and Arraid L.L.C. that is more fully discussed in Item 3, Legal Proceedings.

#### Results of Operations

In accordance with accounting principles generally accepted in the United States of America, the Company is reporting consolidated revenues for fiscal years ended June 30, 2006 and 2005 from its Computer Data Storage segment and its RFID Technology segment.

	Data Storage	RFID Technology	Wireless Asset Management	Corporate	Total
	-----	-----	-----	-----	-----
Fiscal year 2006					
Revenue	\$ 6,028,100	\$ 631,500	\$ -	\$ -	\$ 6,659,600
Cost of Goods Sold	3,877,800	479,900	-	-	4,357,700
	-----	-----	-----	-----	-----
Gross Profit	2,150,300	151,600	-	-	2,301,900
Selling, General & Administrative	2,081,600	2,669,600	-	1,553,100	6,304,300
	-----	-----	-----	-----	-----
Operating Income (Loss)	\$ 68,700	\$ (2,518,000)	\$ -	\$ (1,553,100)	\$ (4,002,400)
	=====	=====	=====	=====	=====
Accounts Receivable	\$ 645,400	\$ 178,300	\$ 919,700	\$ 17,300	\$ 1,760,700
	=====	=====	=====	=====	=====
Inventory	\$ 1,317,500	\$ 940,500	\$ 885,900	\$ -	\$ 3,143,900
	=====	=====	=====	=====	=====
Total Assets	\$ 2,344,200	\$ 7,239,800	\$ 17,572,200	\$ 528,300	\$ 27,684,500
	=====	=====	=====	=====	=====
Capital Expenditures	\$ 15,800	\$ 54,400	\$ -	\$ 600	\$ 70,800
	=====	=====	=====	=====	=====
Depreciation & Amortization	\$ 24,200	\$ 355,600	\$ -	\$ 3,200	\$ 383,000
	=====	=====	=====	=====	=====
Fiscal year 2005					
Revenue	\$ 6,363,300	\$ 820,900	\$ -	\$ -	\$ 7,184,200
Cost of Goods Sold	4,161,200	514,300	-	-	4,675,500
	-----	-----	-----	-----	-----
Gross Profit	2,202,100	306,600	-	-	2,508,700
Selling, General & Administrative	1,918,300	2,697,600	-	1,755,400	6,371,300

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Operating Income (Loss)	\$ 283,800	\$ (2,391,000)	\$ -	\$ (1,755,400)	\$ (3,862,600)
Accounts Receivable	\$ 827,600	\$ 246,400	\$ -	\$ 17,400	\$ 1,091,400
Inventory	\$ 1,091,900	\$ 810,700	\$ -	\$ -	\$ 1,902,600
Total Assets	\$ 2,398,800	\$ 6,987,600	\$ -	\$ 1,157,500	\$ 10,543,900
Capital Expenditures	\$ 41,600	\$ 108,900	\$ -	\$ 2,400	\$ 152,900
Depreciation & Amortization	\$ 20,300	\$ 326,400	\$ -	\$ 3,100	\$ 349,800

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Consolidated revenues for fiscal year 2006 were \$6,659,600, a decrease of 7.3% when compared to \$7,184,200 revenues for fiscal year 2005. The revenue decrease resulted from decreases in both the Data Storage and the RFID Technology segments. The decrease in Data Storage segment revenue of \$335,200, or 5.3%, resulted from a change in product mix, redirecting military defense expenditures from computer system support to the war effort and general reduction in selling prices of data storage products. The RFID Technology segment also reported decreased revenues to \$631,500 compared to \$820,900 for the previous year. The decrease in RFID Technology segment revenues was due to a lack of sales of the TSI PRISM system products. The TSI PRISM revenue level is significantly below the Company's expectation. The Company believed the slow sales growth of the RFID Technology segment in fiscal year 2005 was related to the economic conditions that reduced both state and federal government tax revenues and the prolonged government procurement process. We believe that assessment was accurate and that prolonged government procurement process was again the main influence on the low sales level for fiscal 2006. Customer activity is currently significant and various state governments are considering methods to finance the adoption of RFID technology for their state corrections facilities.

The Company's gross profit for fiscal year 2006 was \$2,301,900 (34.6% of sales), a decrease of \$206,800 or 8.2%, when compared to \$2,508,700 (34.9% of sales) for the prior year. The Data Storage segment reported gross profit of \$2,150,300, a decrease of \$51,800, or 2.4%, compared to \$2,202,100 gross profit reported for the prior year. Gross margin for fiscal year 2006 reported for the Data Storage segment was 35.7%, compared to 34.6% reported in the prior year. The decrease in Data Storage gross profit resulted from decreased sales while the increase in gross margin resulted from changes in product mix. The RFID Technology segment reported a decrease in gross margin to \$151,600, from \$306,600 reported for the prior fiscal year. Reported gross margin of the RFID Technology was 24% compared to 37.4% reported for the prior fiscal year. Due to minimum sales recognized for the RFID Technology segment in both fiscal years, the gross margins are not reflective of the gross margin percentage that is anticipated under higher sales levels.

Consolidated selling, general and administrative expenses for the year ended June 30, 2006 decreased by \$67,000, or 1.0%, to \$6,304,300, compared to \$6,371,300 in fiscal 2005. Selling, general and administrative expense for the Data Storage segment increased by \$163,300, or 8.5%, when compared to the prior year. The increase in Data Storage segment selling, general and administrative costs resulted from increases in sales and administrative costs related to adding sales personnel and enhancing sales support. Selling, general and

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administrative expenses for the RFID Technology segment decreased by \$28,000, or 1.0%. Corporate administrative expenses decreased by \$202,300, or 11.5%, compared to the prior year primarily due to a decrease in legal expenses related to TSIN and other litigations previously discussed. The Company has committed to pursue reimbursement of legal expense incurred.

The operating loss for fiscal year ended June 30, 2006 was \$4,002,400, a \$139,800, or 3.6%, increase when compared to the operating loss for the prior fiscal year of \$3,862,600. The increase in the Company's operating loss resulted from increased operating losses in the RFID Technology segment, increasing their operating loss by approximately \$127,000 in fiscal year 2006 compared to the prior year. The Data Storage segment reported operating income of \$68,700, compared to operating income of \$283,800 reported in the fiscal year ended June 30, 2005. The loss from operations for the fiscal year ended June 30, 2006 was \$4,009,200, a 5.7% increase when compared to a loss of \$3,790,600 for the prior fiscal year.

Fiscal year 2006 interest expense, net of interest income, was \$90,300, compared to net interest expense of \$34,700 for the previous year. The increase in net interest expense reflects increased average borrowing and interest rates under the Company's line of credit agreement during fiscal 2006.

Other income for the year ended June 30, 2006 was \$83,500, compared to \$106,700 for the prior year. Other income for the current fiscal year includes \$54,200 related to the collection of notes receivable associated with the sale of "net assets held for sale" in a prior year and \$30,000 income from the sale of "net assets held for sale" in fiscal year 2006. Fiscal year 2005 included a gain of \$89,600 related to the collection of notes receivable associated with the sale of "net assets held for sale" in the prior year and \$17,100 of income from the sale of "net assets held for sale."

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Preferred Stock dividends paid in-kind for the year ended June 30, 2006 for both Series A and Series B Convertible Preferred Stock amounted to \$582,700, compared to Preferred Stock dividends of \$521,100 for the prior year, an increase of \$61,600, or 11.8%. Series A Preferred shareholders received in-kind dividends of 341,700 shares valued at \$512,500, compared to 304,400 shares valued at \$456,600 in the prior year. Series B Preferred shareholders received 7,000 shares valued at \$70,200 compared to 6,500 shares valued at \$64,500 in fiscal year 2005. See Footnote 12 - Shareholders' Equity for additional discussion of Preferred Stock transactions.

Consolidated net loss attributable to Common stockholders for fiscal year ended June 30, 2006 was \$4,591,900, or (\$.16) per share, an increase of 6.5% when compared to a net loss attributable to Common stockholders of \$4,311,700, or (\$.17) per share, for the prior year. The increase in net loss attributable to Common stockholders of \$280,200 was due to increases in operating losses of the RFID Technology segment and increases in preferred stock dividends, partially offset by a reduction in legal expenses.

Net cash used in operating activities for the fiscal year ended June 30, 2006 was \$3,713,500 compared with net cash used in operating activities for the prior fiscal year of \$3,514,000. The increase of \$199,500, or 5.7%, resulted primarily from an increase in loss from operations of \$218,600. See "Liquidity and Capital Resources" below for management's discussion of major items affecting the Consolidated Statement of Cash Flow.

Any new Statements of the Financial Accounting Standards affecting the Company are disclosed in the "Notes to Consolidated Financial Statements."

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### Liquidity and Capital Resources

At June 30, 2006 the Company's current liabilities exceeded current assets by approximately \$7.2 million, resulting in a current ratio of .5 to 1. At June 30, 2005, the Company's current assets exceeded current liabilities by \$2.8 million, reflecting a current ratio of 3.1 to 1. The substantial decrease in current ratio resulted from an increase of approximately \$9.4 million in net current liabilities related to the acquisition of StarTrak Systems, LLC. \$5.7 million of the increase is represented by the current liability presented as Deferred stock payment, StarTrak, a liability that relates to the Company's commitment as part of the merger agreement to issue, after shareholder approval expected at the next annual meeting of the Company's shareholders, up to 8.2 million shares of the Company's Class A Common Stock. The Deferred stock payment liability is valued at market value on June 30, 2006 and may be adjusted from time to time until paid, based upon market price fluctuation of the Company's stock. Approximately \$4.1 million of the increase in net current liabilities is related to current liabilities of StarTrak assumed in excess of current assets. The balance of the increase in net liabilities relates to incurred expenses related to the transaction.

Accounts receivable at June 30, 2006 of \$1,760,700 reflects an increase of \$669,300 from the \$1,091,400 reported as consolidated accounts receivable at the end of fiscal year 2005. \$919,700, or 52.2% of the current fiscal year end balance, was acquired in the acquisition of StarTrak Systems, LLC, effective June 30, 2006. Receivables for the Data Storage and RFID Technology segments decreased by \$250,300, or 23.3%. Data Storage segment accounts receivable balances at June 30, 2006 amounted to \$645,400, a decrease of \$182,200, or 22.0%, compared to the previous year. The Data Storage segment accounts receivable balance at June 30, 2006 represented twenty-eight days' sales in receivables compared to thirty-four days at fiscal year end 2005. Accounts receivable for the RFID Technology segment amount to \$178,300 compared to \$246,400 at year end June 30, 2005. Days' sales for the RFID Technology segment are distorted due to the lack of significant reported sales. In addition, a receivable in the amount of \$62,200, representing the final payment for a system installation, was significantly past our normal terms due to a special arrangement whereby the Company was allowed to utilize the site for a research and development project. The project has been completed and the customer is processing the invoice for payment.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Consolidated inventories at June 30, 2006 amounted to \$3,143,900 compared to \$1,902,600 at the end of the prior fiscal year, an increase of \$1,241,300, or 65.2%. \$885,900 or 71% of the increase is due to inventory acquired in the merger with StarTrak. The Data Storage segment accounted for \$225,600, or 18.2% of the inventory increase; and increases in the RFID Technology segment inventory accounted for \$129,800 or 10.5% of the increase. The RFID Technology segment inventory levels increased due to a system installation in process at June 30, 2006 that required certain site specific equipment. The Data Storage segment inventory increase resulted from inventory acquired to complete a warranty project, inventory acquired for new products evaluation and general inventory increases. The June 30, 2006 Data Storage segment inventory balance reflects an inventory turnover of 2.9 compared to 3.8 for inventory levels at June 30, 2005.

Cash used in investing activities during the current year was \$753,900, compared to cash used in investing activities of \$10,400 for the previous year. The increase was due primarily to cash funding of StarTrak prior to the June 2006 acquisition in the amount of \$774,300.

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Net cash provided by financing activities during fiscal year ended June 30, 2006 amounted to \$4,885,600, compared to \$2,286,100 for the prior year. Cash provided by financing activities included \$3,465,100 and \$1,963,500 in proceeds from the sale of common stock, net of additional shares listing fees of \$44,000 and \$38,300, for fiscal years ended June 30, 2006 and 2005, respectively. Advances on borrowings amounted to \$1,993,500 compared to \$329,500 for the previous year. Cash repayments of borrowing and capital leases during the year amounted to \$573,000, compared to \$6,900 during the prior fiscal year.

The Company had a \$2,000,000 line of credit balance at June 30, 2006 under a \$2,000,000 line of credit agreement with a private trust that was last amended effective June 30, 2006. The secured line of credit is based upon accounts receivable and inventory values, and is secured by all assets of the Company. The line of credit has an interest rate of prime plus 2% (10.25% at June 30, 2006). Under an amendment to the line of credit agreement, the Company must maintain a balance due under the line of at least \$1,500,000 through July 2007 (reduced to \$1,000,000 under certain conditions controlled by the lender). Due to the minimum borrowing requirement and the July 2007 expiration date, \$1.0 million of the balance due is presented at June 30, 2006 as notes payable, long term, more fully discussed in Note 7 to the consolidated financial statements.

Although management cannot assure that future operations will be profitable or that additional debt and/or equity will not be required, we believe our cash balances of \$1,155,500, additional capital raised subsequent to the end of fiscal 2006 and a term loan currently being negotiated, will provide adequate capital resources to maintain operations for the next year. However, if additional working capital is required and not obtained through additional long-term debt, equity capital or operations, it could adversely affect future operations. Management has historically been successful in obtaining financing and has demonstrated the ability to implement a number of cost-cutting initiatives to reduce working capital needs. As previously discussed, the Company requires and continues to pursue additional capital for growth and strategic plan implementation. Accordingly, the accompanying consolidated financial statements have been prepared assuming the Company will continue to operate and do not include any adjustments that might be necessary if the Company is unable to continue as a going concern. As a result, the Company's independent certified public accountants have issued a going concern opinion on the consolidated financial statements of the company for the fiscal year ended June 30, 2006.

### Product and Environmental Contingencies

The Company is not aware of any material liabilities, either product or environmental related.

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

### ITEM 7. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

See Consolidated Financial Statements.

Index to Financial Statements

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

REPORT OF REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders  
Alanco Technologies, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Alanco Technologies, Inc. and Subsidiaries as of June 30, 2006 and 2005, and the related consolidated statements of operations, changes in shareholders' equity and preferred stock, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits include consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Alanco Technologies, Inc. and Subsidiaries as of June 30, 2006 and 2005, and the results of its operations, changes in shareholders' equity and preferred stock, and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.



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The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the Company has incurred significant losses from operations, anticipates additional losses in the next year, and has insufficient working capital as of June 30, 2006 to fund the anticipated losses. These conditions raise substantial doubt as to the ability of the Company to continue as a going concern. These consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Semple & Cooper LLP  
 Certified Public Accountants

Phoenix, Arizona  
 September 15, 2006

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### CONSOLIDATED BALANCE SHEETS AS OF JUNE 30,

	2006	2005
	-----	-----
ASSETS		
CURRENT ASSETS		
Cash	\$ 1,155,500	\$ 737,300
Accounts receivable, net	1,760,700	1,091,400
Notes receivable, current	31,600	80,000
Inventories, net	3,143,900	1,902,600
Prepaid expenses and other current assets	556,600	378,200
	-----	-----
Total current assets	6,648,300	4,189,500
	-----	-----
PROPERTY, PLANT AND EQUIPMENT, NET	202,300	273,500
	-----	-----
OTHER ASSETS		
Goodwill, net	20,417,100	5,356,300
Other intangible assets	339,200	560,700
Long-term notes receivable, net	-	8,000
Net assets held for sale	28,200	100,200
Other assets	49,400	55,700
	-----	-----
Total other assets	20,833,900	6,080,900
	-----	-----
TOTAL ASSETS	\$ 27,684,500	\$ 10,543,900
	=====	=====
LIABILITIES AND EQUITY		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	\$ 5,066,200	\$ 1,279,600
Credit Line	1,000,000	-
Billings in excess of cost and est. earnings on uncompleted contracts	43,500	4,200
Notes payable, current	875,300	-

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Deferred stock payment, StarTrak	5,715,400	-
Customer advances	1,001,100	-
Deferred revenue, current	126,000	60,100
	-----	-----
Total Current Liabilities	13,827,500	1,343,900
	-----	-----
LONG TERM LIABILITIES		
Notes payable, long term	2,679,100	1,143,600
	-----	-----
TOTAL LIABILITIES	16,506,600	2,487,500
	-----	-----
Preferred Stock - Series B Convertible		
500,000 shares authorized, 75,000 and		
68,000 issued and outstanding,		
respectively	737,500	667,300
	-----	-----
SHAREHOLDERS' EQUITY		
Preferred Stock - Series A Convertible		
5,000,000 shares authorized, 3,122,900		
and 2,781,200 shares issued and		
outstanding, respectively	3,925,200	3,412,700
Common Stock		
Class A - 75,000,000 shares authorized,		
38,653,700 and 26,680,200 shares, net of		
treasury shares, outstanding, respectively	78,845,300	71,714,600
Class B - 25,000,000 shares authorized		
and none were issued	-	-
Treasury Stock, at cost		
500,000 shares at June 30, 2006 and 2005	(375,100)	(375,100)
Accumulated deficit	(71,955,000)	(67,363,100)
	-----	-----
Total shareholders' equity	10,440,400	7,389,100
	-----	-----
TOTAL LIABILITIES & SHAREHOLDERS' EQUITY	\$ 27,684,500	\$ 10,543,900
	=====	=====

See accompanying notes to the consolidated financial statements

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS  
FOR THE YEAR ENDED JUNE 30,

	2006	2005
	-----	-----
NET SALES	\$ 6,659,600	\$ 7,184,200

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Cost of goods sold	4,357,700	4,675,500
	-----	-----
GROSS PROFIT	2,301,900	2,508,700
Selling, general and administrative expense	6,304,300	6,371,300
	-----	-----
OPERATING LOSS	(4,002,400)	(3,862,600)
OTHER INCOME & EXPENSES		
Interest expense, net	(90,300)	(34,700)
Other income, net	83,500	106,700
	-----	-----
LOSS FROM OPERATIONS	(4,009,200)	(3,790,600)
Preferred stock dividend - in kind	(582,700)	(521,100)
	-----	-----
NET LOSS ATTRIBUTABLE TO COMMON STOCKHOLDERS	\$ (4,591,900)	\$ (4,311,700)
	=====	=====
NET LOSS PER SHARE - BASIC AND DILUTED		
- Net Loss Attributable to Common Shareholders	\$ (0.16)	\$ (0.17)
	=====	=====
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	29,106,100	25,355,500
	=====	=====

See accompanying notes to the consolidated financial statements

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY & PREFERRED STOCK  
FOR THE YEARS ENDED JUNE 30, 2006 AND 2005

	COMMON STOCK		SERIES A PREFERRED STOCK		TREASURY STOCK	
	SHARES	AMOUNT	SHARES	AMOUNT	SHARES	AMOUNT
	-----	-----	-----	-----	-----	-----
Balances, June 30, 2004	23,732,800	\$ 69,334,700	2,476,800	\$ 2,956,100	500,000	\$ (375,100)
Options, warrants exercised	3,113,200	2,025,100	-	-	-	-
Shares & warrants issued for services	334,200	319,700	-	-	-	-
Preferred Dividend, Series A, paid in kind	-	-	304,400	456,600	-	-
Warrants issued for loan amendment and licensing agreement	-	73,400	-	-	-	-
NASDAQ listing of additional shares	-	(38,300)	-	-	-	-
Net Loss	-	-	-	-	-	-
	-----	-----	-----	-----	-----	-----
Balances, June 30, 2005	27,180,200	\$ 71,714,600	2,781,200	\$ 3,412,700	500,000	\$ (375,100)

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Options, warrants exercised	2,100,000	1,235,000	-	-	-	-
Shares & warrants issued for services	158,500	110,400	-	-	-	-
Shares issued for prepaid services	225,000	135,000	-	-	-	-
Private Offerings, Net	3,990,000	2,274,100	-	-	-	-
Acquisition of StarTrak	5,000,000	3,485,000	-	-	-	-
Preferred Dividend, Series A, paid in kind	-	-	341,700	512,500	-	-
Stock adjustment	-	(64,700)	-	-	-	-
NASDAQ listing of additional shares	-	(44,100)	-	-	-	-
Net loss	-	-	-	-	-	-
	-----	-----	-----	-----	-----	-----
Balances, June 30, 2006	38,653,700	\$ 78,845,300	3,122,900	\$ 3,925,200	500,000	\$ (375,100)
	=====	=====	=====	=====	=====	=====

See accompanying notes to the consolidated financial

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR FISCAL YEARS ENDED JUNE 30,

	2006	2005
	-----	-----
CASH FLOWS FROM OPERATING ACTIVITIES		
Loss from operations	\$ (4,009,200)	\$ (3,790,600)
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	383,100	349,800
Stock and warrants issued for services	51,100	82,400
Income from assets held for sale	(30,000)	(106,700)
Loss on disposal of asset	22,600	-
Changes in:		
Accounts receivable, net	250,300	(434,200)
Inventories, net	(355,500)	379,700
Prepaid expenses and other current assets	(125,600)	(46,900)
Accounts payable and accrued expenses	103,300	34,800
Deferred revenue	(53,900)	33,000
Billings and estimated earnings in excess of costs on uncompleted contracts	39,300	(21,600)
Other assets	11,000	6,300
	-----	-----
Net cash used in continuing operations	(3,713,500)	(3,514,000)
	-----	-----
CASH FLOWS FROM INVESTING ACTIVITIES		
Net cash from assets held for sale	101,900	73,000
Collection of notes receivable	56,400	149,600
Cash advances - TSIN litigation	-	(80,000)
Purchase of property, plant and equipment	(70,800)	(153,000)
Goodwill, acquisition	(67,100)	-
Cash funding of StarTrak prior to acquisition	(774,300)	-

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Net cash provided by (used in) investing activities	(753,900)	(10,400)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on borrowings	1,993,500	329,500
Repayment on borrowings	(573,000)	(6,900)
Net Proceeds from sale of Common Stock	3,465,100	1,963,500
Net cash provided by financing activities	4,885,600	2,286,100
NET INCREASE (DECREASE) IN CASH	418,200	(1,238,300)
CASH AND CASH EQUIVALENTS, beginning of period	737,300	1,975,600
CASH AND CASH EQUIVALENTS, end of period	\$ 1,155,500	\$ 737,300
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION		
Net cash paid during the period for interest	\$ 90,300	\$ 34,700
Non-cash activities:		
Value of stock issued for services and prepayments	\$ 245,400	\$ 303,200
Value of warrants issued for credit line extension and licensing agreement	\$ -	\$ 113,200
Value of shares issued in payment of notes receivable	\$ 107,000	\$ -
Stock issued for StarTrak acquisition	\$ 3,485,000	\$ -
Purchase of goodwill that is accrued at year-end	\$ 67,100	\$ -
StarTrak liabilities assumed in excess of assets acquired	\$ 5,425,800	\$ -
Net value of equipment written off during the period	\$ 22,700	\$ -
Preferred Stock issued, in kind	\$ 552,800	\$ 521,100

See accompanying notes in the consolidated financial statements

ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

1. NATURE OF OPERATIONS AND SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations - Alanco Technologies, Inc. was incorporated in Arizona in 1969.

Alanco Technologies, Inc. and subsidiaries (the "Company") business operations for the past several years have emphasized a plan to strategically position the Company as a provider of information

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technology. The plan was initiated in fiscal year 2000 by acquiring Arraid, Inc. ("Arraid"), a manufacturer of proprietary storage products to upgrade older "legacy" computer systems, and Excel/Meridian Data, Inc. ("Excel"), a manufacturer of Network Attached Storage ("NAS") systems for mid-range organizations. These acquisitions formed the Company's Computer Data Storage business segment.

Concurrent with the implementation of the strategic plan, Alanco established a formal plan to sell the previously reported business segments. During fiscal years ended June 30, 2006 and 2005, the only activity related to the previously reported business segments was the continued liquidation of restaurant equipment assets, the net value of which is presented in the balance sheets at June 30, 2006 and 2005 as "net assets held for sale."

The Company continued its new strategic direction in fiscal year 2002 when Alanco/TSI PRISM, Inc. ("ATSI") acquired wireless tracking RFID (Radio Frequency Identification) technology designed to be used in the corrections market, through its acquisition of the operations of Technology Systems International, Inc., a Nevada corporation ("TSIN"); and again in fiscal year 2006 when the Company expanded its footprint in wireless tracking and data services into wireless asset management for the refrigerated or "Reefer" market through the acquisition, effective June 30, 2006, of StarTrak Systems, LLC, a provider of GPS tracking and wireless data services for the Reefer segment of the transport industry.

In fiscal years 2006 and 2005, the Company had continuing operations in the RFID Technology segment and in the Computer Data Storage segment. The StarTrak acquisition, effective June 30, 2006, created the Company's new Wireless Asset Management segment, the accounts of which are included in the consolidated balance sheet at June 30, 2006. Operating results for the Wireless Asset Management will be reported starting in the quarter ending September 30, 2006.

Principles of Consolidation - The consolidated financial statements for the years ended June 30, 2006 and 2005 include the accounts of Alanco Technologies, Inc. and its wholly-owned subsidiaries, ATSI, Arraid, Excel, Fry Guy Inc. and StarTrak Systems, LLC (collectively, the "Company"). StarTrak Systems, LLC operations were acquired effective June 30, 2006 and therefore are not included in the Company's consolidated Statement of Operations. All subsidiaries are Arizona corporations, except Fry Guy Inc., which is a Nevada corporation and StarTrak Systems, LLC, which is a Delaware LLC. All significant intercompany accounts and transactions have been eliminated in consolidation.

Cash Equivalents - The Company considers all highly liquid debt instruments with original maturities of three months or less to be cash equivalents.

Accounts Receivable Trade - The Company provides for potentially uncollectible accounts receivable by use of the allowance method. An allowance is provided based upon a review of the individual accounts outstanding and the Company's prior history of uncollectible accounts. Provision for uncollectible accounts receivable amounted to approximately \$71,600 and \$60,200 at June 30, 2006 and 2005, respectively. The Company does not typically accrue interest or fees on past due amounts.

Inventories - Inventories consist of materials and parts, work-in-process, and finished goods. Inventories are stated at the lower of cost or market. Cost is calculated using the average-cost method for the Data Storage segment and first-in, first-out ("FIFO") for the RFID Technology and the Wireless Asset Management segments.

ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Property, Plant and Equipment - Property, plant and equipment are stated at cost. Depreciation is computed over the estimated useful lives of the assets using the straight-line method, generally over a 3 to 10-year period. Leasehold improvements are amortized on the straight-line method over the lesser of the lease term or the useful life. Expenditures for ordinary maintenance and repairs are charged to expense as incurred. Betterments are capitalized as incurred. Upon retirement or disposal of assets, the cost and accumulated depreciation are eliminated from the account and any gain or loss is reflected in the statement of operations.

Fair Value of Financial Instruments - The estimated fair values for financial instruments are determined at discrete points in time based on relevant market information. These estimates involve uncertainties and cannot be determined with precision. The carrying amounts of accounts receivable, notes receivable, accounts payable, accrued liabilities, and notes payable approximate fair value.

Goodwill and Other Intangible Assets - In June 2001, the Financial Accounting Standards Board issued SFAS No.141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets". SFAS No. 141 requires the use of the purchase method of accounting for all business combinations initiated after June 30, 2001. It also provides guidance on purchase accounting related to the recognition of intangible assets. SFAS No. 142 requires that goodwill and identifiable acquired intangible assets with indefinite useful lives shall no longer be amortized, but tested for impairment annually and whenever events or circumstances occur indicating that goodwill might be impaired. SFAS No. 142 also requires the amortization of identifiable assets with finite useful lives. Identifiable acquired intangible assets, which are subject to amortization, are to be tested for impairment in accordance with SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets."

The Company elected to adopt the provisions of SFAS No. 142 as of July 1, 2001, and identified its reporting units (components) to be two separate units (Arraid and Excel), which continue to make up the Company's Data Storage segment. In May of 2002 the Company added its ATSI unit and, effective June 30, 2006, it added its StarTrak unit. The Company determines the carrying value of each reporting unit by assigning assets and liabilities, including the existing goodwill and intangible assets, to the reporting units. Upon adoption of SFAS No. 142, amortization of goodwill recorded for business combinations consummated prior to June 30, 2001 ceased, and intangible assets acquired prior to June 30, 2001 that did not meet the criteria for recognition apart from goodwill under SFAS No. 141 were reclassified to goodwill. In connection with the adoption of SFAS No. 142, the Company was required to perform a transitional goodwill impairment assessment. The annual goodwill impairment assessment involves estimating the fair value of the reporting unit and comparing it with the carrying amount. If the carrying amount of the reporting unit exceeds its fair value, additional steps are followed to recognize a potential impairment loss. Calculating the fair value of the reporting units requires significant estimates and assumptions by management. The Company estimates the fair value of its reporting units by applying third-party market value indicators to the reporting unit's projected earnings before interest, taxes, depreciation and amortization. The Company completed its impairment tests with no adjustment to the carrying value of its goodwill as of June 30, 2006.

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Intangible assets consist of goodwill, the excess of purchase price over fair value of net assets acquired in connection with the acquisitions of its wholly owned subsidiaries, and other intangible assets, including cost of licenses, patents, developed software, etc. Prior to fiscal year 2002, goodwill was being amortized over 15 years. Commencing in year 2002, the Company adopted SFAS 142 and ceased amortizing goodwill balances over a specific period pursuant to SFAS 142. However, per Company policy, goodwill balances are reviewed at least annually to determine appropriateness of valuation and presentation based upon anticipated cash flows. See Impairment of Intangibles and Other Long-lived assets below for additional discussion of valuation for Intangible Assets.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

The following is a summary of Goodwill, net:

	RFID Technology	Data Storage	StarTrak	Total
	-----	-----	-----	-----
Balance as of June 30, 2005 & 2004	5,076,700	279,600	-	5,356,300
Goodwill related to acquisition	-	-	15,060,800	15,060,800
	-----	-----	-----	-----
Balance as of June 30, 2006	\$ 5,076,700	\$ 279,600	\$15,060,800	\$20,417,100
	=====	=====	=====	=====

The Company completed the acquisition of StarTrak effective June 30, 2006. The purchase price, considering the 5 million Class A Common Shares issued at closing (valued at \$3,485,000), 8.2 million Class A shares to be issued upon shareholder approval (valued at \$5,715,400 on June 30, 2006), StarTrak net liabilities assumed of \$5,425,800 and the related costs of the acquisition of \$434,500, was valued at of \$15,060,800. The Company has engaged an independent consultant for valuation services related to FASB 141 required disclosures of the allocation of the purchase price paid to the assets acquired and liabilities assumed by balance sheet caption. We believe the allocation will focus primarily on intangible assets other than goodwill. The consultant's report has not been received by the date of this audit report and therefore the entire transaction value is presented as goodwill. The consultant's report is expected in the next few weeks when the appropriate allocation of the purchase price will be completed.

Other intangible assets, excluding any allocations required due to the StarTrak acquisition, consist of the following:

	Amortization Period (in years)	Gross Carrying Value	Accumulated Amortization	Net Other Intangible Assets
	-----	-----	-----	-----
As of June 30, 2005				
Patents license	3	\$ 51,900	\$ (51,900)	\$ -
Manufacturing license	6	500,000	(256,900)	243,100



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Software development	5	600,000	(370,000)	230,000
Technology license	5	90,000	(2,400)	87,600
		-----	-----	-----
Total Other Intangible Assets		\$1,241,900	\$ (681,200)	\$ 560,700
		=====	=====	=====
As of June 30, 2006				
Patents license	3	\$ 51,900	\$ (51,900)	\$ -
Manufacturing license	6	500,000	(340,200)	159,800
Software development	5	600,000	(490,000)	110,000
Technology license	5	90,000	(20,500)	69,500
		-----	-----	-----
Total Other Intangible Assets		\$1,241,900	\$ (902,600)	\$ 339,300
		=====	=====	=====

The amortization expenses for aggregate other intangible assets for the fiscal years ended June 30, 2006 and 2005 were \$221,500 and \$222,900, respectively.

The following table summarizes the estimated amortization charges related to the other intangible assets as of June 30, 2006, excluding any allocations required due to the StarTrak acquisition, which will be determined after an independent consultant has completed valuation pursuant to FASB 141:

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### June 30th Amount

2007	\$	211,400
2008		94,100
2009		18,100
2010		15,600
----		-----
	\$	339,200
		=====

Net Assets Held For Sale - At June 30, 2006 and 2005, the "net assets held for sale" consist of the remaining restaurant equipment assets. The Company is continuing to sell the equipment in small quantities and believes the carrying value is supportable under the small unit sales. "Net assets held for sale" at June 30, 2006 and 2005 are valued at the lower of cost or market.

Income Taxes - The Company accounts for income taxes under the asset and liability method, which requires recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement basis and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse.

Use of Estimates - The preparation of the Company's financial statements in conformity with accounting principles generally accepted in the United

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States of America requires the Company's management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Actual results could differ from those estimates.

The Company makes significant assumptions concerning the realizability of its goodwill and other intangible assets, warranty reserves, percentage of completion method of accounting, deferred tax assets, investments and assets held for sale. Due to the uncertainties inherent in the estimation process and the significance of these items, it is at least reasonably possible that the estimates in connection with these items could be further materially revised within the next year.

Impairment of Other Long-Lived Assets - The Company performs an assessment for impairment whenever events or changes in circumstances indicate that the carrying amount of a long-lived asset may not be recoverable. If the net carrying value of the asset exceeds estimated future net cash flows, then impairment is recognized to reduce the carrying value to the estimated fair value. No impairment to Other Long-Lived Assets was recorded during fiscal years ended June 30, 2006 or 2005.

Revenue Recognition - The Company recognizes revenue from computer data storage sales, net of anticipated returns, at the time products are shipped to customers, or at the time service is provided. Revenues from material long-term contracts that extend over a reporting period in both the Computer Data Storage segment and the RFID Technology segment are recognized on the percentage-of-completion method for individual contracts, commencing when significant costs are incurred and adequate estimates are verified for substantial portions of the contract to where experience is sufficient to estimate final results with reasonable accuracy. Revenues are recognized in the ratio that costs incurred bear to total estimated costs. Changes in job performance, estimated profitability and final contract settlements would result in revisions to costs and income, and are recognized in the period in which the revisions are determined.

Contract costs include all direct materials, subcontracts, labor costs and those direct and indirect costs related to contract performance. General and administrative costs are charged to expense as incurred. At the time a loss on a contract becomes known, the entire amount of the estimated ultimate loss is accrued.

Loss Per Share - The loss per share ("EPS") is presented in accordance with the provisions of Statement of Financial Accounting Standards (SFAS) No. 128, Earnings Per Share. Basic EPS is calculated by dividing the income or loss available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Basic and diluted EPS were the same for fiscal 2006 and 2005, as the Company had losses from operations and therefore the effect of all potential common stock equivalents is antidilutive (reduces loss per share). Stock options representing 14,302,500 shares of Class A Common Stock were outstanding at year-end with exercise prices ranging between \$0.37 and \$2.75. The weighted average exercise price for all outstanding

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options was \$0.79. Stock warrants representing 7,191,700 Class A Common Shares were outstanding at year-end with exercise prices ranging between \$0.50 and \$2.00. The weighted average exercise price was \$0.93.

At June 30, 2006, there were 3,122,900 shares of Series A Convertible Preferred Stock and 75,000 shares of Series B Convertible Preferred Stock outstanding. The Series A Convertible Preferred shares are convertible into Class A Common shares at a ratio of 3 shares of common stock for each share of Series A Preferred. The Series B Convertible Preferred shares are convertible into Class A Common shares at a ratio of 13 shares of common stock for each share of Series B Preferred. If the preferred shares had been converted into common shares at June 30, 2006, there would have been an additional 10,344,700 Class A Common shares outstanding.

Stock-Based Compensation - At June 30, 2006 and 2005, the Company had stock-based compensation plans accounted for under the recognition and measurement principles of Accounting Principles Board Opinion ("APBO") No. 25 "Accounting for Stock Issued to Employees," and related interpretations, as more fully described in Note 12. Pro forma information regarding the impact of stock-based compensation on net income and earnings per share is required by SFAS No. 123 "Accounting for Stock-Based Compensation," and SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure." Such pro forma information, determined as if the Company had accounted for its employee stock options under the fair value recognition provisions of SFAS No. 123, is illustrated in the following table:

	Year Ended June 30, 2006	2005
	-----	-----
Net loss attributable to Common Shareholders	\$ (4,591,900)	\$ (4,311,700)
Deduct: Total stock-based compensation expense determined under fair value-based method for all awards, net of related tax effects	(1,881,900)	(255,600)
	-----	-----
Pro Forma Net Loss	\$ (6,473,800)	\$ (4,567,300)
	=====	=====
Loss per Share		
Basic and Diluted, as Reported	\$ (0.16)	\$ (0.17)
	=====	=====
Pro Forma Basic and Diluted	\$ (0.21)	\$ (0.18)
	=====	=====
Weighted Shares Outstanding, Basic and Diluted	29,106,100	25,355,500
	=====	=====
Pro Forma Weighted Shares Outstanding, Basic and Diluted	30,657,771	25,590,800
	=====	=====

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## ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

The fair value for these options was estimated as of the date of grant using a Black-Scholes option-pricing model with the following weighted average assumptions for all options granted.

	Year Ended June 30,	
	2006	2005
	-----	-----
Volatility	27%	30%
Risk free interest	4.5%	3.5%
Expected dividends	none	none
Expected term in years	5-10	10

Concentrations of Credit Risks and Significant Customers - The Company sells products and extends credit based on an evaluation of the customer's financial condition, generally without requiring collateral. Exposure to losses on receivables is principally dependent on each customer's financial condition. The Company monitors its exposure for credit losses and maintains allowances for anticipated losses.

The RFID Technology segment utilizes various domestic suppliers for purchases of materials and parts used to manufacture its products. Due to the advantage of volume manufacturing, one domestic supplier represented approximately 34% of those purchases for fiscal year ended June 30, 2005. No supplier accounted for 10% or more of those purchases for fiscal year ended June 30, 2006.

The Company anticipates that due to the advantages of volume manufacturing, a concentration of vendor purchases may occur in the RFID Technology segment; however, additional suppliers are readily available at competitive pricing levels. The Company does not foresee any future significant shortages or substantial price increases that cannot be recovered from its customers.

No Data Storage customer accounted for more than 10% of the segment sales in fiscal year 2006 and one Data Storage customer account for 10.2% of the segment sales in fiscal year 2005. Four state governments accounted for substantially all of the RFID Technology segment's revenues for fiscal year 2006, while two state governments accounted for substantially all of the revenues for fiscal year 2005.

The largest accounts receivable balance in the Data Storage segment represented 15.6% and 8.9% of consolidated accounts receivable (41.6% and 11.7% of Data Storage receivables) at June 30, 2006 and 2005, respectively. The largest accounts receivable balance in the RFID Technology segment at June 30, 2006 represented 6.9% of consolidated accounts receivable (56.7% of RFID receivables) compared to 13.3% (61% of RFID receivables) at June 30, 2005. The largest accounts receivable in the Wireless Asset Management segment amounted to 17.1% of consolidated receivables and 32.6% of the Wireless Asset Management segment receivables.

Segment Information - SFAS No. 131, "Disclosure About Segments of an Enterprise and Related Information," defines operating segments as

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components of a company about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Company had identified RFID Technology and Data Storage as the continuing operating segments of the Company for fiscal year 2006 and 2005. The acquisition of StarTrak Systems, LLC, effective June 30, 2006 added an additional reporting segment for future reporting periods that is referred to as Wireless Asset Management. All assets related to previously disclosed segments have either been sold or have been classified as "net assets held for sale" at June 30, 2006 and 2005. See Note 14 for further information related to the Company's operating segments.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Recent Accounting Pronouncements - In November 2004, the FASB issued Statement No. 151 ("SFAS 151"), "Inventory Cost - An Amendment of ARB No. 43, Chapter 4." SFAS 151 clarifies accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. It requires that those items be recognized as current-period charges regardless of whether they meet the criterion of abnormal. Currently, we do not have any inventory items that fall into the classifications discussed; accordingly, adoption of SFAS 151 does not have a significant impact on our financial statements.

In December 2004, the FASB issued Statement No. 153 ("SFAS 153"), "Exchanges of Nonmonetary Assets - An Amendment of APB Opinion No. 29." SFAS 153 amends APB Opinion No. 29 to eliminate the exception for nonmonetary exchanges of similar productive assets and replaces it with a general exception for exchanges of nonmonetary assets that do not have commercial substance. A nonmonetary exchange has commercial substance if the future cash flows of the entity are expected to change significantly as a result of the exchange. Adoption of SFAS 153 does not have a significant impact on our financial statements.

In December 2004, the FASB issued Statement No. 123R ("SFAS 123R"), "Share-Based Payment." This Statement focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. It requires that the fair-value-based method be used to account for these transactions for all public entities. This Statement is effective for small business issuers for the first reporting period after December 15, 2005, subject to additional extensions granted by the SEC, and will affect any stock-based compensation for options issued after that date, or not vested as of that date. The effect of the adoption should not be significantly different than provided in the previously reported proforma presentation in the notes to the consolidated financial statements.

In May 2005, the FASB issued Statement No. 154 ("SFAS 154"), "Accounting Changes and Error Corrections". SFAS 154 replaces APB Opinion No. 20, (APB 20") and SFAS No. 3 to require retrospective application of changes to all prior period financial statements so that those financial statements are presented as if the current accounting principle had always been applied. APB 20 previously required most voluntary changes in accounting principles to be recognized by including in net income of the period of change the cumulative effect of changing to the new accounting principle. In addition SFAS 154 carries forward without change the guidance contained in APB 20 for reporting a correction of an error in previously issued financial statements and a change in accounting

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estimate. SFAS 154 is effective for changes and corrections made after January 1, 2006, with early adoption permitted. The Company is currently not contemplating changes that would be impacted by SFAS 154.

### 2. LIQUIDITY AND GOING CONCERN

The Company incurred significant losses and negative cash flows from operations during fiscal year ended June 30, 2006 and in prior fiscal years, and anticipates additional losses and negative cash flows in early fiscal year 2007. These factors, as well as the uncertain conditions that the Company faces regarding its ability to secure significant contracts for the TSI PRISM installations, creates an uncertainty about the Company's ability to finance its operations and remain a going concern. Although management cannot assure that future operations will be profitable or that additional debt and/or equity capital will be raised, management believes cash balances at June 30, 2006 of approximately \$1,155,500 and the \$410,400 of additional equity capital raised subsequent to the end of fiscal 2006 through the sale of stock, and the additional long-term debt financing anticipated to close shortly, will provide adequate capital resources to maintain the Company's net cash requirements for the next year. However, if additional working capital is required and not obtained through long-term debt, equity capital or operations, it could adversely affect future operations. Management has historically been successful in obtaining financing and has demonstrated the ability to implement a number of cost-cutting initiatives to reduce working capital needs. The Company requires and continues to pursue additional capital for growth and strategic plan implementation. Accordingly, the accompanying consolidated financial statements have been prepared assuming the Company will continue to operate and do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

### 3. NOTES RECEIVABLE

Notes receivable at June 30, 2006 and 2005 consisted of the following:

	2006	2005
TSIN Board of Directors	\$ 29,600	\$ 80,000
Notes receivable - other	2,000	10,200
	31,600	90,200
Less - allowance for uncollectible	-	(2,200)
	\$ 31,600	\$ 88,000

At June 30, 2006 and 2005, Notes - "TSIN Board of Directors" consisted of notes receivable related to advances made to TSIN in fiscal year ended June 30, 2005 to assist the newly elected TSIN board of directors in obtaining legal representation. The new board required legal representation since the previous board was attempting to stop the new board from assuming their responsibilities. The notes incur interest at 9% and are due on demand. During fiscal 2006, the Company received

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payments on the notes of approximately \$50,000. At June 30, 2006, the TSIN Board of Directors had filed for reimbursement from TSIN under the Directors indemnification provisions of the Articles of Incorporation, Bylaws of TSIN and corporate laws of the State of Nevada. The new board is awaiting payment so the funds received can be used to repay the notes.

### 4. INVENTORIES

Inventories consist of the following at June 30:

	2006	2005
Raw materials and purchased parts	\$ 3,251,000	\$ 2,011,900
Work-in-progress	98,100	106,000
Finished goods	198,700	99,300
	3,547,800	2,217,200
Less reserves for obsolescence	(403,900)	(314,600)
	\$ 3,143,900	\$ 1,902,600

### 5. PROPERTY, PLANT AND EQUIPMENT

Property, Plant and Equipment consist of the following at June 30:

	2006	2005
Machinery and equipment	\$ 351,500	\$ 202,600
Furniture and office equipment	608,000	586,800
Marketing site equipment	50,000	250,000
Leasehold improvement	9,700	9,700
	1,019,200	1,049,100
Less accumulated depreciation	(816,900)	(775,600)
Net book value	\$ 202,300	\$ 273,500

Related depreciation expense for the years ended June 30, 2006 and 2005, was \$161,600 and \$126,900, respectively.

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## ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

### 6. NET ASSETS HELD FOR SALE

Several years ago, the Company formally adopted a plan to sell all business segment assets not related to information technology. The only remaining assets presented as "net assets held for sale" at both June 30, 2006 and 2005 related to restaurant equipment assets.

### 7. LINE OF CREDIT AND NOTES PAYABLE

At June 30, 2006, the Company has a \$2,000,000 outstanding balance,

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\$1,000,000 presented in current liabilities as Credit Line and \$1,000,000 presented as Notes payable - long term, under a \$2.0 million line of credit Agreement. The Agreement is with a private trust, initially entered into in June 2002, for a credit line of \$1.3 million. The Agreement has been amended various times since June 2002 with the last amendment in June 2006. Under the current amended agreement, which expires on July 1, 2007, the Company must maintain a minimum outstanding balance under the line of \$1.5 million through July 1, 2007 and pay interest on the outstanding balance at a rate of prime plus 2% (10.25% at June 30, 2006). Under the Agreement, the lender has the unilateral right to reduce the line of credit Agreement to \$1.5 million, at which time the minimum outstanding balance under the Agreement reduces from \$1.5 million to \$1.0 million. At June 30, 2006 the Company was fully drawn under the line of credit Agreement. At June 30, 2005, the Company had an outstanding balance of \$829,500 under the Agreement. Interest payments made under the Agreement amount to \$89,500 and \$34,700 in fiscal years ended June 30, 2006 and 2005, respectively.

Notes payable at June 30, 2006 and 2005 consist of the following:

	2006	2005
	-----	-----
Notes payable - TSI Acquisition	\$ 314,100	\$ 314,100
Notes payable - Bank	1,000,000	829,500
Notes payable - StarTrak Acquisition	1,733,300	-
Notes payable - Other	507,000	-
	-----	-----
Notes payable	3,554,400	1,143,600
Less current portion	(875,300)	-
	-----	-----
Notes payable - long term	\$ 2,679,100	\$ 1,143,600
	=====	=====

The Notes payable - TSI Acquisition primarily represent payables assumed as an obligation under the TSI acquisition agreement. The balance at June 30, 2006 and 2005 is payable to TSIN upon ATSI achieving a net profit of \$1 million in any twelve-month period ending on June 30th. The Notes payable - TSI Acquisition balance of \$314,100 at June 30, 2006 and 2005 has been reduced by approximately \$10,500 for costs incurred and paid by the Company that had been indemnified by TSIN in the acquisition agreement.

Notes payable - StarTrak Acquisition represent notes assumed in the acquisition and include a \$1.5 million non interest bearing note payable to Tenix Holding, Inc. (a prior investor in StarTrak) due December 31, 2007 that has been discounted to \$1.365 million due to the non interest bearing nature of the note, and \$368,300 of notes due on demand (expected to be repaid in the quarter ended December 31, 2006) that bear interest at 7%.

Notes payable - Other includes a \$257,000 non interest bearing note due to an investment banker involved in the StarTrak acquisition (\$150,000 of which was paid August 31, 2006 and \$107,000 is due by January 31, 2007 and may, if approved by shareholders, be paid in stock) and a \$250,000 demand note bearing interest at 12% and due to the Company's Chief Executive Officer.



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## ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

### 8. CONTRACTS IN PROGRESS

The Company had one fixed price contract in progress at June 30, 2006 and 2005, within the RFID Technology segment, for the installation of a TSI PRISM system. Billings in excess of costs and estimated earnings as of June 30, 2006 and 2005 consist of the following:

	June 30, 2006	June 30, 2005
	-----	-----
Costs incurred on uncompleted contract	\$ 97,100	\$ 34,100
Gross profit earned to date	19,900	1,700
	-----	-----
Revenues earned to date	117,000	35,800
Less: billings to date	(160,500)	(40,000)
	-----	-----
Billings in excess of cost and estimated earnings on uncompleted contracts	\$ (43,500)	\$ (4,200)
	=====	=====

### 9. INCOME TAXES

A reconciliation of anticipated statutory rates is as follows:

	2006	2005
	-----	-----
Statutory Rate	34%	34%
State income taxes, net of Federal income tax benefit	5%	5%
Increase (reduction) in valuation allowance related to net operating loss carry-forwards and change in temporary differences	-39%	-39%
	-----	-----
	0%	0%
	=====	=====

The components of the net deferred tax asset (liability) recognized as of June 30, 2006 and 2005, are as follows:

	2006	2005
	-----	-----
Deferred tax assets (liabilities):		
Net operating loss, capital loss carryforwards, amortization of intangibles	\$ 14,498,000	\$ 12,827,000
Property, plant and equipment	22,000	(49,000)
Other timing differences	23,000	62,000
Less: valuation allowance	(14,543,000)	(12,840,000)
	-----	-----
Net deferred tax	\$ -	\$ -
	=====	=====

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A valuation allowance is recognized if it is more likely than not that some or all of the deferred income tax assets will not be realized. A valuation allowance is used to offset the related income tax assets due to uncertainties of realizing the benefits of certain net operating loss and tax credits. The valuation allowance reflects a 100% reserve for all years reported above. At June 30, 2006, the Company had net operating loss and capital loss carryforwards for Federal tax purposes of approximately \$37,527,000. The loss carryforwards, unless utilized, will expire from 2007 through 2025.

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### 10. RELATED PARTY TRANSACTIONS

At June 30, 2006, the Company had a line of credit agreement with a trust controlled by Donald Anderson, a member of the Company's Board of Directors. In addition, the Company also had a demand note payable to Mr. Robert Kauffman, CEO of the Company, in the amount of \$250,000. See Note 7 for additional discussion of both the line of credit agreement and the note due to Mr. Kauffman.

During 2006, as more fully described in Note 12, Shareholders' Equity, the Company raised approximately \$2.3 million in private offerings to accredited investors, with twenty-two percent being attributable to insiders.

### 11. COMMITMENTS AND CONTINGENCIES

Leases - The Company leases certain facilities under non-cancelable operating lease agreements that expire through fiscal year 2009. Future minimum payments under non-cancelable operating leases at June 30, 2006 are as follows:

Year Ended June 30, -----	Operating Leases -----
2007	\$ 412,700
2008	197,200
2009	105,200
2010	-
2011	-
	-----
	\$ 715,100
	=====

Rent expense related to these operating leases totaled approximately \$340,400 and \$342,600 for the years ended June 30, 2006 and 2005, respectively.

Legal Proceedings - The Company is a party to litigation that relates to the acquisition, in May of 2002, of substantially all the assets of Technology Systems International, Inc., a Nevada Corporation, to litigation arising out of Carolina Casualty Insurance Company's failure to pay a claim (relating to the TSIN litigation) pursuant to a Directors and Officers insurance policy, and to litigation arising from an expired property lease between the Company's subsidiary, Arraid, Inc., and Arraid Property L.L.C., an Arizona limited liability company. The actions are more fully described below:

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On January 30, 2003, a shareholder of TSIN filed a derivative suit naming as defendants the Company and its wholly owned subsidiary, Alanco/TSI PRISM, Inc. The venue for this action is the Arizona Superior Court in and for Maricopa County, Arizona, as case number CV2003-001937. The complaint sets forth various allegations and seeks damages arising out of the Company's acquisition of substantially all of the assets of TSIN. This derivative suit was terminated and the action converted into a direct action by TSIN by stipulation and court order in July 2003.

TSIN is currently in Chapter 7 bankruptcy. The Chapter 7 Trustee failed to prosecute the action timely and the state court dismissed the action for lack of prosecution, but allowed the Trustee to restart the action, which the Trustee has done as case number CV2006-007398. The Company is seeking its attorney's fees with respect to the dismissed action, and will appeal the court's order allowing the Trustee to restart the action. The Company's management, in consultation with legal counsel, believes the plaintiff's claims are without merit and the Company will continue to aggressively defend the action. In addition, the Company will pursue reimbursement of legal expenses incurred from TSIN.

The Company is the plaintiff in a lawsuit (U.S. District Court No. CV-04-0789-PHX-DGC) arising out of Carolina Casualty Insurance Company's ("Carolina") failure to pay a claim regarding the TSIN litigation, that the Company made pursuant to its Directors and Officers Insurance Policy ("Policy") issued by Carolina. The Company seeks payment for its legal expenses in the TSIN litigation and reimbursement of legal fees incurred in the Carolina litigation. The District Court granted summary judgment in favor of Carolina and the Company has filed an appeal with the Ninth Circuit Court of Appeals.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

On July 18, 2003, Arraid Property L.L.C., an Arizona limited liability company ("Arraid LLC"), filed a complaint in the Arizona Superior Court in and for Maricopa County, Arizona (case number CV 2003-13999) against the Company and its wholly owned subsidiary, Arraid, Inc., alleging breach of lease and seeking substantial monetary damages. The suit relates to an expired lease agreement for property previously leased by Arraid. Following a trial, the Court found in favor of Arraid LLC against the Company with respect to certain factual findings resulting in damages owed by the Company in an amount currently undecided, but anticipated to be less than \$35,000. The prevailing party, which has not yet been determined by the court, will likely be awarded some attorney' fees. Based upon a determination of the amount of any final award against the Company, the Company's management, in consultation with legal counsel, will determine whether to appeal the decision of the court.

The Company may also, from time to time, be involved in litigation arising from the normal course of business. As of June 30, 2006, there was no such litigation pending deemed material by the Company.

#### 12. SHAREHOLDERS' EQUITY

Preferred Shares - During the fourth quarter of the fiscal year ended 2003, the Company allocated 5,000,000 of the 25,000,000 authorized shares of the Company's Preferred Stock to be known as Series A Convertible Preferred Stock ("Series A") and issued 2,248,400 of Series A shares in a transaction with accredited investors. The Company exchanged a Series A share and a warrant to purchase a share of the Company's Class A Common

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Stock at \$.50 ("Warrant"), for two shares of Class A Common Stock ("Common") and \$.50. The transaction recorded at June 30, 2003 was valued at \$2,833,000. In July 2003, an additional 261,000 Series A shares, plus applicable warrants, valued at \$328,900 were issued to complete the private offering. In April 2004, one of the holders of the Series A shares elected to convert 168,000 preferred shares into 504,000 shares of Class A Common Stock.

Holder of Series A Preferred Stock are entitled to receive, when declared by the Board of Directors, out of funds and assets of the Company legally available therefore, an annual dividend of 12% per annum, paid in kind semi-annually, based upon a per share value of \$1.50 for purposes of such dividend payment. Dividends shall accrue and be cumulative from the date of issue. The Company issued 341,700 shares and 304,400 shares representing "in kind" dividends to the holders of Series A shares in fiscal 2006 and 2005, respectively, with corresponding values of approximately \$512,500 and \$456,600. The Series A shares are convertible by the holder at any time into three shares of the Company's Class A Common Stock. The Company may redeem the Series A Preferred Shares for \$1.50 per share, provided the Common stock achieves a trading value in excess of \$2.00 for twenty consecutive trading days and meets minimum daily trading volume requirements. At June 30, 2006 and 2005, there were 3,122,900 and 2,781,200 shares of Series A Convertible Preferred Stock outstanding, respectively.

During fiscal 2002, the Company allocated 500,000 of the authorized shares of the Company's Preferred Stock to be known as Series B Convertible Preferred Stock ("Series B"), and in a transaction with an accredited investor, the Company issued 50,000 shares of Series B at \$10.00 per share and 500,000 warrants to purchase Common Stock at an exercise price of \$1.00 per share for a value received of \$500,000 (\$487,300 net of related expenses). The preferred shares are each convertible into thirteen (13) shares of Common Stock. Holders of shares of the Company's Series B Preferred Stock shall be entitled to receive, when declared by the Board of Directors, out of funds and assets of the Company legally available therefore, an annual dividend of 10% per annum based upon a per share value of \$10 for purposes of such dividend payment. Dividends shall accrue, be cumulative from the date of issue and may be paid "in kind." Dividends on Series B Preferred Shares paid "in-kind" during 2006 and 2005 amounted to 7,000 and 6,500 Preferred Shares with values of approximately \$70,200 and \$64,500, respectively. At June 30, 2006 and 2005, there were 75,000 and 68,000 shares of Series B Convertible Preferred Stock outstanding, respectively.

Both the Series A and Series B are characterized as "restricted securities" under federal securities laws as they were acquired from the Company in a transaction not involving a public offering and that under such laws and applicable regulations such shares may be resold without registration under the Securities Act of 1933, as amended, only in certain limited circumstances.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Common Shares - The authorized capital stock of the Company consists of 75,000,000 shares of Class A Common Stock (reduced from the previously authorized 100,000,000 shares), each entitled to one vote per share, and 25,000,000 shares of Class B Common Stock, each entitled to one-one hundredth (1/100th) of one vote per share. No Class B Common Stock has been issued and none was outstanding at June 30, 2006 and 2005.

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The Company issued a total of 11,473,500 shares of Class A Common Stock in fiscal year 2006. The issued shares were comprised of 2,100,000 shares issued in connection with the exercise of employee stock options and warrants, resulting in proceeds of \$1,235,000; 383,500 shares issued to outside vendors as payment for services rendered valued at \$245,400; 3,990,000 shares issued in connection with private offerings; and 5,000,000 shares in June 2006 in connection with the Company's acquisition of StarTrak Systems, LLC.

The 2006 private offerings included the January 2006 sale to an institutional investor of 1,500,000 units consisting of one share of Class A Common Stock together with a 3-year warrant to purchase one-half share of the Company's Common Stock at a price of \$.85 per share ("Unit") for a unit sale price of \$.60. The Company received \$830,000, net of commission, from the offering. The Company granted additional warrants to purchase 52,500 shares of its Common Stock on terms identical to those granted in the private offering as commissions related to the offering. In addition, in April 2006 the Company completed the sale, in a private offering to a trust beneficially owned by a Director of the Company, of 820,000 units for \$500,200. The units consisted of one share of Class A Common Stock, together with a warrant to purchase one share at a price of \$.65 per share. In June 2006, the Company completed two additional private offerings, the first to three institutional investors for a total of 835,000 units consisting of one share of Class A Common Stock together with a 3-year warrant to purchase one-half share of the Company's Common Stock at a price of \$.85 per share ("Unit"), for a unit sale price of \$.60. The Company received \$479,000, net of commission, from the offering. The second June 2006 offering consisted of 835,000 units to an institutional investor, each unit composed of one share of Class A Common Stock together with a 3-year warrant to purchase one-half share of the Company's Common Stock at a price of \$.85 per share ("Unit"), for a unit sale price of \$.60. The Company received \$464,900, net of commission, from the offering. The Company also granted warrants to purchase 29,225 shares of Common Stock on terms identical to those granted in the private offering as commissions related to the offering. Nasdaq listing fees paid during fiscal year 2006 amounted to \$44,100.

Effective June 30, 2006, the Company acquired StarTrak Systems, LLC, a Delaware limited liability company ("StarTrak"). The transaction was structured as a merger between a newly formed subsidiary of the Company and StarTrak, resulting in the Company owning all of the post-transaction membership interests in StarTrak and the previous StarTrak members receiving 5,000,000 shares of the Company's Class A common stock and the right to receive in the future either cash or additional shares of the Company's Class A common stock. The 5,000,000 initial shares issued to the StarTrak members were valued at \$3,485,000. Potential additional shares to be issued to the StarTrak members will be presented for approval as a proposal to the Alanco's shareholders at the 2006 Annual Shareholders Meeting.

During fiscal year 2005, the Company issued a total of 3,447,400 shares of Class A Common Stock. Of those shares, 3,113,200 were issued in connection with the exercise of employee stock options and warrants, resulting in proceeds of \$2,001,700. In addition, five-year warrants to purchase 75,000 shares at \$.90 per share (valued at \$23,200) were granted in connection with an amendment to the Company's line of credit agreement and five-year warrants to purchase 500,000 shares at \$1.00 per share (valued at \$90,000) were granted in connection with a technology licensing agreement. Shares issued to outside vendors by the Company as payment for services rendered totaled 334,200 shares and were valued at \$303,200. Nasdaq listing fees, associated with listing the additional shares in fiscal year 2005, amounted to \$38,200.

## ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

In August, 2005, the Company received notification from NASDAQ indicating that due to the failure of the Company to maintain the minimum \$1.00 bid price per share requirement, the Company's securities were subject to delisting from NASDAQ. In accordance with Marketplace Rule 4310(c) (8) (D), the Company had 180 days, or until January 31, 2006, to comply with the Rule. The minimum bid price requirement was not met by the date specified, and in accordance with Marketplace Rule 4310(c), NASDAQ officials determined the Company met the NASDAQ Capital Market initial listing criteria except for the bid price requirement and notified the Company that it had been granted an additional 180 calendar days (until July 31, 2006) to meet the \$1.00 minimum bid price requirement. In August, 2006, the Company received notification from NASDAQ indicating that it had not regained compliance with the minimum \$1.00 bid price per share requirement and that the Company's securities would be delisted. The Company elected to appeal the NASDAQ Staff delisting determination and an oral hearing before the NASDAQ Listing Qualifications Panel ("Panel") was scheduled for September 14, 2006. There can be no assurance that the Panel will grant the Company's request for continued listing. Pending a decision by the Panel, the Company's Common Stock will remain listed on the NASDAQ Capital Market.

The Company's Board of Directors have shareholder authorization to effect, if the Board believes necessary, up to a 1 for 10 reverse stock split at a future date through December 31, 2008. As of September 27, 2006, no split was effected.

Warrants - As of June 30, 2006, the Company had 7,191,726 warrants outstanding with a weighted average exercise price of \$1.09. The life of the outstanding warrants extends from May 2007 through April 2016. The following is a table of activity related to all warrants.

	Number of Shares	Weighted Average Exercise Price \$
	-----	-----
WARRANTS OUTSTANDING, June 30, 2004	6,154,400	1.01
Granted	1,430,000	0.96
Exercised	(2,544,400)	0.61
Canceled/Expired	(35,000)	1.54
	-----	-----
WARRANTS OUTSTANDING, June 30, 2005	5,005,000	1.09
Granted	4,336,726	0.74
Exercised	(1,850,000)	0.61
Canceled/Expired	(300,000)	0.70
	-----	-----
WARRANTS OUTSTANDING, June 30, 2006	7,191,726	1.09
	=====	=====

## ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Details relative to the 7,191,726 outstanding warrants at fiscal 2006 year end are outlined below.

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Outstanding Warrants

Date of Grant	Number of Shares	Exercise Price \$	Date of Expiration	Purpose of Issuance
5/16/2002	500,000	\$1.00	5/16/2007	(1)
6/19/2002	100,000	\$0.87	6/19/2007	(2)
9/4/2002	25,000	\$1.00	9/4/2007	(3)
11/26/2002	50,000	\$0.75	10/15/2007	(3)
10/31/2003	50,000	\$0.60	10/31/2008	(2)
4/18/2004	700,000	\$2.00	8/2/2009	(5)
3/22/2005	75,000	\$0.90	3/22/2010	(2)
3/23/2005	500,000	\$1.00	3/23/2010	(3)
6/29/2005	855,000	\$0.95	6/29/2010	(6)
8/31/2005	700,000	\$1.00	6/9/2007	(7)
11/16/2005	1,150,000	\$0.50	11/16/2008	(6)
1/16/2006	802,500	\$0.85	1/16/2009	(8)
4/26/2006	820,000	\$0.65	4/25/2016	(9)
6/2/2006	417,501	\$0.85	6/2/2009	(10)
6/15/2006	446,725	\$0.85	6/15/2009	(10)
-----				
Total Warrants Outstanding @ 6/30/2006	7,191,726			
=====				

Warrants exercised in fiscal 2006 and 2005, were 1,850,000 and 2,544,400, respectively. Exercise of these warrants generated approximately \$1,135,000 in fiscal 2006 and \$1,557,200 in fiscal 2005.

Stock Options - As of June 30, 2006, the Company had a total of 14,302,500 stock options outstanding with a weighted average exercise price of \$0.79. Of these options, 11,926,500 are exercisable at 2006 fiscal year end. The tables below, as well as the narrative following, provide further information regarding the Company's stock options.

The following is a table of activity of all options:

	Number of Shares	Weighted Average Exercise Price
-----		
OPTIONS OUTSTANDING, June 30, 2004	\$ 8,409,000	\$ 0.86
Granted	640,000	1.05
Exercised	(568,750)	0.78
Canceled/Expired	(673,750)	1.35
-----		
OPTIONS OUTSTANDING, June 30, 2005	7,806,500	\$ 0.84
Granted	7,620,000	0.75
Exercised	(250,000)	0.40

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Canceled/Expired	(874,000)	0.89
OPTIONS OUTSTANDING, June 30, 2006	14,302,500	\$ 0.79

For all options granted during fiscal years 2006 and 2005, the option price was not less than the market price, as defined in the stock option plans, of the Company's Common Stock on the grant date. At June 30, 2006,

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

options for 11,926,500 shares were exercisable and options for the remaining shares become exercisable within the next four years. If not previously exercised, options outstanding at June 30, 2006 will expire as follows:

Calendar Year of Expiration	Number of Shares	Weighted Average Exercise Price \$
2008	1,120,000	\$ 0.43
2009	772,500	1.15
2010	320,000	1.71
2011	5,860,000	0.76
2012	1,405,000	0.97
2013	952,500	0.40
2014	1,907,500	0.92
2015	1,910,000	0.76
2016	55,000	0.64
	14,302,500	\$ 0.79

Additional information about outstanding options to purchase the Company's Common Stock as of June 30, 2006 is as follows:

Exercise Price	Options Outstanding			Options Exercisable	
	Number of Shares	Weighted Avg. Remaining Contractual Life (in years)	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
\$0.37-\$0.46	2,105,000	4.82	\$0.41	2,105,000	\$0.41
\$0.50-\$0.75	6,277,500	5.31	\$0.72	3,901,500	\$0.72
\$0.80-\$1.00	4,932,500	7.35	\$0.92	4,932,500	\$0.92
\$1.08-\$1.75	764,000	4.52	\$1.20	764,000	\$1.20
\$2.00-\$2.75	223,500	4.13	\$2.16	223,500	\$2.16
Totals	14,302,500			11,926,500	



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The Company Stock Option Plans are administered by the Compensation/Administration Committee, currently comprised of two independent members of the Company's Board of Directors. Company stock options are issued to employees at an exercise price not less than the fair market value, as determined under the option plan, on the date of grant and must be granted within 10 years from the effective date of the Plan, with the term of the option not exceeding 10 years. Under the Employee Incentive Stock Option Plans, incentive and non-qualified stock options may be granted, with the incentive stock options intended to qualify under Section 422 of the Internal Revenue Code of 1986, as amended. Unless otherwise established by the Committee, the standard vesting schedule for the incentive stock options issued currently is 10% vested immediately upon grant, 15% vested after twelve months from date of grant, 25% after two years from the date of grant, 25% after three years, and 25% after four years. All of the options have been or will be registered on Form S-8 filings. In accordance with accounting for such options utilizing the intrinsic value method, there is no related compensation expense recorded in the Company's financial statements for the current fiscal year. The stock option plans outlined below allow for reissuance of the authorized shares upon cancellation of a stock option grant.

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Alanco Stock Option Summary (1)  
as of 6/30/06

Plan		Authorized	Issued	Exercised	Cancelled	Outstanding	Balance to Issue
Misc	(2)	N/A	3,670,000	305,000	1,115,000	2,250,000	
1998	(3)	750,000	1,459,500	162,500	709,500	587,500	
1998 D&O	(4)	750,000	750,000	405,000	0	345,000	
1999	(3)	1,500,000	3,956,250	375,000	2,456,250	1,125,000	
1999 D&O	(4)	500,000	645,000	0	150,000	495,000	5,000
2000	(3)	1,000,000	1,912,500	234,250	923,250	755,000	10,750
2000 D&O	(4)	500,000	490,000	120,000	0	370,000	10,000
2002	(3)	1,500,000	1,745,000	0	250,000	1,495,000	5,000
2002 D&O	(4)	500,000	500,000	40,000	0	460,000	
2004	(3)	2,000,000	2,550,000	0	550,000	2,000,000	
2004 D&O	(4)	1,000,000	990,000	0	0	990,000	10,000
2005	(3)	3,000,000	2,580,000	0	0	2,580,000	420,000
2005 D&O	(4)	1,000,000	850,000	0	0	850,000	150,000
Totals		14,000,000	22,098,250	1,641,750	6,154,000	14,302,500	610,750

- (1) Only includes plans with options currently outstanding or having a balance available to issue  
(2) Options issued to officers and other employees outside of any plan as an inducement at time of employment.  
(3) Employee Incentive Stock Option Plan  
(4) Directors and Officers Stock Option Plan  
(5) Range of exercise prices for outstanding options only.

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### 13. RETIREMENT PLAN

The Company provides a 401(k) retirement plan for its employees. Employees are eligible to participate in the plan on the first of the month following 90 days of continuous employment. Employee salary deferral rates are not restricted by the Company, however, IRS limits and limitations imposed by discrimination tests may affect the allowed salary deferral rate. The Company matches 25% of the amount deferred by employees, matching up to 4% of an employee's annual compensation. The Company's matching contributions totaled \$17,000 and \$13,300 for the years ended June 30, 2006 and 2005, respectively.

### 14. STARTRAK ACQUISITION

Alanco shareholders entered into an Agreement and Plan of Reorganization (the "Transaction") in June 2006 to acquire 100% of StarTrak Systems, LLC ("StarTrak"), a Delaware LLC, located in Morris Plains, New Jersey. StarTrak, a leading provider of GPS tracking and wireless subscription data services to the transportation industry, specifically focuses upon the refrigerated or "Reefer" segment of the transport industry providing the dominant share of all wireless tracking, monitoring and control services to this market segment. The transaction closed effective June 30, 2006.

The Transaction, anticipated to be all stock, was effected by the issuance of 5 million Alanco Class A Common shares at closing, effective June 30, 2006, and the obligation to issue an additional 8.2 million shares by January 31, 2007 upon approval by Alanco shareholders. In addition, the sellers could potentially earn up to an additional \$8 million (a maximum of \$4 million each year) based upon StarTrak operations achieving certain financial targets in fiscal years 2007 and 2008 ("Earn-out"). The value of the Earn-out is calculated for fiscal year 2007 as two hundred percent of StarTrak gross profit in excess of \$6 million. For fiscal year 2008, the Earn-out is calculated as two hundred percent of gross profit in excess of \$8 million. Upon shareholder approval, the Earn-out may be paid in shares of Alanco Class A Common stock valued at market, determined as a ten-day average closing price immediately prior to issuance.

The annual Alanco shareholders' meeting is tentatively scheduled for December 28, 2006, at which the shareholders will be asked to approve various proposals related to the acquisition including the issuance of the 8.2 million common shares required by the Agreement, as well as authorization of the issuance of common shares as payment of any potential Earn-out obligation under the Agreement. A preliminary proxy statement for the annual meeting is scheduled to be filed shortly following the filing of the Company's Form 10-KSB for the year ended June 30, 2006.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

The value of the Transaction, considering the 5 million Class A Common Shares issued at closing (valued at \$3,485,000), 8.2 million Class A Common shares to be issued upon shareholder approval (valued at \$5,715,400 on June 30, 2006), StarTrak net liabilities assumed of \$5,425,800 and the related costs of the acquisition of \$434,500, was valued at of \$15,060,700. In accordance with the provisions of SFAS 141, Business Combinations, the transaction must be recorded using the purchase method of accounting, which requires the allocation of the purchase price to the fair value of the assets acquired and the

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liabilities assumed by balance sheet classifications. The Company has engaged the services of an independent consultant for valuation services related to FASB 141. The consultant's report has not been received by the date of this audit report and therefore the entire transaction value is presented as goodwill. The consultant's report is expected in the next few weeks when the appropriate allocation of the purchase price will be completed. We believe the allocation will focus primarily on intangible assets other than goodwill. If additional payments are made pursuant to the Earn-out provisions of the merger agreement, or if the value of the 8.2 million shares to be issued upon shareholder approval is valued differently than valued at closing, the purchase price and related goodwill value may be adjusted.

A summary of the amounts of the assets and liabilities acquired in the StarTrak acquisition are as follows:

Current Assets	
Accounts receivable	\$ 919,700
Inventory	885,900
Prepaid expense	33,500
	-----
Total current assets	\$ 1,839,100
Property and Equipment	42,300
Other Assets - deposits	4,500
	-----
Total Assets	\$ 1,885,900
	=====
Current Liabilities	
Accounts payable	\$ 3,683,300
Notes payable	368,300
Customer advances	1,001,100
Deferred revenues	119,700
Due to Alanco	774,300
	-----
Total current liabilities	5,946,700
Long-Term debt	1,365,000
	-----
Total Liabilities	7,311,700
	-----
Liabilities assumed in excess of assets acquired	\$ 5,425,800
	=====

Amounts classified as "due to Alanco" at the time of the acquisition consisted of operating advances made to StarTrak prior to the acquisition.

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The following table is a summary of the results of operations and other financial information by major segment:

	Data Storage	RFID Technology	Wireless Asset Management	Corporate	Total
	-----	-----	-----	-----	-----
Fiscal year 2006					
Revenue	\$ 6,028,100	\$ 631,500	\$ -	\$ -	\$ 6,659,600
Cost of Goods Sold	3,877,800	479,900	-	-	4,357,700
Gross Profit	2,150,300	151,600	-	-	2,301,900
Selling, General & Administrative	2,081,600	2,669,600	-	1,553,100	6,304,300
Operating Income (Loss)	\$ 68,700	\$ (2,518,000)	\$ -	\$ (1,553,100)	\$ (4,002,400)
Accounts Receivable	\$ 645,400	\$ 178,300	\$ 919,700	\$ 17,300	\$ 1,760,700
Inventory	\$ 1,317,500	\$ 940,500	\$ 885,900	\$ -	\$ 3,143,900
Total Assets	\$ 2,344,200	\$ 7,239,800	\$ 17,572,200	\$ 528,300	\$ 27,684,500
Capital Expenditures	\$ 15,800	\$ 54,400	\$ -	\$ 600	\$ 70,800
Depreciation & Amortization	\$ 24,200	\$ 355,600	\$ -	\$ 3,200	\$ 383,000
Fiscal year 2005					
Revenue	\$ 6,363,300	\$ 820,900	\$ -	\$ -	\$ 7,184,200
Cost of Goods Sold	4,161,200	514,300	-	-	4,675,500
Gross Profit	2,202,100	306,600	-	-	2,508,700
Selling, General & Administrative	1,918,300	2,697,600	-	1,755,400	6,371,300
Operating Income (Loss)	\$ 283,800	\$ (2,391,000)	\$ -	\$ (1,755,400)	\$ (3,862,600)
Accounts Receivable	\$ 827,600	\$ 246,400	\$ -	\$ 17,400	\$ 1,091,400
Inventory	\$ 1,091,900	\$ 810,700	\$ -	\$ -	\$ 1,902,600
Total Assets	\$ 2,398,800	\$ 6,987,600	\$ -	\$ 1,157,500	\$ 10,543,900
Capital Expenditures	\$ 41,600	\$ 108,900	\$ -	\$ 2,400	\$ 152,900
Depreciation & Amortization	\$ 20,300	\$ 326,400	\$ -	\$ 3,100	\$ 349,800

### 16. SELECTED CONSOLIDATED QUARTERLY FINANCIAL DATA (unaudited)

The following table sets forth certain unaudited selected consolidated financial information for each of the four quarters in fiscal 2006 and 2005. In management's opinion, this unaudited consolidated quarterly selected information has been prepared on the same basis as the audited consolidated financial statements and includes all necessary adjustments,

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consisting only of normal recurring adjustments that management considers necessary for a fair presentation when read in conjunction with the consolidated financial statements and notes thereto. The Company believes these comparisons of consolidated quarterly selected financial data are not necessarily indicative of future performance.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Quarterly earnings per share may not total to the fiscal year earnings per share due to the weighted average number of shares outstanding at the end of each period reported.

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
2006				
Total revenues	\$ 1,601,600	\$ 1,624,900	\$ 1,466,200	\$ 1,966,000
Cost of sales	1,056,700	1,113,800	914,700	1,272,000
Gross profit	544,900	511,100	551,500	694,000
Operating Loss	(1,064,300)	(1,041,800)	(1,028,600)	(867,000)
Net loss*	(1,330,000)	(1,059,100)	(1,273,600)	(929,000)
Loss per share - basic & diluted	\$ (0.05)	(0.04)	\$ (0.04)	\$ (0.04)
Weighted Average Shares	26,915,400	28,269,300	30,111,900	31,138,000
2005				
Total revenues	\$ 1,737,200	\$ 2,085,500	\$ 1,531,200	\$ 1,830,000
Cost of sales	1,115,800	1,402,400	975,300	1,182,000
Gross profit	621,400	683,100	555,900	648,000
Operating Loss	(908,600)	(871,200)	(1,103,600)	(979,000)
Net loss*	(1,145,400)	(886,200)	(1,355,600)	(924,000)
Loss per share - basic & diluted	\$ (0.05)	\$ (0.03)	\$ (0.05)	\$ (0.03)
Weighted Average Shares	24,312,600	25,416,700	25,514,500	26,091,000

\*Attributable to Common Shareholders

#### 17. SUBSEQUENT EVENTS

The Company announced on August 28, 2006, that it had completed agreements whereby the Company raised \$1.3 million in debt financing from certain officers and members of the Company's Board of Directors. The funds were used for working capital requirements related primarily to the acquisition of StarTrak Systems, LLC an acquisition that was effective on June 30, 2006.

In August of 2006, Alanco announced that it had received a staff determination letter from Nasdaq indicating that the Company failed to comply with the minimum bid price requirements for continued listing as

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set forth in Nasdaq Marketplace Rule 4310(c)(4), and that its securities may be subject to delisting from the Nasdaq Capital Market. The Company has appealed the Staff determination and requested a hearing before the Nasdaq Listing Qualifications Panel ("Panel"). Under Nasdaq Marketplace rules, a request for a hearing stays the delisting action pending the issuance of a written determination by the Panel. The hearing was held on September 14, 2006 in Washington, D.C. with representatives of the Company present. There can be no assurance that the Panel will grant the Company's request for continued listing. Pending a decision by the Panel, the Company's common stock will remain listed on the Nasdaq Capital Market.

The Company announced on July 14, 2006, that the Company completed the sale, in a private offering to several private and institutional investors, of 240,000 Units consisting of one share of its Series A Convertible Preferred Stock together with a 5-year warrant to purchase three shares of the Company's Class A Common Stock at a price of \$.60 per share ("Unit") for a Unit price of \$1.71. The Company received \$410,400 from the offering. Twenty five percent of the Units, or 60,000 Units, were purchased by an institutional investor with the balance purchased by members of the Company's Board of Directors. Due to the structure of the offering and the Nasdaq stock market requirements, warrants issued in this offering to members of the Board of Directors are restricted from being exercised without shareholders' approval, which shall be requested at the next annual meeting of the Company's Shareholders.

On July 6, 2006, the Company announced the completion of the acquisition of StarTrak Systems, LLC, effective June 30, 2006. In conjunction with the acquisition, effective July 1, 2006, Mr. Tim Slifkin, President and Chief Executive Officer of StarTrak, was appointed to the Company's Board

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

of Directors to replace Mr. Steven Oman, who resigned. Mr. Oman's resignation was not due to any disagreement with the registrant, but was solely for the purpose of compliance with the Sarbanes-Oxley requirement that the Company's Board of Directors be comprised of a majority of independent members. Mr. Oman will continue as Alanco's Corporate Counsel.

#### ITEM 8. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE: NONE

#### ITEM 8A. CONTROL AND PROCEDURES

The Company maintains disclosure controls and procedures designed to ensure that it is able to collect the information it is required to disclose in the reports it files with the Securities and Exchange Commission (SEC), and to process, summarize and disclose this information within the time periods specified in the rules of the SEC. Based on various evaluations of the Company's disclosure controls and procedures, through the date of this filing, the Chief Executive and Chief Financial Officers believe that these controls and procedures are effective to ensure that the Company is able to collect, process and disclose the information it is required to disclose in the reports it files with the SEC within the required periods.

The Company also maintains a system of internal controls designed to provide reasonable assurance that transactions are executed in accordance with management's general or specific authorization; transactions are recorded as

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necessary (1) to permit preparation of financial statements in conformity with generally accepted accounting principles, and (2) to maintain accountability for assets. Access to assets is permitted only in accordance with management's general or specific authorization, and the recorded accountability for assets is compared with the existing assets at reasonable intervals and appropriate action is taken with respect to any differences.

Since the date of the most recent evaluation of the Company's internal controls by the Chief Executive and Chief Financial Officers, there have been no significant changes in such controls or in other factors that could have significantly affected those controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

### PART III

#### ITEM 9. DIRECTORS, EXECUTIVE OFFICERS, PROMOTERS AND CONTROL PERSONS; COMPLIANCE WITH SECTION 16(A) OF THE EXCHANGE ACT.

##### Officers and Directors

The officers and directors of the Company are:

Name	Age	Position	Year First Director
Harold S. Carpenter	72	Director	1995
James T. Hecker	49	Director	1997
Robert R. Kauffman	66	Director/C.O.B./C.E.O.	1998
Thomas C. LaVoy	46	Director	1998
John A. Carlson	59	Director/E.V.P./C.F.O.	1999
Donald E. Anderson	72	Director	2002
Timothy P. Slifkin	51	Director/C.E.O. - StarTrak	2006

Robert R. Kauffman: Mr. Kauffman was appointed as Chief Executive Officer and Chairman of the Board effective July 1, 1998. Mr. Kauffman was formerly President and Chief Executive Officer of NASDAQ-listed Photocomm, Inc., from 1988 until 1997 (since renamed Kyocera Solar, Inc.). Photocomm was the nation's largest publicly owned manufacturer and marketer of wireless solar electric power systems with annual revenues in excess of \$35 million. Prior to Photocomm, Mr. Kauffman was a senior executive of the Atlantic Richfield Company (ARCO) whose varied responsibilities included Senior Vice President of ARCO Solar, Inc., President of ARCO Plastics Company and Vice President of ARCO Chemical Company. Mr. Kauffman earned an M.B.A. in Finance at the Wharton School of the University of Pennsylvania, and holds a B.S. in Chemical Engineering from Lafayette College, Easton, Pennsylvania.

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#### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

John A. Carlson: Mr. Carlson, Executive Vice President and Chief Financial Officer of Alanco Technologies, Inc., joined the Company in September 1998 as Senior Vice President/Chief Financial Officer. Mr. Carlson started his career with Price Waterhouse & Co. in Chicago, Illinois. He has over twenty-five years of public and private financial and operational management experience, including over twelve years as Chief Financial Officer of a Fortune 1000 printing and publishing company. He earned his Bachelor of Science degree in Business Administration at the University of South Dakota, and is a Certified Public

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Accountant

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Donald E. Anderson: Donald E. Anderson is President and owner of Programmed Land, Inc., a Minnesota and Scottsdale, Arizona, based company. Programmed Land is a diversified holding company engaged in real estate, including ownership, development, marketing and management of properties. He is also majority owner of a company involved in the automotive industry. From 1988 until 1997, Mr. Anderson was Chairman of the Board of NASDAQ-listed Photocomm, Inc., a company involved in the solar electric business. Since 1983, Mr. Anderson has also been President of Pine Summit Bible Camp, a non-profit organization that operates a year-round youth camp in Prescott, Arizona. Mr. Anderson has a B.A. degree in accounting.

Harold S. Carpenter: Mr. Carpenter is the former President of Superiorgas Co., Des Moines, Iowa, which is engaged in the business of trading and brokering bulk refined petroleum products with gross sales of approximately \$500 million per year. He is also the General Partner of Superiorgas L.P., an investment company affiliated with Superiorgas Co. Mr. Carpenter founded these companies in 1984 and 1980, respectively. Mr. Carpenter is also the President of Carpenter Investment Company, Des Moines, Iowa, which is a real estate investment company holding properties primarily in central Iowa. From 1970 until 1994, Mr. Carpenter was the Chairman of the George A. Rolfes Company of Boone, Iowa, which manufactured air pollution control equipment. Mr. Carpenter graduated from the University of Iowa in 1958 with a Bachelor of Science and Commerce degree.

James T. Hecker: Mr. Hecker is both an Attorney and a Certified Public Accountant. Since 1987 Mr. Hecker has been Vice President, Treasurer and General Counsel of Rhino Capital Incorporated, Evergreen, Colorado, a private capital management company which manages a \$60 million portfolio. He also served, since 1992, as a trustee of an \$11 million charitable trust. From 1984 to 1987, Mr. Hecker was the Controller of Northern Pump Company, Minneapolis, Minnesota, a multi-state operating oil and gas company with more than 300 properties, with responsibility of all accounting and reporting functions. Prior to that, from 1981 to 1984, Mr. Hecker was Audit Supervisor of Total Petroleum, Inc., Denver, responsible for all phases of internal audit and development of audit and systems controls. Mr. Hecker received a J.D. degree from the University of Denver in 1992, and a B.B.A. degree in Accounting and International Finance from the University of Wisconsin in 1979. He is a member in good standing of the Colorado and the American Bar Associations, the Colorado Society of CPAs, and the American Institute of CPAs.

Thomas C. LaVoy: Thomas C. LaVoy has served as Chief Financial Officer of SuperShuttle International, Inc., since July 1997 and as Secretary since March 1998. From September 1987 to February 1997, Mr. LaVoy served as Chief Financial Officer of NASDAQ-listed Photocomm, Inc. Mr. LaVoy was a Certified Public Accountant with the firm of KPMG Peat Marwick from 1980 to 1983. Mr. LaVoy has a Bachelor of Science degree in Accounting from St. Cloud University, Minnesota, and is a Certified Public Accountant.

Timothy P. Slifkin: Timothy P. Slifkin, President and Chief Executive Officer of the Company's subsidiary, StarTrak Systems, LLC, is directly responsible for development of StarTrak's wireless product line and for leading the North American rail industry's acceptance of the technology for damage prevention, refrigeration transport, and asset management applications. Mr. Slifkin has been developing remote monitoring systems since founding Elexor Associates in 1986, and in developing and deploying wireless systems (satellite and terrestrial) since 1992. He has several patents issued or pending on related technology. Prior to founding StarTrak, Mr. Slifkin was employed with Hewlett Packard, Johansson Microwave, American Microsystems, and Jet Propulsion Laboratories. He holds a Bachelors Degree in Engineering.



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## ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

### Non-Director Significant Employees

The following table provides information regarding key officers for the Company's primary subsidiaries.

Name	Age	Position	Year Appointed to Position
Greg M. Oester	57	President - Alanco/TSI PRISM, Inc.	2002
Thomas A. Robinson	45	Executive Vice President - StarTrak Systems, LLC	2006

Greg M. Oester: Mr. Oester started his employment as President of Alanco/TSI PRISM, Inc. (formerly Technology Systems International, Inc.) in 2000. He practiced international business law for 12 years and founded a firm in Los Angeles, CA. He co-founded North American Enterprises, Inc. in 1989 and engaged in sales & marketing of European specialty products in the U.S.A. Mr. Oester conducted seminars on foreign investment in the U.S.A. throughout Asia. He was admitted to practice before the U.S. Customs Court, the Court of International Trade and numerous State and Federal venues. Mr. Oester holds Bachelor of Arts degrees in Political Science and Economics from the University of Arizona and also a Juris Doctor Degree from the University of Laverne.

Thomas A. Robinson: Mr. Robinson, Executive Vice President of StarTrak Systems, LLC, has been responsible for major program deliveries at StarTrak since 1999. He is intimately involved in the systems development, network completion, customer commitments, and deployments for all major products of StarTrak. Prior to joining StarTrak, Mr. Robinson was employed by Varlen Corporation (acquired by Amsted Industries in 1999) where he was responsible for mergers and acquisitions. Prior to Varlen, he was a Program Manager at Hughes Aircraft. Mr. Robinson holds Bachelors and Masters Degrees in Engineering from Case Western Reserve University and an MBA from Wharton.

### Audit/Corporate Governance Committee

The Audit/Corporate Governance Committee of the Board of Directors is currently comprised of three independent directors, and operates under a written charter adopted by the Board. The Audit/Corporate Governance Committee Charter was included as Exhibit A in the Company's Definitive Proxy Statement filed with the SEC on October 18, 2004. The members of the Audit/Corporate Governance Committee are Harold S. Carpenter, a CEO with over 30 years senior management experience, James T. Hecker, an attorney and CPA, and Thomas C. LaVoy, a CPA. All three individuals are experienced in reading and understanding financial statements, and, in fact, are deemed to be financial experts as defined by audit committee requirements.

The Audit/Corporate Governance Committee is directly responsible for the appointment, compensation, retention and oversight of the work of the independent auditor engaged for the purpose of preparing an audit report or performing other audit, review or attest services for the Company. The auditor reports directly to the Audit/Corporate Governance Committee. The Audit/Corporate Governance Committee has established "whistleblower" procedures for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls or auditing matters, including procedures for the confidential anonymous submission by employees of the Company of concerns

regarding questionable accounting or auditing matters.

Authority to engage independent counsel and other advisors has been given to the Audit/Corporate Governance Committee as it determines is necessary to carry out its duties. The Company provides appropriate funding for the Audit/Corporate Governance Committee to compensate the outside auditors and any lawyers and advisors it employs and to fund ordinary administrative expenses of the Audit/Corporate Governance Committee that are necessary in carrying out its duties.

The Audit/Corporate Governance Committee provides general oversight of the Company's financial reporting and disclosure practices, system of internal controls, and the Company's processes for monitoring compliance by the Company with Company policies. The Audit/Corporate Governance Committee reviews with the

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

Company's independent auditors the scope of the audit for the year, the results of the audit when completed, and the independent auditor's fee for services performed. The Audit/Corporate Governance Committee also recommends independent auditors to the Board of Directors and reviews with management various matters related to its internal accounting controls. During the last fiscal year, there were three meetings of the Audit/Corporate Governance Committee.

Management is responsible for the Company's internal controls and the financial reporting process. The independent auditors are responsible for performing an independent audit of the Company's consolidated financial statements in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States) and issuing a report thereon. The Audit/Corporate Governance Committee is responsible for overseeing and monitoring the quality of the Company's accounting and auditing practices.

The members of the Audit/Corporate Governance Committee are not professionally engaged in the practice of auditing or accounting and may not be experts in the fields of accounting or auditing, or in determining auditor independence. Members of the Audit/Corporate Governance Committee rely, without independent verification, on the information provided to them and on the representations made by management and the independent accountants. Accordingly, the Audit/Corporate Governance Committee's oversight does not provide an independent basis to determine that management has maintained procedures designed to assure compliance with accounting standards and applicable laws and regulations. Furthermore, the Audit/Corporate Governance Committee's considerations and discussions referred to above do not assure that the audit of the Company's financial statements has been carried out in accordance with auditing standards generally accepted in the United States, that the financial statements are presented in accordance with accounting principles generally accepted in the United States of America or that the Company's auditors are in fact "independent."

Compliance with Section 16(a) of Securities Exchange Act of 1934

Section 16(a) of the Securities Exchange Act of 1934 requires the Company's Officers and Directors, and persons who own more than 10% of a registered class of the Company's equity securities, to file reports of ownership and changes in ownership with the Securities and Exchange Commission ("SEC"). Officers, Directors and greater than 10% shareholders are required by SEC regulations to furnish the Company with copies of all Section 16(a) forms they file. Based solely upon a review of the copies of such forms furnished to the Company, or

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written representations that no Form 5's were required, the Company believes that as of the date of filing of this Form 10-KSB, all Section 16(a) filing requirements applicable to its officers, Directors and greater than 10% beneficial owners were satisfied, with the exception of Technology Systems International, Inc., a Nevada corporation (TSIN), who, to the best of our knowledge, continues to own approximately 4.5 million shares of the Company's Class A Common Stock. TSIN is currently in Chapter 7 Bankruptcy proceedings and has not, to our knowledge, filed any current Section 16 (d) forms.

### Code of Ethics

The Company has adopted a Corporate Code of Business Conduct and Ethics, which was included as Exhibit 99.2 in the Company's Form 10-QSB filed with the SEC on November 15, 2004. We believe our code of ethics is reasonably designed to deter wrongdoing and promote honest and ethical conduct; provide full, fair, accurate, timely and understandable disclosure in public reports; comply with applicable laws; ensure prompt internal reporting of code violations; and provide accountability for adherence to the code.

The Code of Business Conduct and Ethics is presented on the Company's web page under the subheading "Corporate Governance." Shareholders may receive a copy of the Company's adopted Code of Conduct, without charge, via e-mail request to [alanco@alanco.com](mailto:alanco@alanco.com), by calling the Company at 480 607-1010, Ext. 857, or by writing to the Company to the attention of the Company's Corporate Secretary at 15575 N. 83rd Way, Suite 3, Scottsdale, Arizona 85260.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### ITEM 10. EXECUTIVE COMPENSATION

##### Summary Compensation Table

The following table sets forth the compensation paid or accrued by the Company for the services rendered during the fiscal years ended June 30, 2006, 2005 and 2004 to the Company's Chief Executive Officer, Chief Financial Officer, and President of the Company's subsidiary, Alanco/TSI PRISM, Inc., an Arizona corporation (ATSI), acquired effective June 1, 2002, whose salaries and bonus exceeded \$100,000 during the last fiscal year (collectively, the "Named Executive Officers"). No stock appreciation rights ("SARs") have been granted by the Company to any of the Named Executive Officers during the last three fiscal years.

Name and Principal Position	Annual Compensation			Long-Term Compensation
	Annual Salary	Bonus	Other (1) Annual Compensation \$	Securities (# shares) Underlying Options Granted during FY
Robert R. Kauffman, C.E.O.				
FY 2006	\$225,000	None	\$17,400	940,000
FY 2005	183,750	None	17,400	100,000
FY 2004	180,000	None	17,400	650,000
John A. Carlson, C.F.O.				
FY 2006	200,000	None	10,400	570,000
FY 2005	163,333	None	10,033	75,000
FY 2004	160,000	None	9,467	350,000

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Greg M. Oester, President, ATSI					
	FY 2006	154,500	None	None	120,000
	FY 2005	154,500	None	None	35,000
	FY 2004	146,625	None	None	250,000

(1) Represents supplemental executive benefit reimbursement for the year and Company matching for Alanco's 401(K) Profit Sharing Plan.

### Option Grants in Last Fiscal Year

The following table sets forth each grant of stock options made during the fiscal year ended June 30, 2006, to each of the Named Executive Officers and/or Directors and to all other employees as a group. No stock appreciation rights ("SARs") have been granted by the Company.

### INDIVIDUAL GRANTS

Name	Number of Securities Underlying		Exercise Price (\$/Sh)	Grant Date	Expiration Date
	Option Grante	% of Total Options Granted			
Robert Kauffman	400,000	5.25%	\$0.81	9/13/2005	9/13/2015
Robert Kauffman	40,000	0.52%	\$0.46	11/16/2005	11/16/2015
Robert Kauffman	500,000	6.56%	\$0.73	6/30/2006	6/30/2011
John Carlson	200,000	2.62%	\$0.81	9/13/2005	9/13/2015
John Carlson	100,000	1.31%	\$0.46	11/16/2005	11/16/2015
John Carlson	20,000	0.26%	\$0.46	11/16/2005	11/16/2015
John Carlson	250,000	3.28%	\$0.73	6/30/2006	6/30/2011
Harold Carpenter	80,000	1.05%	\$0.81	9/13/2005	9/13/2015
Harold Carpenter	100,000	1.31%	\$0.73	6/30/2006	6/30/2011
James Hecker	80,000	1.05%	\$0.81	9/13/2005	9/13/2015
James Hecker	100,000	1.31%	\$0.73	6/30/2006	6/30/2011
Thomas LaVoy	80,000	1.05%	\$0.81	9/13/2005	9/13/2015
Thomas LaVoy	40,000	0.52%	\$0.46	11/16/2005	11/16/2015
Thomas LaVoy	100,000	1.31%	\$0.73	6/30/2006	6/30/2011
Donald Anderson	80,000	1.05%	\$0.81	9/13/2005	9/13/2015
Donald Anderson	100,000	1.31%	\$0.73	6/30/2006	6/30/2011
Greg Oester	100,000	1.31%	\$0.81	2/16/2005	2/16/2015
Greg Oester	20,000	0.26%	\$0.46	11/16/2005	11/16/2015
Timothy Slifkin	1,000,000	13.12%	\$0.73	6/30/2006	6/30/2011
Thomas Robinson	1,000,000	13.12%	\$0.73	6/30/2006	6/30/2011
Other Employees	3,230,000	42.39%	\$0.50 - \$1.00	Various	(1)
Total	7,620,000	100.00%			

### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

(1) The expiration dates for these options range from 9/27/2007 to 5/25/2016.

All options are granted at a price not less than "grant-date market." During the fiscal year 874,000 previously granted stock options expired or were cancelled.

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Aggregated Options and Warrants - Exercised in Last Fiscal Year and Values at Fiscal Year End

The following table sets forth the number of exercised and unexercised options and warrants held by each of the Named Executive Officers and/or Directors at June 30, 2006, and the value of the unexercised, in-the-money options at June 30, 2006.

Name	Shares Acquired On Exercise During 2006 Fiscal Year	Value Realized (\$) (1)	Unexercised Options & Warrants at Fiscal Year End (Shares) (2)	Value of Unexercised In-The-Money Options & Warrants at FYE (\$) (3)
Robert Kauffman	120,000	\$4,600	3,507,500	\$441,200
John Carlson	85,000	5,800	1,460,000	112,650
Harold Carpenter	100,000	4,000	680,000	60,800
James Hecker	0	0	400,000	14,400
Thomas LaVoy	20,000	1,800	380,000	10,800
Donald Anderson	400,000	16,000	2,505,000	187,500
Greg Oester	10,000	900	1,220,000	37,800
Timothy Slifkin	0	0	400,000	0
Thomas Robinson	0	0	400,000	0

- (1) Calculated as the difference between closing price on the date exercised and the exercise price, multiplied by the number of options exercised.
- (2) Represents the number of securities underlying unexercised options and warrants that were exercisable at 2006 Fiscal Year End.
- (3) Calculated as the difference between the closing price of the Company's Common Stock on June 30, 2006, and the exercise price for those options exercisable on June 30, 2006, with an exercise price less than the closing price, multiplied by the number of applicable options.

Option Grants Subsequent to Fiscal Year End

Name	Number of Underlying Securities Options Granted	Date of Grant	Date Exercisable	Expiration Date	Option Price
Robert R. Kauffman	150,000 (1)	8/15/06	(3)	8/15/11	\$0.55
John A. Carlson	50,000 (2)	8/15/06	(3)	8/15/11	\$0.55
Harold S. Carpenter	100,000 (2)	8/15/06	(3)	8/15/11	\$0.55
Donald E. Anderson	250,000 (1)	8/15/06	(3)	8/15/11	\$0.55

- (1) Issued pursuant to the 2005 Stock Option Plan.
- (2) Issued pursuant to the 2005 Directors & Officers Stock Option Plan.
- (3) 10% vest on 8/15/2006, 15% vest on 8/15/2007, 25% vest on 8/15/2008, 25% vest on 8/15/2009 and 25% vest on 8/15/2010.

### Employment Agreements and Executive Compensation

The Executive Officers are at-will employees without employment agreements.

Compensation of Directors

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During Fiscal Year 2006, non-employee Directors were compensated for their services in cash (\$750 per meeting per day up to a maximum of \$1,500 per meeting) and through the grant of options to acquire shares of Class A Common Stock as provided by the 1996, 1998, 1999, 2000, 2002, 2004, and 2005 Directors and Officers Stock Option Plans (the "D&O Plans") which are described below. All Directors are entitled to receive reimbursement for all out-of-pocket expenses incurred for attendance at Board of Directors meetings.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

The 1996 Directors and Officers Stock Option Plan was approved by the Board of Directors on September 9, 1996. Shareholders approved the 1998, 1999, 2000, 2002, 2004, and 2005 Directors and Officers Stock Option Plans on November 6, 1998, November 5, 1999, November 10, 2000, November 22, 2002, November 19, 2004, and January 20, 2006, respectively. The purpose of the 1996, 1998, 1999, 2000, 2002, 2004, and 2005 D&O Plans is to advance the business and development of the Company and its shareholders by affording to the Directors and Officers of the Company the opportunity to acquire a proprietary interest in the Company by the grant of Options to acquire shares of the Company's common stock. All Directors and Executive Officers of the Company are eligible to participate in the 1996, 1998, 1999, 2000, 2002, 2004, and 2005 Plans. Newly appointed Directors receive options to purchase shares of common stock at fair market value. Upon each subsequent anniversary of the election to the Board of Directors, each non-employee Director may receive an additional option to purchase shares of common stock at fair market value.

#### ITEM 11. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

##### Security Ownership of Certain Beneficial Owners

The following table sets forth certain information with respect to each shareholder known by Alanco to be the beneficial owner of more than 5% of the outstanding Alanco common stock or common stock equivalent as of September 22, 2006. Information regarding the stock ownership of Robert R. Kauffman, Alanco Chairman and Chief Executive Officer, Donald E. Anderson, Alanco Director, and Timothy P. Slifkin, StarTrak Chief Executive Officer, is also shown in the table in the following section, Current Directors and Executive Officers.

##### Five Percent Owners

	Class A Common Shares Owned	Class A Percent of Class (5)	Series A Preferred Shares Owned (4)	Total Common Stock Equivalent	Total Common Stock Equivalent Owned Percent of Class (5)	Exercisable Stock Options and Warrants
Technology Systems International, Inc. (1)	4,500,000	11.79%	--	4,500,000	9.14%	--
Donald E. Anderson (2)	3,321,261	8.70%	1,132,434	6,718,563	13.65%	2,350,000

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Robert R. Kauffman (3)	507,000	1.33%	729,051	2,694,153	5.47%	3,342,500
Timothy P. Slifkin (4)	2,164,706	5.67%	0	2,164,706	4.40%	400,000

- (1) Technology Systems International, Inc., a Nevada corporation, (TSIN) is an independent, private company, which was issued 6,000,000 shares of Alanco common stock in 2002 in connection with the acquisition of the assets of TSIN effective in June 2002. The only Form 13D filed by TSIN was filed on September 9, 2002, and indicated TSIN ownership of 6,000,000 Alanco common shares. TSIN is currently in bankruptcy proceeding and to our knowledge, no filings have been made by TSIN to adjust that initial Form 13D filing. However, based on stock transfer records and information obtained from public bankruptcy hearings, we believe the current TSIN ownership of Alanco common stock is approximately 4.5 million shares. To our knowledge, no person or entity owns in excess of 25% of the outstanding shares of TSIN. The only TSIN shareholder that we are aware of who may beneficially control a significant percentage of the outstanding shares of TSIN, and who could potentially own more than 5% of the outstanding Alanco common stock equivalent, is Richard C. Jones, who, to the best of our knowledge, owns approximately 5.3 million TSIN shares, representing approximately 23% of the outstanding TSIN shares. TSIN has previously indicated their intention to distribute the shares of Alanco common stock in excess of certain corporate litigation and liquidation expenses on a pro-rata basis to their shareholders; however, the shares have not been distributed as of the date of this Proxy Statement, and there is no assurance that the shares will be distributed. The address of TSIN is c/o Jill H. Ford, Trustee, P.O. Box 5845, Carefree, AZ 85377.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

- (2) The number of shares, options and warrants owned includes The Anderson Family Trust, owner of 2,568,161 shares of Alanco Class A Common Stock, 654,713 shares of Alanco Series A Convertible Preferred Stock and 1,545,000 exercisable warrants; Programmed Land, Inc., owner of 733,100 shares of Alanco Class A Common Stock, 477,721 shares of Alanco Series A Convertible Preferred Stock and 500,000 exercisable warrants, both of which Mr. Anderson claims beneficial ownership; and 20,000 shares of Alanco Class A Common Stock and 305,000 exercisable options owned by Mr. Anderson. Mr. Anderson also has an additional 225,000 stock options with a vesting schedule ranging from August 15, 2007 to August 15, 2010, and a warrant to purchase 180,000 shares of Class A Common Stock which requires shareholder approval before it can be exercised, a proposal for which will be presented at the Company's Annual Shareholders Meeting tentatively scheduled for December 28, 2006. The 1,132,434 shares of Series A Convertible Preferred Stock beneficially owned by Mr. Anderson represent 33.67% of the total Series A Convertible Preferred shares outstanding. Mr. Anderson's address is 11804 North Sundown Drive, Scottsdale, Arizona 85260.
- (3) In addition to the shares shown above, Robert R. Kauffman, Alanco Chairman and Chief Executive Officer, also beneficially owns 455,000 shares of TSIN stock, representing an ownership position of less than 2% of the outstanding TSIN shares. If TSIN distributes the shares of Alanco common stock owned by TSIN to TSIN shareholders on a proportionate basis, Mr. Kauffman may acquire additional shares of Alanco common stock, thereby slightly increasing his percentage of Alanco common shares owned; but due to matters as discussed in Footnote 1 above, we are unable to accurately calculate the changes to Mr. Kauffman's ownership. Mr. Kauffman also has an additional 135,000 stock options with a vesting schedule ranging from August 15, 2007 to August 15, 2010, and a warrant to purchase 180,000

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shares of Class A Common Stock which requires shareholder approval before it can be exercised, a proposal for which will be presented at the Company's Annual Shareholders Meeting tentatively scheduled for December 28, 2006. The 729,051 shares of Series A Convertible Preferred Stock beneficially owned by Mr. Kauffman represent 21.68% of the total Series A Convertible Preferred shares outstanding. The address for Mr. Kauffman is: c/o Alanco Technologies, Inc., 15575 North 83rd Way, Suite 3, Scottsdale, Arizona 85260.

- (4) In addition to the stock options shown above, Timothy P. Slifkin, Chief Executive Officer of StarTrak Systems, LLC, has 600,000 options with a vesting schedule ranging from June 30, 2007 to June 30, 2010
- (5) Preferred Shares are Series A Convertible Preferred Stock, each share of which is convertible into three (3) shares of Class A Common Stock. As of September 22, 2006, there are 3,362,937 shares of Series A Convertible Preferred Stock outstanding. The 5% owners do not own any shares of the Series B Convertible Preferred Stock.
- (6) The percentages for Class A Common Stock shown are calculated based upon 38,163,706 shares of Class A Common Stock outstanding on September 22, 2006. The percentages for Total Common Stock Equivalent are calculated based upon 49,227,816 shares outstanding on September 22, 2006.
- (7) In calculating the percentage of ownership, option and warrant shares are deemed to be outstanding for the purpose of computing the percentage of shares of common stock equivalent owned by such person, but are not deemed to be outstanding for the purpose of computing the percentage of shares of common stock equivalent owned by any other stockholders.

### Security Ownership of Management

The following table sets forth the number of exercisable stock options and the number of shares of the Company's Common Stock and Preferred Stock beneficially owned as of September 22, 2006, by individual directors and executive officers and by all directors and executive officers of the Company as a group.

The number of shares beneficially owned by each director or executive officer is determined under rules of the Securities and Exchange Commission, and the information is not necessarily indicative of the beneficial ownership for any other purpose. Unless otherwise indicated, each person has sole investment and voting power (or shares such power with his or her spouse) with respect to the shares set forth in the following table.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### Securities of the Registrant Beneficially Owned (1)

Name of Beneficial Owner (2)	Class A Common Stock Shares Owned	Shares Owned Percent of Class (7)	Series A Preferred Stock Shares Owned	Shares Owned Percent of Class (7)	Total Common Stock Equivalent Owned	Shares Owned Percent of Class (7)	Exerc St Opti Warra
Robert R. Kauffman (3) Director/COB/CEO	507,000	1.33%	729,051	21.68%	2,694,153	5.47%	3,
John A. Carlson Director/EVP/CFO	250,644	0.66%	129,993	3.87%	640,623	1.30%	1,



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Harold S. Carpenter Director	305,541	0.80%	292,875 (5)	8.71%	1,184,166	2.41%	
James T. Hecker Director	32,893	0.09%	27,183 (6)	0.81%	114,442	0.23%	
Thomas C. LaVoy Director	55,265	0.14%	46,901	1.39%	195,968	0.40%	
Donald E. Anderson (4) Director	3,321,261	8.70%	1,132,434	33.67%	6,718,563	13.65%	2,
Timothy P. Slifkin Director/CEO - StarTrak	2,164,706	5.67%	0	0.00%	2,164,706	4.40%	
Greg M. Oester President - TSIA	57,888	0.15%	13,183	0.39%	97,437	0.20%	1,
Thomas A. Robinson	1,443,138	3.78%	0	0.00%	1,443,138	2.93%	
Officers and Directors	8,136,336	21.32%	2,371,620	70.52%	15,253,196	30.98%	10,

as a Group (9 individuals)

### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

- (1) Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission ("SEC") and generally indicates voting or investment power with respect to securities. In accordance with SEC rules, shares that may be acquired upon conversion or exercise of stock options, warrants or convertible securities which are currently exercisable or which become exercisable within 60 days are deemed beneficially owned. Except as indicated by footnote, and subject to community property laws where applicable, the persons or entities named in the table above have sole voting and investment power with respect to all shares of Common Stock shown as beneficially owned.
- (2) COB is Chairman of the Board; CEO is Chief Executive Officer; EVP is Executive Vice President; CFO is Chief Financial Officer.
- (3) In addition to the shares shown above, Robert R. Kauffman, Alanco Chairman and Chief Executive Officer, also beneficially owns 455,000 shares of TSIN stock, representing an ownership position of less than 2% of the outstanding TSIN shares. If TSIN distributes the shares of Alanco common stock owned by TSIN to TSIN shareholders on a proportionate basis, Mr. Kauffman may acquire additional shares of Alanco common stock, thereby slightly increasing his percentage of Alanco common shares owned; but due to matters as discussed in Footnote 1 of the Five Percent Owners table above, we are unable to accurately calculate the changes to Mr. Kauffman's ownership. Mr. Kauffman also has a warrant to purchase 180,000 shares of Class A Common Stock which requires shareholder approval before it can be exercised, a proposal which will be presented at the Company's Annual Shareholders Meeting tentatively scheduled for December 28, 2006.
- (4) The number of shares, options and warrants owned also includes The Anderson Family Trust, owner of 2,568,161 shares of Alanco Class A Common Stock, 654,713 shares of Alanco Series A Convertible Preferred Stock and 1,545,000 exercisable warrants; Programmed Land, Inc., owner of 733,100 shares of Alanco Class A Common Stock, 477,721 shares of Alanco Series A Convertible Preferred Stock and 500,000 exercisable warrants, both of which Mr. Anderson claims beneficial ownership; and 20,000 shares of Alanco Class A Common Stock and 305,000 exercisable options owned by Mr. Anderson. Mr. Anderson's address is 11804 North Sundown Drive, Scottsdale, Arizona 85260. Mr. Anderson also has a warrant to purchase

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180,000 shares of Class A Common Stock which requires shareholder approval before it can be exercised, a proposal which will be presented at the Company's Annual Shareholders Meeting tentatively scheduled for December 28, 2006.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

- (5) Excludes 440,000 shares of Class A Common Stock, 319,370 shares of Series A Convertible Preferred Stock and 230,000 warrants to purchase Class A Common Stock owned by Heartland Systems Co., a company for which Mr. Carpenter serves as an officer. Mr. Carpenter disclaims beneficial ownership of such shares.
- (6) Excludes 510,000 shares of Class A Common Stock, 413,290 shares of Series A Convertible Preferred Stock and 435,000 warrants to purchase Class A Common Stock owned by Rhino Fund LLP. The fund is controlled by Rhino Capital Incorporated, for which Mr. Hecker serves as Treasurer and General Counsel. Mr. Hecker disclaims beneficial ownership of such shares.
- (7) The percentages for Class A Common Stock shown are calculated based upon 38,163,706 shares of Class A Common Stock outstanding on September 22, 2006. The percentages for Series A Convertible Preferred Stock are calculated based upon 3,362,937 shares of Series A Convertible Preferred Stock outstanding on September 22, 2006, each of which is convertible into three (3) shares of Class A Common Stock. The percentages for Common Stock Equivalent shares are calculated based upon 49,227,816 Common Stock Equivalent shares outstanding as of September 22, 2006.
- (8) Represents unexercised stock options and warrants issued to named executive officers and directors. All options and warrants listed that were issued to the executive officers and directors were exercisable at September 22, 2006. Robert Kauffman also holds the following options: 22,500 options exercisable in fiscal year 2008, 37,500 options exercisable in fiscal year 2009, 37,500 options exercisable in fiscal year 2010, and 37,500 options exercisable in fiscal year 2011. John Carlson also holds the following options: 7,500 options exercisable in fiscal year 2008, 12,500 options exercisable in fiscal year 2009, 12,500 options exercisable in fiscal year 2010, and 12,500 options exercisable in fiscal year 2011. Donald Anderson also holds the following options: 37,500 options exercisable in fiscal year 2008, 62,500 options exercisable in fiscal year 2009, 62,500 options exercisable in fiscal year 2010, and 62,500 options exercisable in fiscal year 2011. Harold Carpenter also holds the following options: 15,000 options exercisable in fiscal year 2008, 25,000 options exercisable in fiscal year 2009, 25,000 options exercisable in fiscal year 2010, and 25,000 options exercisable in fiscal year 2011. Timothy Slifkin also holds the following options: 150,000 options exercisable in fiscal year 2007, 150,000 options exercisable in fiscal year 2008, 150,000 options exercisable in fiscal year 2009, and 150,000 options exercisable in fiscal year 2010. Thomas Robinson also holds the following options: 150,000 options exercisable in fiscal year 2007, 150,000 options exercisable in fiscal year 2008, 150,000 options exercisable in fiscal year 2009, and 150,000 options exercisable in fiscal year 2010.
- (9) The number and percentages shown include the shares of common stock equivalent actually owned as of September 22, 2006 and the shares of common stock that the identified person or group had a right to acquire within 60 days after September 22, 2006. The percentages shown are calculated based upon 49,227,816 Common Stock Equivalent shares

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outstanding as of September 22, 2006. In calculating the percentage of ownership, option and warrant shares are deemed to be outstanding for the purpose of computing the percentage of shares of common stock equivalent owned by such person, but are not deemed to be outstanding for the purpose of computing the percentage of shares of common stock equivalent owned by any other stockholders.

### ITEM 12. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

#### Transactions with Management

Mr. Steve Oman, a former member of the Board of Directors, received compensation in the amount of approximately \$70,200 for legal services to the Company for the fiscal year ended June 30, 2006.

Mr. Donald Anderson, a member of the Board of Directors and trustee and beneficial owner of the Anderson Family Trust, was paid interest in fiscal year 2006 under the Line of Credit Agreement in the amount of approximately \$89,500.

See Note 7 and 10 to the consolidated financials for additional related party transactions and discussion.

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

#### PART IV

### ITEM 13. EXHIBITS

#### A. Exhibits

- 3(i) Articles of Incorporation of Alanco Technologies, Inc (1)
- 3(ii) Bylaws of Alanco Technologies, Inc (2)
- 4.1 Series A Preferred Convertible Stock Description (3)
- 4.2 Series B Preferred Convertible Stock Description (4)
- 10.1 1996 Directors and Officers Stock Option Plan and Kauffman and Carlson Stock Option Agreements (5)
- 10.2 1998 Incentive Stock Option Plan and Directors and Officers Stock Option Plan (6)
- 10.3 1999 Incentive Stock Option Plan and Directors and Officers Stock Option Plan (7)
- 10.4 2000 Incentive Stock Option Plan and Directors and Officers Stock Option Plan (8)
- 10.5 2002 Incentive Stock Option Plan and Directors and Officers Stock Option Plan (9)
- 10.6 2004 Incentive Stock Option Plan and Directors and Officers Stock Option Plan (10)
- 10.7 2005 Incentive Stock Option Plan and Directors and Officers Stock Option Plan (11)
- 10.8 Nasdaq Delisting Notification (12)
- 10.98 Amendment 3 to Line of Credit Agreement (13)
- 10.10 Amendment 4 to Line of Credit Agreement (14)

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10.11 Amendment 5 to Line of Credit Agreement (15)

14.1 Corporate Code of Business Conduct and Ethics (16)

21. Active Subsidiaries of the Registrant

Name	State of Incorporation
Arraid, Inc.	Arizona
Excel/Meridian Data, Inc.	Arizona
Fry Guy Inc.	Nevada
Alanco/TSI PRISM, Inc. (formerly Technology Systems International, Inc.)	Arizona
StarTrak Systems, LLC	Delaware

31.1 Certification of Robert R. Kauffman, Chairman and Chief Executive Officer of Alanco Technologies, Inc. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of John A. Carlson, Executive Vice President and Chief Financial Officer of Alanco Technologies, Inc., pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer and Chief Financial Officer of Alanco Technologies, Inc., pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

99.1 Audit/Corporate Governance Committee Charter (17)

### Footnotes:

- (1) Incorporated by reference to Form 10KSB filed September 27, 2001
- (2) Incorporated by reference to Form 8-K filed September 27, 2002
- (3) Incorporated by reference to Form S-3/A filed November 21, 2004

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### ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

- (4) Incorporated by reference to Form DEFM14A filed April 22, 2002
- (5) Incorporated by reference to Form S-8 filed October 22, 1998
- (6) Incorporated by reference to Form S-8 filed November 30, 1998
- (7) Incorporated by reference to Form S-8 filed November 29, 1999
- (8) Incorporated by reference to Form S-8 filed December 14, 2000
- (9) Incorporated by reference to Form S-8 filed January 22, 2003
- (10) Incorporated by reference to Form S-8 filed February 17, 2005
- (11) Incorporated by reference to Form S-8 filed February 2, 2006
- (12) Incorporated by reference to Form 8-K filed August 4, 2006
- (13) Incorporated by reference to Form 8-K filed March 28, 2005
- (14) Incorporated by reference to Form 8-K filed July 6, 2005
- (15) Incorporated by reference to Form 8-K filed July 14, 2006
- (16) Incorporated by reference to Form 10QSB filed November 15, 2004
- (17) Incorporated by reference to Form 14A filed October 18, 2004

### B. Schedules NONE

Exhibits or schedules other than those mentioned above are omitted because the conditions requiring their filing do not exist or because the required information is given in the financial statements, including the notes thereto.

### ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

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### Audit Fees

The aggregate fees billed by Semple & Cooper, LLP, the Company's independent auditor, for professional services rendered for the audit of the Company's annual financial statements for the fiscal years ended June 30, 2006 and 2005 and the review of the financial statements included in the Company's Forms 10-QSB for such fiscal years were approximately \$107,100 and \$96,900, respectively.

### Financial Information Systems Design and Implementation

There were no fees billed for the professional services described in Paragraph (c) (4) (ii) of Rule 2-01 of Regulation S-X rendered by Semple & Cooper, LLP for the fiscal year ended June 30, 2006.

### All Other Fees

Semple & Cooper, LLP billed the Company during fiscal year 2006 and 2005 a total of approximately \$11,000 and \$10,000, respectively, for tax preparation and tax consulting services. The Audit Committee has considered whether the provision of these services is compatible with maintaining the principal accountant's independence.

### Audit Committee Pre-Approval Policies and Procedures

The 2006 and 2005 audit services provided by Semple & Cooper were approved by our Audit/Corporate Governance Committee. The Audit/Corporate Governance Committee implemented pre-approval policies and procedures related to the provision of audit and non-audit services. Under these procedures, the Audit/Corporate Governance Committee pre-approves both the type of services to be provided by our independent accountants and the estimated fees related to these services. During the approval process, the Audit/Corporate Governance Committee considers the impact of the types of services and related fees on the independence of the auditor. These services and fees must be deemed compatible with the maintenance of the auditor's independence, in compliance with the SEC rules and regulations. Throughout the year, the Audit/Corporate Governance Committee and, if necessary, the Board of Directors, reviews revisions to the estimates of audit and non-audit fees initially approved.

## SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunder duly authorized.

ALANCO TECHNOLOGIES, INC.  
(Registrant)  
/s/ John A. Carlson  
John A. Carlson  
Chief Financial Officer

Date: September 27, 2006

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

EXHIBIT 31.1

Certification of  
Chairman and Chief Executive Officer

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of Alanco Technologies, Inc.

I, Robert R. Kauffman, certify that:

1. I have reviewed this annual report on Form 10-KSB of Alanco Technologies, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the period presented in this report;

4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and

5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: September 27, 2006

/s/ Robert R. Kauffman

-----  
Robert R. Kauffman  
Chairman and Chief Executive Officer

ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

EXHIBIT 31.2

Certification of  
Vice President and Chief Financial Officer  
of Alanco Technologies, Inc.

I, John A. Carlson, certify that:

1. I have reviewed this annual report on Form 10-KSB of Alanco Technologies, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the small business issuer as of, and for, the period presented in this report;

4. The small business issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the small business issuer and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the small business issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Evaluated the effectiveness of the small business issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(c) Disclosed in this report any change in the small business issuer's internal control over financial reporting that occurred during the small business issuer's most recent fiscal quarter (the small business issuer's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the small business issuer's internal control over financial reporting; and

5. The small business issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the small business issuer's auditors and the audit committee of the small business issuer's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably

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likely to adversely affect the small business issuer's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the small business issuer's internal control over financial reporting.

Date: September 27, 2006

/s/ John A. Carlson

-----  
John A. Carlson  
Vice President and Chief Financial Officer

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

EXHIBIT 32.1

Certification of  
Chief Executive Officer and Chief Financial Officer  
of Alanco Technologies, Inc.

This certification is provided pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and accompanies this annual report of Form 10-KSB (the "Report") for the period ended June 30, 2006 of Alanco Technologies, Inc. (the "Issuer").

Each of the undersigned, who are the Chief Executive Officer and Chief Financial Officer, respectively, of Alanco Technologies, Inc., hereby certify that, to the best of each such officer's knowledge:

(i) the Report fully complies with the requirements of Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Issuer.

Dated: September 27, 2006

/s/ Robert R. Kauffman  
-----  
Robert R. Kauffman  
Chief Executive Officer

/s/ John A. Carlson  
-----  
John A. Carlson  
Chief Financial Officer



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In accordance with Section 13 or 15(d) of the Securities Exchange Act of 1934, the Small business issuer caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

DATE: September 27, 2006

/s/ Robert R. Kauffman

-----  
 Robert R. Kauffman, CEO,  
 Chairman of the Board

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ALANCO TECHNOLOGIES, INC. AND SUBSIDIARIES

KNOWN ALL MEN BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Robert R. Kauffman and John A. Carlson, and each of them, his true and lawful attorney-in-fact and agents, with full power of substitution and resubstitution for him or in his name, place and stead, in any and all capacities, to sign any and all amendments to this Form 10-KSB Annual Report, and to file the same, with all exhibits thereto, and other documents in connection therewith with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully and to all intents and purposes as he might or could do in person hereby ratifying and confirming all that said attorneys-in-fact and agents, or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

SIGNATURE -----	TITLE -----	DATE ----
/s/Robert R. Kauffman ----- Robert R. Kauffman	Director & Chief Executive Officer	September 27, 2006
/s/James T. Hecker ----- James T. Hecker	Director	September 27, 2006
/s/Harold S. Carpenter ----- Harold S. Carpenter	Director	September 27, 2006
/s/Thomas C. LaVoy ----- Thomas C. LaVoy	Director	September 27, 2006
/s/Donald E. Anderson ----- Donald E. Anderson	Director	September 27, 2006
/s/John A. Carlson ----- John A. Carlson	Director & Chief Financial Officer	September 27, 2006

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/s/Timothy P.Slifkin  
-----

Director

September 27, 2006

Timothy P. Slifkin

By /s/ Robert R. Kauffman  
Chairman and Chief Executive Officer

Transfer Agent  
Computershare Trust Company, Inc.  
350 Indiana Street, Suite 800  
Golden, CO 80401  
303-262-0600  
Fax: 303-262-0700