ALANCO TECHNOLOGIES INC
Form 10-Q
February 18, 2011

ALANCO TECHNOLOGIES, INC.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

_ X QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2010

____TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT
For the transition period from _____________ to ____________

Commission file number 0-9347

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

Arizona
(State or other jurisdiction of incorporation or organization)

86-0220694
(I.R.S. Employer Identification No.)

15575 N. 83rd Way, Suite 3, Scottsdale, Arizona 85260
(Address of principal executive offices) (Zip Code)

(480) 607-1010
(Registrant's telephone number)

____
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 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 in the past 90 days. X Yes ___ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	___	Accelerated filer	___
Non-accelerated file	___	Smaller reporting company	X_

(Do not check if a smaller reporting company)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:
As of February 9, 2011 there were 5,534,400 shares, net of treasury shares, of common stock outstanding.

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Forward-Looking Statements: 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. The words “believe,” “may,” “estimate,” “continue,” “anticipate,” “intend,” ”should,” “plan,” “could,” “target,” “pote “will,” “expect” and similar expressions, as they relate to the Company are intended to identify forward-looking statements within the meaning of the “safe harbor” provisions of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. 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. New risk factors emerge from time to time and it is not possible to accurately predict all such risk factors, nor can we assess the impact of all such risk factors on our business or the extent to which any risk factor, or combination of risk factors, may cause results to differ materially from those contained in any forward-looking statements. Except as otherwise required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statements or the risk factors described in this Quarterly Report or in the documents we incorporate by reference, whether as a result of new information, future events, changed circumstances or any other reason after the date of this Quarterly Report on Form 10-Q.

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 2010 AND JUNE 30, 2010

		December 31, 2010 (unaudited)		June 30, 2010
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents	$	537,600	$	400,500
Accounts receivable, net		1,984,200		2,493,900
Inventories, net		1,848,900		1,222,500
Assets related to discontinued operations		39,500		1,971,000
Prepaid expenses and other current assets		491,600		654,700
Total current assets		4,901,800		6,742,600
PROPERTY, PLANT AND EQUIPMENT, NET		327,600		233,800
OTHER ASSETS				
Goodwill		12,575,400		12,575,400
Other intangible assets, net		554,700		770,200
Other assets		32,100		174,200
Total other assets		13,162,200		13,519,800
TOTAL ASSETS	$	18,391,600	$	20,496,200
LIABILITIES AND SHAREHOLDERS' EQUITY				
CURRENT LIABILITIES				
Accounts payable and accrued expenses	$	2,387,700	$	1,917,100
Dividends payable		51,500		56,400
Notes payable, current		4,428,000		6,328,000
Capital leases		14,500		18,100
Customer advances		176,900		4,500
Liabilites related to discontinued operations		1,433,100		1,498,100
Deferred revenue		325,000		309,300
Total current liabilities		8,816,700		10,131,500
LONG-TERM LIABILITIES				
Deferred revenue, long-term		329,800		375,500
Capital leases, long-term		-		5,000
TOTAL LIABILITIES		9,146,500		10,512,000

Preferred Stock - Series B Convertible - 500,000 shares authorized, 116,800 and 111,200 issued and outstanding, respectively	1,154,500	1,098,500
SHAREHOLDERS' EQUITY		
Preferred Stock		
Preferred Stock - Series D Convertible - 500,000 shares authorized, 82,300 and 134,200 shares issued and outstanding, respectively	814,900	1,333,800
Preferred Stock - Series E Convertible - 750,000 shares authorized, 725,000 and 735,000 shares issued and outstanding, respectively	3,165,900	3,210,900
Common Stock		
Class A - 75,000,000 shares authorized, 5,507,600 and 4,665,500 shares, net of 200 treasury shares valued at $2,800 and 2,000 valued at $30,000, outstanding at December 31, 2010 and June 30, 2010, respectively	109,336,200	107,355,700
Class B - 25,000,000 shares	-	-

authorized and 0 shares oustanding				
Accumulated deficit		(105,226,400)		(103,014,700)
Total shareholders' equity		8,090,600		8,885,700
TOTAL LIABILITIES & SHAREHOLDERS' EQUITY	$	18,391,600	$	20,496,200

See accompanying notes to the condensed consolidated financial statements

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ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE THREE MONTHS ENDED DECEMBER 31, (unaudited)

	2010	2009
NET SALES	$ 3,958,200	$ 3,627,200
Cost of goods sold	2,475,300	2,297,100
GROSS PROFIT	1,482,900	1,330,100
Selling, general and administrative expense	1,587,500	1,235,900
Corporate expense	282,900	269,700
Amortization of stock-based compensation	59,800	70,200
Depreciation and amortizaton	126,300	134,500
OPERATING LOSS	(573,600)	(380,200)
OTHER INCOME & (EXPENSES)		
Interest expense, net	(86,300)	(205,400)
Other income (expense), net	(9,000)	(1,100)
LOSS FROM CONTINUING OPERATIONS	(668,900)	(586,700)
LOSS FROM DISCONTINUED OPERATIONS	(100,000)	(603,600)
NET LOSS	(768,900)	(1,190,300)
Preferred stock dividends	(79,800)	(117,700)
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	$(848,700)	$(1,308,000)
NET LOSS PER COMMON SHARE - BASIC AND DILUTED		
- Continuing operations	$(0.12)	$(0.14)
- Discontinued operations	$(0.02)	$(0.14)
- Preferred stock dividends	$ (0.02)	$(0.03)
- Net loss per share attributable to common shareholders	$(0.16)	$(0.31)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING		
- Basic and diluted	5,437,400	4,241,400

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE SIX MONTHS ENDED DECEMBER 31, (unaudited)

	2010	2009
NET SALES	$ 7,652,800	$ 6,604,100
Cost of goods sold	4,966,500	4,001,500
GROSS PROFIT	2,686,300	2,602,600
Selling, general and administrative expense	3,135,000	2,430,500
Corporate expense	585,800	430,500
Amortization of stock-based compensation	397,700	239,000
Depreciation and amortizaton	256,500	270,100
OPERATING LOSS	(1,688,700)	(767,500)
OTHER INCOME & (EXPENSES)		
Interest expense, net	(254,100)	(379,900)
Other income (expense), net	(9,300)	(1,900)
LOSS FROM CONTINUING OPERATIONS	(1,952,100)	(1,149,300)
LOSS FROM DISCONTINUED OPERATIONS	(100,000)	(1,106,400)
NET LOSS	(2,052,100)	(2,255,700)
Preferred stock dividends	(159,600)	(258,200)
NET LOSS ATTRIBUTABLE TO COMMON SHAREHOLDERS	$(2,211,700)	$(2,513,900)
NET LOSS PER COMMON SHARE - BASIC AND DILUTED		
- Continuing operations	$(0.37)	$(0.28)
- Discontinued operations	$(0.02)	$(0.26)
- Preferred stock dividends	$(0.03)	$(0.06)
- Net loss per share attributable to common shareholders	$(0.42)	$(0.60)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING		
- Basic and diluted	5,265,800	4,158,100

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
FOR THE SIX MONTHS ENDED DECEMBER 31, 2010 (unaudited)

	COMMON STOCK (NET OF TREASURY STOCK)		SERIES D PREFERRED STOCK		SERIES E PREFERRED STOCK		ACCUMULA
	SHARES	AMOUNT	SHARES	AMOUNT	SHARES	AMOUNT	DEFICIT
Balances, June 30, 2010	4,665,500 $	107,355,700	134,200 $	1,333,800	735,000 $	3,210,900 $	(103,014
Shares issued for services	3,100	5,300	-	-	-	-	
Shares issued for payment of notes	1,100	2,100	-	-	-	-	
Shares issued for exercise of warrants	256,200	304,800	-	-	-	-	
Value of stock based compensation	-	400,700	-	-	-	-	
Private offering, net of expenses	384,300	612,400	-	-	-	-	
Series B Preferred dividends, paid in kind	-	-	-	-	-	-	(56
Series D Preferred dividends, paid or accrued	16,600	27,100	-	-	-	-	(20
Conversion of Series D preferred stock to common stock	129,700	518,900	(51,900)	(518,900)	-	-	
Series E Preferred dividends, paid or accrued	34,300	54,900	-	-	-	-	(82
Conversion of Series E preferred							

stock to common stock	15,000	45,000	-	-	(10,000)	(45,000)	
NASDAQ listing fees	-	(17,900)	-	-	-	-	
Treasury share adjustment	1,800	27,200					
Net loss	-	-	-	-	-	-	(2,052
Balances, December 31, 2010	5,507,600	$ 109,336,200	82,300	$ 814,900	725,000	$ 3,165,900	$ (105,226

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE SIX MONTHS ENDED DECEMBER 31, (unaudited)

	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (2,052,100)	$ (2,255,700)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	259,900	324,000
Stock-based compensation	400,700	259,400
Stock issued for services	5,300	19,000
Impairment charge	-	325,000
Interest converted to equity	-	50,000
Fees and interest paid with debt	-	96,200
Changes in operating assets and liabilities:		
Accounts receivable, net	502,200	2,500
Inventories, net	(556,000)	474,300
Costs and estimated earnings in excess of billings on uncompleted contracts	12,700	55,000
Prepaid expenses and other current assets	113,000	119,900
Accounts payable and accrued expenses	297,300	(1,421,800)
Deferred revenue	(46,400)	91,600
Billings in excess of costs and estimated earnings on uncompleted contracts	7,300	(139,700)
Customer advances	172,400	777,400
Other assets	32,200	63,000
Net cash used in operations	(851,500)	(1,159,900)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property, plant and equipment	(4,900)	(10,900)
Proceeds from sale of net RFID Technology segment assets	2,000,000	-
Net cash provided by (used in) investing activities	$ 1,995,100	$ (10,900)

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
FOR THE SIX MONTHS ENDED DECEMBER 31, (continued)

		2010		2009
CASH FLOWS FROM FINANCING ACTIVITIES				
Proceeds from borrowings	$	484,900	$	362,700
Repayment on borrowings		(2,382,800)		(51,200)
Repayment of capital lease		(8,600)		(7,200)
Proceeds from sale of equity instruments, net		944,400		848,300
Cash dividends paid		(26,500)		(5,400)
Other		(17,900)		(19,400)
Net cash provided by (used in) financing activities		(1,006,500)		1,127,800
NET INCREASE (DECREASE) IN CASH		137,100		(43,000)
CASH AND CASH EQUIVALENTS, beginning of period		400,500		726,900
CASH AND CASH EQUIVALENTS, end of period	$	537,600	$	683,900
SUPPLEMENTAL SCHEDULE OF CASH FLOW INFORMATION				
Net cash paid during the period for interest	$	254,100	$	171,500
Non-Cash Activities:				
Value of shares issued for services and credit line amendment	$	5,300	$	19,000
Value of stock issued for payment of notes	$	2,100	$	460,000
Series B preferred stock dividend, paid in kind	$	56,000	$	50,700
Series D preferred stock dividend, paid in kind	$	-	$	166,700
Series D preferred stock dividend, paid in common stock or	$	33,400	$	67,000

accrued				
Series D preferred stock converted to line of credit	$	-	$	1,691,100
Series D preferred stock converted to common stock	$	518,900	$	-
Series E preferred stock dividend, paid in common stock or accrued	$	53,500	$	-
Series E preferred stock converted to common stock	$	45,000	$	-

See accompanying notes to the condensed consolidated financial statements

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note A – Basis of Presentation and Recent Accounting Pronouncements

Alanco Technologies, Inc., an Arizona corporation ("Alanco" or "Company"), has in recent years reported three business segments: Data Storage, Wireless Asset Management and RFID Technology. At June 30, 2010, in compliance with the Company's divestiture plan to divest the Data Storage and RFID Technology segments and invest the proceeds into the Wireless Asset Management segment, the Data Storage and RFID Technology segments had either been sold or were presented as "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale". The Wireless Asset Management segment was the only business segment classified as a continuing operation at December 31, 2010.

As previously reported, the Company has solicited investment banker advice to evaluate strategic alternatives available to enhance shareholder value and is continuing its evaluation of those alternatives. Although the Company is committed to maximizing shareholder value and will continue to evaluate it strategic initiatives, there can be no assurance of any particular outcome or course of action.

The Company announced on August 26, 2010 that the Board of Directors had elected to effect a 1 for 8 reverse stock split that was effective on August 27, 2010, when the Company's common stock began trading on a post split-adjusted basis under the interim trading symbol "ALAND" for a period of 20 days, after which the Company's trading symbol returned to "ALAN". (The Company again began trading under the symbol "ALAN" on September 27, 2010.) The Company had previously received authority from its shareholder to effect a reverse split at a ratio within a specified range, if and as determined by the Board of Directors, in order to maintain NASDAQ listing.

As a result of the reverse split, each eight (8) shares of the Company's Class A Common Stock outstanding at the time of the reverse split was automatically reclassified and changed into one share of common stock, and the total number of common shares outstanding was reduced from approximately 41.7 million shares to approximately 5.2 million shares post split. The reverse stock split resulted in the same adjustment to the Company's outstanding stock options and securities reserved for issuance under its current incentive plans. No fractional shares were issued in connection with the reverse stock split. Upon surrender of their stock certificates, shareholders have received or will receive, cash in lieu of the fractional shares to which they would otherwise be entitled. All per share amounts and outstanding shares, including all common stock equivalents (stock options, warrants and convertible securities) have been restated in the Condensed Consolidated Financial Statements, the Notes to the Consolidated Financial Statements and the loss per share for all periods presented to reflect the reverse stock split.

The unaudited condensed consolidated financial statements presented herein have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and in accordance with the instructions to Form 10-Q. Accordingly, certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. In our opinion, the accompanying condensed consolidated financial statements include all adjustments necessary for a fair presentation of such condensed consolidated financial statements. Such necessary adjustments consist of normal recurring items and the elimination of all significant intercompany balances and transactions.

These interim condensed consolidated financial statements should be read in conjunction with the Company's June 30, 2010 Annual Report filed on Form 10-K. Interim results are not necessarily indicative of results for a full year. Certain reclassifications may have been made to conform prior period financials to the presentation in the current reporting period. The reclassifications had no effect on net loss.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statement and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

The Company received a letter of reprimand from Nasdaq on December 28, 2010 concerning Nasdaq's belief that the Company has failed to maintain a majority of independent directors on its Board of Directors in violation of Nasdaq rule 5605 (b)(1), and had a non-independent director on its Nominating Committee in violation of Nasdaq Rule 5605 (e)(1). In particular, Nasdaq has determined that Donald E. Anderson, who served as a director from June 2002 until his resignation on October 4, 2010 and was a member of the Company's Nominating Committee, should not have been classified as an independent director under Nasdaq Rule 5605(a)(2)(d). The Company relied upon outside counsel who determined that the instrument representing the Company's obligation to repay a long term loan by a Trust involving Mr. Anderson constituted a security and that the exception provided by Nasdaq Rule 5605(a)(2)(D)(i) applied. Although there is no Nasdaq Rule or published interpretation to the contrary, Nasdaq staff determined that said obligation of the Company does not constitute a security for purposes of the exemption and Mr. Anderson was therefore not independent.

Nasdaq also found that the Company's violation does not appear to have been the result of a deliberate intent to avoid compliance and was based upon advice of outside counsel. Therefore, the appropriate sanction is issuance of the Letter of Reprimand. The Company has until its next Annual Meeting of Shareholders anticipated to occur in April 2011 to regain compliance with Nasdaq Rule 5605(b)(1).

The Company has stock-based compensation plans and reports stock-based compensation expense for all stock-based compensation awards based on the estimated grant date fair value. The value of the compensation cost is amortized at a minimum on a straight-line basis over the requisite service periods of the award (generally the option vesting term).

The Company estimates fair value using the Black-Scholes valuation model. Assumptions used to estimate compensation expense are determined as follows:

- Expected term is determined under the simplified method using an average of the contractual term and vesting period of the award as appropriate statistical data required to properly estimate the expected term was not available;

- Expected volatility of award grants made under the Company's plans is measured using the historical daily changes in the market price of the Company's common stock over the expected term of the award;

- Risk-free interest rate is to approximate the implied yield on zero-coupon U.S. Treasury bonds with a remaining maturity equal to the expected term of the awards; and,

- Forfeitures are based on the history of cancellations of awards granted by the Company and management's analysis of potential future forfeitures.

Long-lived assets and intangible assets – The Company reviews carrying values at least annually or whenever events or circumstances indicate the carrying values may not be recoverable through projected discounted cash flows.

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, accounts payable, accrued liabilities, and notes payable approximate fair value given their short-term nature or with regards to long-term notes payable based on borrowing rates currently available to the Company for loans with similar terms and maturities.

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

Recent Accounting Pronouncements

With the exception of those discussed below, there have been no recent accounting pronouncements or changes in accounting pronouncements during the six months ended December 31, 2010, that are of significance, or potential significance, to us.

In October 2008, the EITF issued guidance which addresses the accounting when entities enter into revenue arrangements with multiple payment streams for a single deliverable or a single unit of accounting. The Company has adopted the guidance which does not have an impact on its financial position and results of operations at this time.

In December 2010, the FASB issued guidance which addresses the pro forma disclosure requirements for business combinations. The guidance is effective for acquisition dates on or after the beginning of the first annual reporting period after December 15, 2010. The Company has adopted the guidance which does not have an impact on its financial position and results of operations at this time.

Note B – Stock-Based Compensation and Warrants

The Company has several employee stock option and officer and director stock option plans that have been approved by the shareholders of the Company. The plans require that options be granted at a price not less than market on date of grant and are more fully discussed in our Form 10-K for the year ended June 30, 2010.

The Company uses the Black-Scholes option pricing model to estimate fair value of stock-based awards.

Assumptions for awards of options granted during the six months ended December 31, 2010 were:

	Awards granted six months ended December 31, 2010
Dividend yield	0%
Expected volatility	62%
Weighted-average volatility	62%
Risk-free interest rate	2% - 4%
Expected life of options (in years)	2.0 - 3.75
Weighted average grant-date fair value	$.67

The following table summarizes the Company's stock option activity during the first six months of fiscal 2011:

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

	Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term (1)	Aggregate Fair Value	Aggregate Intrinsic Value (2)
Outstanding July 1, 2010	955,800	$6.27	3.01	$ 4,324,300	-
Shares repriced during period	(866,000)	$5.82	2.78	(3,873,400)	-
Repriced replacement shares	866,000	$1.52	2.78	415,900	-
Granted	110,000	$2.14	4.60	73,800	-
Exercised	-	$0.00	-	-	-
Forfeited or expired	(64,800)	$6.07	-	(293,200)	-
Outstanding December 31, 2010	1,001,000	$1.98	2.76	$ 647,400	$0
Exercisable December 31, 2010	746,600	$2.09	2.30	$ -	$0

(1) Remaining contractual term presented in years.

(2) The aggregate intrinsic value is calculated as the difference between the exercise price of the underlying awards and the closing price of the Company's common stock as of December 31, 2010, for those awards that have an exercise price below the closing price as of December 31, 2010 of $1.40.

As of December 31, 2010, the Company had 201,100 warrants outstanding with a weighted average exercise price of $5.77. The life of the outstanding warrants extends from September 30, 2011 through July 9, 2013. The following table summarizes the Company’s warrant activity during the first six months of fiscal 2011:

	Number of Shares	Weighted Average Exercise Price $
Warrants Outstanding, June 30, 2010	409,000	$ 11.47

Granted	95,100	2.64
Exercised	(256,200)	1.19
Canceled/Expired	(46,800)	24.00
Warrants Outstanding, December 31, 2010 (unaudited)	201,100	$ 5.77

Note C – Inventories

Inventories are recorded at the lower of cost or market. During the quarter ended December 31, 2010, the Company wrote off obsolete inventory against the recorded reserve. The composition of inventories as of December 31, 2010 and June 30, 2010 are summarized as follows:

ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

	December 31, 2010 (unaudited)	June 30, 2010
Raw materials and purchased parts	$ 1,848,900	$ 1,637,500
Finished goods	-	-
	1,848,900	1,637,500
Less reserves for obsolescence	-	(415,000)
	$ 1,848,900	$ 1,222,500

Note D – Discontinued Operations

During fiscal 2009, the Company implemented a plan to divest the operations of its Data Storage segment and reinvest the proceeds into the remaining business segments. The Company expanded its divestiture plan during the quarter ended September 30, 2009 to include the RFID Technology segment. During the quarter ended March 31, 2010, the Company executed an agreement to sell substantially all of the assets and liabilities of its Data Storage segment. Accordingly, the "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale" presented in the June 30, 2010 balance sheet consist primarily of the RFID Technology segment. The reclassification of those segment assets and liabilities to "Assets Held for Sale" and "Liabilities Related to Assets Held for Sale" does not affect the reported net loss for the periods presented.

On August 18, 2010, the Company announced the divestiture of Alanco/TSI PRISM, Inc. ("TSI") operations, the Company's RFID Technology segment, with the sale of substantially all of the assets and business of TSI to Black Creek Integrated Systems Corp., a private company located in Irondale, Alabama. The transaction, which closed August 17, 2010, consisted of approximately $2 million in cash, and a potential earn-out that could approach five hundred thousand to one million dollars. (The earn-out has not been valued in the transaction due to the lack of supportability.) With the previously announced sale of the Company's Data Storage segment, the transaction marks the substantial completion of the Company's asset divestiture program and redeployment of resources to focus upon the future of the Company and growth of the Company's StarTrak wireless asset management business. At December 31, 2010, the "Assets Related to Discontinued Operations" and "Liabilities Related to Discontinued Operations" represent assets retained by seller or receivables resulting from the sales transaction, and liabilities not assumed in the transactions. The divestiture program significantly improved Alanco's financial position by reducing secured debt and eliminating the large operating losses associated with the divested businesses.

During the fourth quarter ended June 30, 2010, the Company recorded an impairment charge of $4.5 million, reducing the RFID Technology segment values in anticipation of a sale. The impairment charge was made as of June 30, 2010 with knowledge of the RFID Technology transaction sales value as well as knowledge of the segment's operating results for the period from July 1, 2010 through the August 17, 2010 sale date of ($142,200) on sales of $38,700. The operating loss had been accrued at June 30, 2010 as it represented the minimum cost to maintain the operation for sale and resulted in no income or loss from discontinued operations reported for the six months ending December 31, 2010. The RFID Technology segment operating loss for the six months ended December 31, 2009 was $754,000, or $.18 per share on sales of $563,700.

The results for Discontinued Operations (Data Storage segment and RFID Technology segment) for the six months and three months ended December 31, 2010 and 2009 were as follows:

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ALANCO TECHNOLOGIES, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (continued)

	Six Months Ended December 31, 2010	Six Months Ended December 31, 2009	Three Months Ended December 31, 2010	Three Months Ended December 31, 2009
Sales				
Data Storage	$ -	$ 829,500	$ -	$ 358,700
RFID Technology	38,700	563,700	-	331,800
Total Sales	$ 38,700	$ 1,393,200	$ -	$ 690,500
Gross Profit				
Data Storage	$ -	$ 284,200	$ -	$ 112,000
RFID Technology	13,500	114,300	-	123,000
Total Gross Profit	$ 13,500	$ 398,500	$ -	$ 235,000
Gross Margin				
Data Storage	-	34.3%	-	31.2%
RFID Technology	34.9%	20.3%	-	37.1%
Total Gross Margin	34.9%	28.6%	-	34.0%
Selling, General and Administrative Expense				
Data Storage	$ -	$ 311,600	$ -	$ 146,000
Data Storage asset impairment charge	100,000	325,000	100,000	325,000
RFID Technology	155,700	868,300	-	367,600
	$ 255,700	$ 1,504,900	$ 100,000	$ 838,600

Total SG&A Expense				
Income (Loss) from Discontinued Operations				
Data Storage	$ (100,000)	$ (352,400)	$ (100,000)	$ (359,000)
RFID Technology	-	(754,000)	-	(244,600)
Total Operating Income (Loss)	$ (100,000)	$ (1,106,400)	$ (100,000)	$ (603,600)
Capital Expenditures				
Data Storage	$ -	$ -	$ -	$ -
RFID Technology	-	5,600		