FONAR CORP
Form 10-Q
February 09, 2007

FORM 10-Q
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

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

For the quarterly period ended DECEMBER 31, 2006

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For the transition period from ____________ to _____________

Commission file number 0-10248

FONAR CORPORATION
(Exact name of registrant as specified in its charter)

DELAWARE	11-2464137
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

110 Marcus Drive Melville, New York 11747
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (631) 694-2929

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 for the past 90 days. YES X NO ____

Indicate by check mark whether the registrant is an accelerated filer (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 close of the latest practicable date.

Class	Outstanding at January 31, 2007
Common Stock, par value $.0001	121,559,660
Class B Common Stock, par value $.0001	3,953
Class C Common Stock, par value $.0001	9,562,824
Class A Preferred Stock, par value $.0001	7,836,287

FONAR CORPORATION AND SUBSIDIARIES
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FONAR CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS
(000's OMITTED)

ASSETS	December 31, 2006 (UNAUDITED)	June 30, 2006
Current Assets:		
Cash and cash equivalents	$ 4,964	$ 4,557
Marketable securities	3,705	4,938
Accounts receivable - net	4,867	3,359
Accounts receivable - related parties - net	454	499
Medical receivables	4,497	6,053
Management fee receivable - related medical practices - net	7,272	7,323
Costs and estimated earnings in excess of billings on uncompleted contracts	127	2,958
Inventories	6,347	7,077
Investment in sales-type lease	-	279
Current portion of advances and notes to related medical practices	156	90
Current portion of note receivable less discount for below market interest	559	459
Prepaid expenses and other current assets	1,596	1,280
Total Current Assets	34,544	38,872
Property and equipment - net	5,877	6,667
Advances and notes to related medical practices - net	575	676
Notes receivable less discount for below market interest	5,425	5,719
Other intangible assets - net	5,137	4,930
Other assets	1,650	366
Total Assets	$ 53,208	$ 57,230

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(000's OMITTED)

LIABILITIES AND STOCKHOLDERS' EQUITY	December 31, 2006 (UNAUDITED)	June 30, 2006
Current Liabilities:		
Current portion of long-term debt and capital leases	$ 243	$ 234
Accounts payable	3,929	4,886
Other current liabilities	6,411	6,102
Unearned revenue on service contracts	5,456	4,238
Unearned revenue on service contracts - related parties	490	544
Customer advances	10,102	5,464
Customer advances - related party	42	42
Income taxes payable	-	8
Billings in excess of costs and estimated earnings on uncompleted contracts	1,760	2,979
Billings in excess of costs and estimated earnings on uncompleted contracts - related party	-	137
Total Current Liabilities	28,433	24,634
Long-Term Liabilities:		
Due to related medical practices	93	93
Long-term debt and capital leases, less current portion	1,068	1,172
Other liabilities	192	215
Total Long-Term Liabilities	1,353	1,480
Total Liabilities	29,786	26,114
Minority interest	691	697

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(000's OMITTED, except share data)

December 31, June 30,

LIABILITIES AND STOCKHOLDERS' EQUITY (continued)	2006 (UNAUDITED)	2006
STOCKHOLDERS' EQUITY		
Class A non-voting preferred stock $.0001 par value; 8,000,000 authorized, 7,836,287 issued and outstanding at December 31, 2006 and June 30, 2006	1	1
Common Stock $.0001 par value; 150,000,000 shares authorized at December 31, 2006 and June 30, 2006, 121,705,391 issued at December 31, 2006 and 114,995,094 at June 30, 2006; 121,414,327 outstanding at December 31, 2006 and 114,704,030 at June 30, 2006	12	11
Class B Common Stock $ .0001 par value; 4,000,000 shares authorized, (10 votes per share), 3,953 issued and outstanding at December 31, 2006 and June 30, 2006	-	-
Class C Common Stock $.0001 par value; 10,000,000 shares authorized, (25 votes per share), 9,562,824 issued and outstanding at December 31, 2006 and June 30, 2006	1	1
Paid-in capital in excess of par value	172,003	168,412
Accumulated other comprehensive loss	(133)	(246)
Accumulated deficit	(147,908)	(136,333)
Notes receivable from employee stockholders	(570)	(752)
Treasury stock, at cost - 291,064 shares of common stock at December 31, 2006 and June 30, 2006	(675)	(675)
Total Stockholders' Equity	22,731	30,419
Total Liabilities and Stockholders' Equity	$ 53,208	$ 57,230

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(000's OMITTED, except per share data)

	FOR THE THREE MONTHS ENDED DECEMBER 31,	
	2006	2005

REVENUES		
Product sales - net	$ 2,082	$ 1,829
Product sales - related parties - net	2	2,337
Service and repair fees - net	2,211	1,854
Service and repair fees - related parties - net	238	250
Management and other fees - related medical practices - net	3,139	3,044
License fees and royalties	-	1,227
Total Revenues - Net	7,672	10,541
COSTS AND EXPENSES		
Costs related to product sales	2,369	1,822
Costs related to product sales - related parties	2	1,907
Costs related to service and repair fees	1,056	1,201
Costs related to service and repair fees - related parties	114	161
Costs related to management and other fees - related medical practices	2,220	2,387
Research and development	1,379	1,725
Selling, general and administrative, inclusive of compensatory element of stock issuances of $ 23 and $ 545 for the three months ended December 31, 2006 and 2005, respectively	5,795	6,857
Provision for bad debts	136	25
Total Costs and Expenses	13,071	16,085
Loss From Operations	(5,399)	(5,544)
Interest Expense	(73)	(90)
Investment Income	230	238
Interest Income - Related Parties	11	2
Other Income	39	321
Minority Interest in Income of Partnerships	(278)	(285)
NET LOSS	$(5,470)	$(5,358)
Net Loss Available to Common Stockholders	$(5,470)	$(5,358)
Basic Loss Per Common Share	$ (.05)	$ (.05)
Diluted Loss Per Common Share	$ (.05)	$ (.05)
Basic and Diluted Earnings Per Share-Common C	N/A	N/A

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(000's OMITTED, except per share data)

	FOR THE SIX MONTHS ENDED DECEMBER 31,	
	2006	2005
REVENUES		
Product sales - net	$ 4,400	$ 5,840

Product sales - related parties - net	142	2,517
Service and repair fees - net	4,491	3,538
Service and repair fees - related parties - net	479	491
Management and other fees - net	-	648
Management and other fees - related medical practices - net	5,943	6,433
License fees and royalties	-	1,227
Total Revenues - Net	15,455	20,694
COSTS AND EXPENSES		
Costs related to product sales	4,811	5,708
Costs related to product sales - related parties	146	2,070
Costs related to service and repair fees	2,299	2,431
Costs related to service and repair fees - related parties	245	337
Costs related to management and other fees	-	528
Costs related to management and other fees - related medical practices	4,224	4,673
Research and development	2,811	3,565
Selling, general and administrative, inclusive of compensatory element of stock issuances of $ 121 and $ 1,069 for the six months ended December 31, 2006 and 2005, respectively	12,223	13,273
Provision for bad debts	186	50
Amortization of management agreements	-	37
Termination costs paid with common stock	-	1,600
Total Costs and Expenses	26,945	34,272
Loss From Operations	(11,490)	(13,578)
Interest Expense	(144)	(164)
Investment Income	429	410
Interest Income - Related Parties	22	6
Other Income	78	218
Minority Interest in Income of Partnerships	(470)	(567)
NET LOSS	$(11,575)	$(13,675)
Net Loss Available to Common Stockholders	$(11,575)	$(13,675)
Basic Loss Per Common Share	$ (.10)	$ (.13)
Diluted Loss Per Common Share	$ (.10)	$ (.13)
Basic and Diluted Earnings Per Share-Common C	N/A	N/A

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(UNAUDITED)

(000'S OMITTED)

FOR THE THREE MONTHS ENDED
DECEMBER 31,

	2006	2005
Net loss	$(5,470)	$(5,358)
Other comprehensive income (loss), net of tax:		
Unrealized gains (losses) on securities, net of tax	27	(127)
Total comprehensive loss	$(5,443)	$(5,485)

	FOR THE SIX MONTHS ENDED DECEMBER 31,	
	2006	2005
Net loss	$(11,575)	$(13,675)
Other comprehensive income (loss), net of tax:		
Unrealized gains (losses) on securities, net of tax	113	(147)
Total comprehensive loss	$(11,462)	$(13,822)

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(000'S OMITTED)

	FOR THE SIX MONTHS ENDED DECEMBER 31,	
	2006	2005
Cash Flows from Operating Activities:		
Net loss	$(11,575)	$(13,675)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		

Minority interest in income of partnerships	470	567
Depreciation and amortization	1,321	1,659
Provision for bad debts	186	50
Compensatory element of stock issuances	121	1,069
Stock issued for costs and expenses	1,815	2,891
Termination costs paid with common stock	-	1,600
Amortization of unearned compensation	-	182
Gain on sale of equipment	-	(3)
Loss from sale of physical medicine management business	-	144
(Increase) decrease in operating assets, net:		
Accounts, management fee and medical receivable(s)	(43)	(522)
Notes receivable	194	(28)
Costs and estimated earnings in excess of billings on uncompleted contracts	2,831	5,447
Inventories	730	1,664
Principal payments received on sales type lease	279	84
Prepaid expenses and other current assets	(315)	(122)
Other assets	(49)	26
Advances and notes to related medical practices	35	54
Increase (decrease) in operating liabilities, net:		
Accounts payable	(957)	(2,544)
Other current liabilities	1,472	770
Customer advances	4,638	626
Billings in excess of costs and estimated earnings on uncompleted contracts	(1,357)	1,316
Other liabilities	(23)	(23)
Due to related medical practices	-	(35)
Income taxes payable	(8)	(11)
Net cash (used in) provided by operating activities	(235)	1,186

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
(000'S OMITTED)

	FOR THE SIX MONTHS ENDED DECEMBER 31,	
	2006	2005
Cash Flows from Investing Activities:		
Sales of marketable securities	1,345	2,684
Purchases of property and equipment	(164)	(1,010)
Costs of capitalized software development	(340)	(373)
Cost of patents and copyrights	(235)	(195)
Proceeds from sale of equipment	-	97

Net cash provided by investing activities	606	1,203
Cash Flows from Financing Activities:		
Distributions to holders of minority interest	(475)	(421)
Proceeds from long-term debt	-	391
Repayment of borrowings and capital lease obligations	(94)	(202)
Net proceeds from exercise of stock options and warrants	50	500
Net proceeds from sale of stock	373	-
Repayment of notes receivable from employee stockholders	182	175
Net cash provided by financing activities	36	443
Net Increase in Cash and Cash Equivalents	407	2,832
Cash and Cash Equivalents - Beginning of Period	4,557	5,517
Cash and Cash Equivalents - End of Period	$ 4,964	$ 8,349

See accompanying notes to condensed consolidated financial statements (unaudited).

FONAR CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006
(UNAUDITED)

NOTE 1 - BASIS OF PRESENTATION & LIQUIDITY & CAPITAL RESOURCES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of

management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the six months ended December 31, 2006 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2007. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K filed on September 20, 2006 for the fiscal year ended June 30, 2006.

Liquidity and Capital Resources

The Company's principal source of liquidity has been cash flows provided by operations. The Company's management currently expects this to continue. At December 31, 2006, the Company had working capital of $6.1 million. For the six months ended December 31, 2006, the Company incurred a net loss of $11.6 million which included non-cash charges of $3.4 million.

In order to conserve our capital resources the Company has and will continue to issue, from time to time, common stock and stock options to compensate employees and non-employees for goods and services. The Company is focusing on increased advertising and marketing campaigns and distribution programs to increase the demand for Fonar's products. Management anticipates that Fonar's capital resources will improve as Fonar's MRI scanner products gain wider market recognition and acceptance resulting in increased product sales. If the Company is not successful with its current marketing efforts to increase sales, then the Company could experience a shortfall in cash necessary to sustain operations at their current levels.

Given the Company's December 31, 2006 cash and marketable securities balance of $8.7 million and the Company's forecasted cash requirements, the Company anticipates that its existing capital resources, funds generated from operations and funds expected to be received from note repayments, will be sufficient to satisfy its cash flow requirements through at least December 31, 2007. Based on current results of operations, the Company believes it will either need to increase sales, reduce expenses or seek other sources of funds through the issuance of equity or debt financing in order to maintain sufficient funds available to operate subsequent to December 31, 2007.

FONAR CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006
(UNAUDITED)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The consolidated financial statements include the accounts of FONAR Corporation, its majority and wholly-owned subsidiaries and partnerships (collectively the "Company"). All significant intercompany accounts and transactions have been eliminated in consolidation.

Earnings (Loss) Per Share

Basic earnings (loss) per share ("EPS") is computed based on weighted average

shares outstanding and excludes any potential dilution. In accordance with EITF 03-6, "Participating Securities and the Two-Class method under FASB Statement No. 128" ("EITF 03-6"), the Company's participating convertible securities, which include Class B common stock and Class C common stock, are not included in the computation of basic EPS for six months ended December 31, 2006 and 2005, because the participating securities do not have a contractual obligation to share in the losses of the Company.

Diluted EPS reflects the potential dilution from the exercise or conversion of all dilutive securities into common stock based on the average market price of common shares outstanding during the period. The number of common shares potentially issuable upon the exercise of certain options and warrants or conversion of the participating convertible securities that were excluded from the diluted EPS calculation was approximately 6,982,000 and 7,025,000 because they are antidilutive as a result of a net loss for the six months ended December 31, 2006 and 2005, respectively.

Stock Options and Warrants and Similar Equity Instruments

In December 2004, the FASB issued SFAS No. 123 (revised 2004), "Share-Based Payment" SFAS 123R. SFAS 123R requires the compensation cost relating to stock-based payment transactions be recognized in financial statements. That cost will be measured based on the fair value of the equity or liability instruments issued on the grant date of such instruments, and will be recognized over the period during which an individual is required to provide service in exchange for the award (typically the vesting period). SFAS 123R covers a wide range of stock-based compensation arrangements including stock options, restricted stock plans, performance-based awards, stock appreciation rights, and employee stock purchase plans. SFAS 123R replaces SFAS 123 and supersedes APB Opinion 25.

On July 1, 2005, the Company adopted SFAS 123R using the modified prospective method, in which compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS 123R for all share-based payments granted after the effective date and (b) based on the fair value as measured under SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123R that remain unvested on the effective date.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006
(UNAUDITED)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Stock Options and Warrants and Similar Equity Instruments (Continued)

Accordingly, the adoption of SFAS 123R's fair value method did not have a significant impact on our result of operations. SFAS 123R requires the benefits of tax deductions in excess of recognized compensation cost to be reported as a financing cash flow, rather than as an operating cash flow as required under current literature. It is unlikely that the Company will have near term benefits from tax deductions. This requirement will reduce net operating cash flows and increase net financing cash flows in periods after adoption. The Company cannot estimate what those amounts will be in the future because of various factors, including but not limited to the timing of employee exercises and whether the Company will be in a taxable position. At this time, there would be no tax impact related to the prior periods since the Company has a net loss.

Recent Accounting Pronouncements

In February 2006, the FASB issued SFAS NO. 155, Accounting for Certain Hybrid Financial Instruments-An Amendment of FASB No. 133 and 140. The purpose of SFAS statement No. 155 is to simplify the accounting for certain hybrid financial instruments by permitting fair value re-measurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation. SFAS No. 155 also eliminates the restriction on passive derivative instruments that a qualifying special-purpose entity may hold. SFAS No. 155 is effective for all financial instruments acquired or issued after the beginning of any entity's first fiscal year beginning after September 15, 2006. We believe that the adoption of this standard on July 1, 2007 will not have a material effect on our consolidated financial statements.

In March 2006, the FASB issued SFAS No. 156, Accounting for Servicing of Financial Assets, an Amendment of SFAS No. 140. SFAS No. 156 requires separate recognition of a servicing asset and a servicing liability each time an entity undertakes and obligation to service a financial asset by entering into a servicing contract. This statement also requires that servicing assets and liabilities be initially recorded at fair value and subsequently adjusted to the fair value at the end of each reporting period. This statement is effective in fiscal years beginning after September 15, 2006. We believe that the adoption of this standard on July 1, 2007 will not have a material effect on our consolidated financial statements.

In June, 2006, the FASB issued Interpretation No. 48, "Accounting of Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109". This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. This Interpretation is effective for fiscal years beginning after December 31, 2006.

The Company is assessing the impact of this Interpretation on its consolidated financial statements, but does not expect it to have a material effect.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Recent Accounting Pronouncements (Continued)

In September, 2006, the FASB issued SFAS No. 157, "Fair Value Measurements", which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This standard applies under other accounting pronouncements that require or permit fair value measurements, but does not require any new fair value measurements. SFAS No. 157 will become effective for us in 2009. We are currently assessing the impact of SFAS No. 157; however, we do not believe the adoption of this standard will have a material effect on our consolidated financial statements.

In September, 2006, the FASB issued SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans", which requires us to recognize the funded status of our defined benefit plans in the consolidated balance sheets and changes in the funded status in comprehensive income. This

standard also requires us to recognize the gains/losses, prior year service costs and transition assets/obligations as a component of other comprehensive income upon adoption, and provide additional annual disclosure. SFAS No. 158 does not affect the computation of benefit expense recognized in our consolidated statements of operations. The recognition and disclosure provisions are effective in 2007. In addition, SFAS No. 158 requires us to measure plan assets and benefit obligations as of the year-end balance sheet date effective in 2009. We are required to apply the provisions of this standard prospectively. We are currently assessing the impact of SFAS No. 158 on our consolidated financial statements.

In September, 2006, the SEC staff issued Staff Accounting Bulletin ("SAB") No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements". This guidance indicates that the materiality of a misstatement must be evaluated using both the rollover and iron curtain approaches. The iron curtain approach quantifies a misstatement based on the amount of the error originating in the current year income statement. SAB No. 108 is effective for our 2007 annual consolidated financial statements. We are currently assessing the impact of SAB No. 108; however, we do not believe the adoption of this standard will have a material effect on our consolidated financial statements.

In October, 2005, the FASB issued FSP FAS 123(R)-2, "Practical Accommodation to the Application of Grant Date as Defined in FASB Statement No. 123(R)", which provides clarification of the concept of mutual understanding between employer and employee with respect to the grant date of a share-based payment award. This FSP provides that a mutual understanding of the key terms and conditions of an award shall be presumed to exist on the date the award is approved by management if the recipient does not have the ability to negotiate the key terms and conditions of the award and those key terms and conditions will be communicated to the individual recipient within a relatively short time period after the date of approval. This guidance was applicable upon the initial adoption of SFAS 123(R). The adoption of this pronouncement did not have an impact on the Company's consolidated financial position, results of operations, or cash flows.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Reclassifications

Certain prior year amounts have been reclassified to conform to the current year presentation. The reclassifcations did not have any effect on reported net losses for any periods presented.

NOTE 3 - MEDICAL RECEIVABLES, ACCOUNTS RECEIVABLE AND MANAGEMENT FEE RECEIVABLE

Medical Receivables

The Company was assigned medical receivables valued at $11,775,000, in connection with the satisfaction of the management fees and termination fees related to a Termination and Replacement Agreement dated May 23, 2005. The balance of the medical receivables as of December 31, 2006 was $4,497,000.

Accounts Receivable and Management Fee Receivable

Receivables, net is comprised of the following at December 31, 2006:
(000's Omitted)

	Gross Receivable	Allowance for doubtful accounts	Net
Receivables from equipment sales and service contracts	$ 5,597	$ 730	$ 4,867
Receivables from equipment sales and service contracts-related parties	$ 1,100	$ 646	$ 454
Management fee receivables from related medical practices ("PC's")	$10,425	$ 3,153	$ 7,272

The Company's customers are concentrated in the healthcare industry.

The Company's receivables from the related PC's consist substantially of fees outstanding under management agreements, service contracts and lease agreements. Payment of the outstanding fees is based on collection by the PC's of fees from third party medical reimbursement organizations, principally insurance companies and health management organizations.

NOTE 3 - MEDICAL RECEIVABLES, ACCOUNTS RECEIVABLE AND MANAGEMENT FEE RECEIVABLE (Continued)

Accounts Receivable and Management Fee Receivable (Continued)

Collection by the Company of its accounts receivable may be impaired by the uncollectibility of the PC's medical fees from third party payors, particularly insurance carriers covering automobile no-fault and workers compensation claims due to longer payment cycles and rigorous informational requirements and certain other disallowed claims. Approximately 41% and 48% of the PC's net revenues for both the six months ended December 31, 2006 and 2005, respectively, were derived from no-fault and personal injury protection claims. The Company considers the aging of its accounts receivable in determining the amount of allowance for doubtful accounts and contractual allowances. The Company generally takes all legally available steps to collect its receivables. Credit losses associated with the receivables are provided for in the condensed consolidated financial statements and have historically been within management's expectations.

Certain no-fault insurers have raised issues concerning whether the Company's clients the "P.C.'s" are in compliance with certain laws, including, but not limited to, laws governing their corporate structure and/or licensing, their

entitlement or standing to seek and/or obtain no-fault benefits, and/or laws prohibiting the corporate practice of medicine, fee-splitting and/or physician self referrals. To the extent any claims are asserted against the P.C.'s, the settlement of such claims could result in the P.C.'s waiving their rights to collect certain of their insurance claims. Management believes that the company and the P.C.'s are not in violation of any of the above mentioned laws. Since the resolution or settlement of these claims with the insurance companies could have a material impact on the collection of management fees by the Company from its P.C.'s, the Company has provided reserves for uncollectable fees related to this matter.

On February 8, 2006, the Deficit Reduction Act of 2005 ("DRA") was signed into law by President George W. Bush. The DRA would result in caps on Medicare and Medicaid payment rates for most imaging services, including MRI and CT, furnished in physicians' offices and other non-hospital based settings. Under the cap, payments for these imaging services could not exceed the hospital outpatient payment rates for those services. This change is to apply to services furnished by the P.C.'s on or after January 1, 2007. Although the professional corporations managed by HCMA bill for scans on a "global" basis, which means a single fee per scan, the limitation is applicable only to the technical component of the services, which is the payment or portion of the payment attributable to the non-professional services. If the fee for the technical component of the service (without including geographic adjustments) exceeds the hospital outpatient payment amount for the service (also without including geographic adjustments), under the Physician Fee Schedule, then the payment would be limited to the Physician Fee Schedule rate. Based on the Company's scan volumes for 2006, the Company estimates that the implementation of the reimbursement reduction contained in the DRA may have the impact of reducing the Company's management fee revenues by approximately $800,000 annually.

NOTE 3 - MEDICAL RECEIVABLES, ACCOUNTS RECEIVABLE AND MANAGEMENT FEE RECEIVABLE (Continued)

Accounts Receivable and Management Fee Receivable (Continued)

Currently, a statute in the State of Florida requires all drivers, licensed in the State of Florida, to carry a $10,000 no-fault insurance policy covering personal injury protection benefits. This statute is due to expire in October 2007 unless extended by legislative actions. Management does not believe that the expiration of this statute will have a material impact on the Company's consolidated financial position or results of consolidated operations in the future.

While the Company has prepared certain estimates of the impact of the above discussed changes and possible changes, it is not possible to fully quantify their impact on its business. There can be no assurance that the impact of these changes will not be greater than estimated or that any future health care legislation or reimbursement changes will not adversely affect the Company's business.

Net revenues from management and other fees charged to the related P.C's accounted for approximately 38.5% and 31.1% of the consolidated net revenues for the six months ended December 31, 2006 and 2005, respectively. Product sales and service repair fees from related parties amounted to approximately 4.0% and

14.5% of consolidated net revenues for the six months ended December 31, 2006 and 2005, respectively.

Unaudited Financial Information of Unconsolidated Managed Medical Practices

Summarized income statement data for the three months ended December 31, 2006 and 2005 related to the unconsolidated medical practices managed by the Company is as follows:

(000's omitted) (Income Tax-Cash Basis)

For the three months ended December 31,	2006	2005
Patient Revenue - Net	$5,025	$4,072
Income from Operations	$ 335	$ 109
Net Income (Loss)	$ 107	$ (103)

Summarized income statement data for the six months ended December 31, 2006 and 2005 related to the unconsolidated medical practices managed by the Company is as follows:

(000's omitted) (Income Tax-Cash Basis)

For the six months ended December 31,	2006	2005
Patient Revenue - Net	$9,787	$8,398
Income from Operations	$ 518	$ 111
Net Income (Loss)	$ 48	$ (314)

NOTE 4 - INVENTORIES

Inventories included in the accompanying condensed consolidated balance sheet at December 31, 2006 consist of:

	(000's omitted)
Purchased parts, components and supplies	$ 4,233
Work-in-process	2,114
	$ 6,347

NOTE 5 - COSTS AND ESTIMATED EARNINGS ON UNCOMPLETED CONTRACTS AND CUSTOMER ADVANCES

1) Information relating to uncompleted contracts as of December 31, 2006 is as follows:

	(000's omitted)
Costs incurred on uncompleted Contracts	$ 5,510

Estimated earnings	2,327
	7,837
Less: Billings to date	9,470
	$(1,633)

Included in the accompanying condensed consolidated balance sheet at December 31, 2006 under the following captions:

Costs and estimated earnings in excess of billings on uncompleted contracts	$ 127
Less: billings in excess of costs and estimated earnings on uncompleted contracts	1,760
	$(1,633)

2) Customer advances consist of the following as of December 31, 2006:

	Total	Related Party	Other
Total Advances	$ 19,614	$ 42	$ 19,572
Less: Advances on contracts under construction	9,470	--	9,470
	$ 10,144	$ 42	$ 10,102

FONAR CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2006
(UNAUDITED)

NOTE 6 -STOCKHOLDERS' EQUITY

Common Stock

During the three months ended December 31, 2006:

a) The Company issued 75,000 shares of common stock to employees as compensation valued at $22,500 under stock bonus plans.

During the six months ended December 31, 2006:

a) The Company issued 125,749 shares of common stock to employees as compensation valued at $41,699 under stock bonus plan.

b) The Company issued 175,000 shares of common stock to consultants and others valued at $78,200.

c) The Company issued 5,227,548 shares of common stock for costs and expenses of $1,815,361.

d) The Company issued 92,000 shares of common stock upon the exercise of stock options resulting in proceeds of $49,680.

e) The Company issued 1,090,000 shares of common stock resulting in proceeds

of $372,760.

The Company pays premiums for life insurance on its Chief Executive Officer. The insurance policies were owned by a life insurance trust. The cash surrender value of the life insurance policies, in the approximate amount of $1.2 million, was contributed to capital during the first quarter of 2007 pursuant to a split dollar agreement.

NOTE 7 - OTHER CURRENT LIABILITIES

Other current liabilities in the accompanying condensed consolidated balance sheet consist of the following:

(000's omitted)

	December 31, 2006	June 30, 2006
Royalties	$ 634	$ 716
Accrued salaries, commissions and payroll taxes	1,050	1,146
Accrued interest	535	535
Litigation judgements	193	193
Sales tax payable	2,368	2,181
Other	1,631	1,331
	$ 6,411	$ 6,102

NOTE 8 -SALE OF PHYSICAL MEDICINE MANAGEMENT BUSINESS

On July 28, 2005 Fonar, HMCA and Dynamic entered into an Asset Purchase Agreement with Health Plus Management Services, L.L.C. ("Health Plus"), pursuant to which HMCA and its subsidiary Dynamic sold to Health Plus the portion of their business which was engaged in the business of managing physical therapy and rehabilitation facilities, together with the assets used in the conduct of such business.

The assets sold consisted principally of the management agreements with the physical therapy and rehabilitation facility management business, the physical therapy equipment, a portion of the accounts receivable and furniture and fixtures the Company provided to the physical therapy and rehabilitation facilities.

The purchase price under the Asset Purchase Agreement was $6.6 million, payable pursuant to a promissory note (the "note") in 120 monthly installments commencing on August 28, 2005. The first twelve installments are interest only and the remaining 108 payments will consist of equal installments of principal and interest in the amount of $76,014 each. The note is secured by a first lien on all of the assets of Health Plus, including its accounts receivable. The Note is subject to prepayment provisions to the extent Health Plus resells all or part of the assets and business or utilizes the assets sold as collateral in any debt financing. The note provides for interest at 5% per annum. The fair value assigned to the note was $6,078,068 reflecting a discount of $521,932 for the below market interest rate. The Company recorded a loss of $143,598 on this

transaction during the year ended June 30, 2006.

The two principals of Health Plus were employed by HMCA and Dynamic up to the time of the closing of the business. In consideration for the termination of their employment agreement, these two individuals each became entitled to receive $800,000. In addition, each became entitled to receive $200,000 for collection services to be provided on behalf of HMCA and Dynamic with respect to a portion of the accounts receivable of certain physical therapy and rehabilitation facilities which arose during the period when HMCA was engaged in the management of those facilities. The $1,000,000 payable to each of these individuals was satisfied in shares of Fonar common stock. During the year ended

June 30, 2006 the Company issued 1,871,490 shares totaling $1,995,675. The remaining balance under this obligation at December 31, 2006 is $4,325 which was included in other current liabilities. The Company capitalized $400,000 with respect to collection services. During the year ended June 30, 2006, $400,000 was charged to compensatory element of stock.

For accounting purposes in accordance with accounting principles generally accepted in the United States of America, the Company determined that the classification of the disposed business described above as discontinued operations would not be appropriate. Accordingly, the operating results of the disposed business have been included in continuing operations in the accompanying consolidated financial statements.

NOTE 9 - SALE OF SUBSIDIARY

On January 31, 2006, the Company sold 100% of the stock of Tallahassee Magnetic Resonance Imaging, P.A. to Raymond V. Damadian for a diminimus amount since the liabilities exceed the assets. No gain or loss was recognized on this sale. Revenue recognized from this entity totaled $516,932 for the six months ended December 31, 2005.

NOTE 10 - SEGMENT AND RELATED INFORMATION

The Company operates in two industry segments - manufacturing and the servicing of medical equipment and management of physician practices, including diagnostic imaging services.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies as disclosed in the Company's 10-K as of June 30, 2006. All inter-segment sales are market-based. The Company evaluates performance based on income or loss from operations.

Summarized financial information concerning the Company's reportable segments is shown in the following table:

(000's omitted)

Physician
Management
and

	Medical Equipment	Diagnostic Imaging Services	Totals
For the three months ended December 31, 2006:			
Net revenues from external customers	$ 4,533	$ 3,139	$ 7,672
Inter-segment net revenues	$ 330	$ -	$ 330
Loss from operations	$ (5,035)	$ (364)	$ (5,399)
Depreciation and amortization	$ 390	$ 275	$ 665
Compensatory element of stock issuances	$ 23	$ -	$ 23
Capital expenditures	$ 249	$ 24	$ 273
For the three months ended December 31, 2005:			
Net revenues from external customers	$ 7,497	$ 3,044	$ 10,541
Inter-segment net revenues	$ 141	$ -	$ 141
Loss from operations	$ (4,756)	$ (788)	$ (5,544)
Depreciation and amortization	$ 505	$ 310	$ 815
Compensatory element of stock issuances	$ 545	$ -	$ 545
Capital expenditures	$ 436	$ 486	$ 922

NOTE 10 - SEGMENT AND RELATED INFORMATION (Continued)

(000's omitted)

	Medical Equipment	Physician Management and Diagnostic Imaging Services	Totals
For the six months ended December 31, 2006:			
Net revenues from external customers	$ 9,512	$ 5,943	$ 15,455
Inter-segment net revenues	$ 513	$ -	$ 513
Loss from operations	$(10,612)	$ (878)	$(11,490)
Depreciation and amortization	$ 773	$ 548	$ 1,321
Compensatory element of stock issuances	$ 116	$ 5	$ 121
Capital expenditures	$ 683	$ 56	$ 739
Identifiable assets	$ 28,983	$ 24,225	$ 53,208
For the six months ended December 31, 2005:			
Net revenues from external customers	$ 13,613	$ 7,081	$ 20,694
Inter-segment net revenues	$ 277	$ -	$ 277
Income from operations	$(10,556)	$ (3,022)	$(13,578)
Depreciation and amortization	$ 999	$ 660	$ 1,659
Compensatory element of stock issuances	$ 756	$ 313	$ 1,069
Termination Costs paid with Common Stock	$ -	$ 1,600	$ 1,600
Capital expenditures	$ 677	$ 901	$ 1,578
Identifiable assets - June 30, 2006	$ 31,264	$ 25,965	$ 57,229

NOTE 11 - SUPPLEMENTAL CASH FLOW INFORMATION

During the six months ended December 31, 2006 and December 31, 2005, the Company paid $144,000 and $164,000 for interest, respectively.

Non-Cash Transaction.

During the six months ended December 31, 2006:

a) The Company recorded the cash surrender value of the split dollar life insurance policies of $1,234,000 to additional paid in capital.

NOTE 12 - POTENTIAL DELISTING OF THE COMPANY'S COMMON STOCK

The Company received written notification from The Nasdaq Stock Market on December 22, 2005 that the bid price of its common stock for the last 30 consecutive trading days had closed below the minimum $1.00 per share required for continued listing under Nasdaq Marketplace Rule 4310(c)(4) (the "Rule"). Pursuant to Nasdaq Marketplace Rule 4310(c)(8)(D), the Company has been provided an initial period of 180 calendar days, or until June 20, 2006, to regain compliance. The notice states that the Company has achieved compliance with the Rule if at any time before June 20, 2006 the bid price of the Company's common stock closes at $1.00 per share or more for a minimum of 10 consecutive business days. The Company had been granted an extension to achieve compliance until December 18, 2006

On December 19, 2006, the Company received a Nasdaq Staff Determination indicating that the Company still fails to comply with the minimum bid price requirement for continued listing and therefore is subject to delisting from the Nasdaq Capital Market. The Company has requested a hearing before a Nasdaq Listing Qualifications Panel to review the staff determination. There can be no assurance the Panel will grant the Company's request for continued listing. The hearing will be held on February 15, 2007.

NOTE 13 - SUBSEQUENT EVENT

Common Stock

During the period from January 1, 2007 through January 31, 2007:

a) The Company issued 145,333 shares of common stock for costs and expenses of $42,118.

FONAR CORPORATION AND SUBSIDIARIES

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

For the six month period ended December 31, 2006 (first half of fiscal 2007), we reported a net loss of $11.6 million on revenues of $15.5 million as compared to net loss of $13.7 million on revenues of $20.7 million for the six month period ended December 31, 2005(first half of fiscal 2006).

For the three month period ended December 31, 2006 we reported a net loss of $5.5 million on revenues of $7.7 million as compared to net loss of $5.4 million on revenues of $10.5 million for the three month period ended December 31, 2005.

Sales of our UPRIGHT(TM) MRI scanners were negatively affected primarily by marketing and advertising pressure from our competitors attempting to minimize the unique medical benefits of UPRIGHT(TM) MRI. These companies may not make UPRIGHT(TM) MRI scanners because of Fonar's patents. Prospective customers continue to have concerns relating to increased difficulty in obtaining insurance reimbursements. We are focusing our marketing campaign to bring the benefits of weight-bearing MRI, and its necessity in the proper evaluation of back pain, to the attention of the consumer and ultimately, referring physicians, hospitals, insurers and other third party payors. In addition, we are targeting orthopedic surgeons, since in order to know the proper surgery to perform, the physician needs images of the patient in the position which causes the patient pain and also in positions of flexion and extension to detect the degree of impairment. Our marketing campaign has had a positive effect on Fonar's overall sales activity and should result in increasing numbers of sales of Fonar UPRIGHT(TM) MRI's.

Sales of our scanners may have been adversely affected by the Deficit Reduction Act of 2005 (DRA) which went into effect in calendar 2007 and establishes caps on Medicare and Medicaid payment rates for most imaging services, including MRI, furnished in physicians' offices and other non-hospital based settings. Under the cap, payments for the "technical" (non-professional services) component of these scans could not exceed the hospital outpatient amount under a Physician Fee Schedule. We believe, however, the UPRIGHT(TM) MRI scanners should not be adversely affected but benefit from increased volumes because the UPRIGHT(TM) MRI with multiple positions is a dynamic MRI as compared with the static conventional recumbent- only single

position MRI. The principal reason for the decline in revenues of our wholly owned subsidiary, Health Management Corporation of America for the six-month period ended December 31, 2006, notwithstanding the increase in revenues in the second quarter of fiscal 2007 compared to fiscal 2006 was the sale of its physical therapy and rehabilitation management business in July, 2005. This resulted in a decline in the first quarter of fiscal 2007 compared to fiscal 2006. We also refer to Health Management Corporation of America as "HMCA".

In addition, we are planning to expand our sales force, both in terms of hiring more sales personnel and establishing a network of domestic distributors (we already use distributors for foreign sales) under the direction of our internal sales force.

We also are monitoring the performance of our existing users in order to establish teams to assist underperforming customers improve their scan volume. In addition, we have held seminars to assist customers in their marketing efforts.

Notwithstanding the disappointing MRI scanner sales revenues. The number of units sold remained constant at six during the first half of fiscal 2006 and fiscal 2007.

Importantly, we believe that our efforts to penetrate the hospital market are beginning to show greater results. For the 2006 fiscal year, two Fonar UPRIGHT(TM) MRI scanners were sold to hospitals, one of which is a member of a chain of hospitals. In the first half of fiscal 2007, we sold one Fonar UPRIGHT(TM) MRI scanner to a hospital. The Fonar UPRIGHT(TM) MRI scanner is the only scanner which enables weight-bearing scans of the spine, which is critical in making a correct diagnosis of spine diseases such as low back pain and therefore the key to performing the correct surgery of the spine. There are approximately 916,000 surgical procedures performed on the spine each year as compared to approximately 950,000 cardiac surgeries annually in the United States (including, stents, bypasses, angioplasties, valve replacements, heart transplants and the like).

Forward Looking Statements

Certain statements made in this Quarterly Report on Form 10-Q are "forward-looking statements" (within the meaning of the Private Securities Litigation Reform Act of 1995) regarding the plans and objectives of Management for future operations. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. The forward-looking statements included herein are based on current expectations that involve numerous risks and uncertainties. The Company's plans and objectives are based, in part, on assumptions involving the expansion of business. Assumptions relating to the foregoing involve judgments with respect to, among other things, future economic, competitive and market conditions and future business decisions, all of which are difficult or impossible to predict accurately and many of which are beyond the control of the Company. Although the Company believes that its assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate and, therefore, there can be no assurance that the forward-looking statements included in this Report will prove to be accurate. In light of the significant uncertainties inherent in the forward-looking statement included herein, the inclusion of such information should not be regarded as a representation by the Company or any other person that the objectives and plans of the Company will be achieved.

Results of Operations

The Company operates in two industry segments: the manufacture and servicing of medical (MRI) equipment, the Company's traditional business which is conducted directly by Fonar, and diagnostic facilities management services, which is conducted through Fonar's wholly-owned subsidiary HMCA. During July 2005 HMCA sold the portion of its business engaged in the management of physical therapy and rehabilitation facilities.

Trends in the second quarter of fiscal 2007 include a decrease in product sales revenues. Sales orders for UPRIGHT(TM) MRI scanners, remained constant at six in the first half of fiscal 2006 and the first half of 2007. Although unrelated party sales revenues increased from $1.8 million in the second quarter of fiscal 2006 to $2.1 million, for the first six month period ended December 31, unrelated party scanner sales revenues decreased from $5.8 million in fiscal 2006 to $4.4 million in fiscal 2007. Related party scanner sales revenues decreased in both of the first two quarters of fiscal 2007, from $2.5 million for the six months ended December 31, 2005 to $142,000 for the six months ended December 31, 2006. The Company will continue to focus on increased marketing efforts, including adding additional sales personnel and distributors, to improve sales performance in fiscal 2007.

For the three month period ended December 31, 2006, as compared to the three month period ended December 31, 2005, overall revenues from MRI product sales decreased 50% ($2.1 million compared to $4.2 million). Unrelated party scanner sales ($2.1 million compared to $1.8 million) increased at a rate of 13.8% and related party scanner sales ($2 thousand compared to $2.3 million) decreased 99.9%. Service revenues, however, increased by 16.4% ($2.4 million compared to $2.1 million) because of customers entering into service agreements with Fonar for their scanners following the expiration of the warranty period on their equipment. Overall, for the second quarter of fiscal 2007, revenues for the medical equipment segment decreased by 39.5% to $4.5 million from $7.5 million for the second quarter of fiscal 2006. The revenues generated by HMCA increased, by 3.1% to $3.1 million for the second quarter of fiscal 2007 as compared to $3.0 million for the second quarter of fiscal 2006.

For the six month period ended December 31, 2006, as compared to the six month period ended December 31, 2005, overall revenues from MRI product sales decreased 45.7% ($4.5 million compared to $8.4 million). Unrelated party scanner sales ($4.4 million compared to $5.8 million) decreased at a rate of 24.7% and related party scanner sales ($142 thousand compared to $2.5 million) decreased 94.4%. Service revenues, however, increased by 23.4% ($5.0 million compared to $4.0 million) because of customers entering into service agreements with Fonar for their scanners following the expiration of the warranty period on their equipment. Overall, for the first half of fiscal 2007, revenues for the medical equipment segment decreased by 30.1% to $9.5 million from $13.6 million for the first half of fiscal 2006. The revenues generated by HMCA also decreased, by 16.1% to $5.9 million for the first half of fiscal 2007 as compared to $7.1 million for the first half of fiscal 2006. The decrease in revenues recognized by HMCA resulted primarily from the sale of HMCA's business of managing physical therapy and rehabilitation centers during July 2005.

There were approximately $480 thousand in foreign revenues for the first six months of fiscal 2007 as compared to approximately $1.5 million in foreign revenues for the first six months of fiscal 2006, representing a decrease in foreign revenues of 68%.

Nevertheless, notwithstanding the decrease in our total net revenues of 25.3% from $20.7 million in the first half of fiscal 2006 to $15.5 million in the first half of fiscal 2007, these decreases were accompanied by a decrease of 21.4% in total costs and revenues from $34.3 million in the first half of fiscal 2006 compared to $26.9 million in the first half of fiscal 2007. As a result, our operating loss decreased from $13.6 million in the first half of fiscal 2006

to $11.5 million in the first half of fiscal 2007.

We recognize MRI scanner sales revenues on the "percentage of completion" basis, which means the revenues are recognized as the scanner is manufactured. Revenues recognized in a particular quarter do not necessarily reflect new orders or progress payments made by customers in that quarter. We build the scanner as the customer meets certain benchmarks in its site preparation in order to minimize the time lag between incurring costs of manufacturing and our receipt of the cash progress payments from the customer which are due upon delivery. Consequently, there can be a disparity between the revenues recognized in a fiscal period and the number of product sales. Generally, the recognized revenue results from revenues from a scanner sale being recognized in a fiscal quarter or quarters following the quarter in which the sale was made. Illustrating this point, the revenue from product sales for the first six months of fiscal 2007 decreased 45.7% from the first six months of fiscal 2006 ($4.5 million compared to $8.4 million). We received, however, orders for six UPRIGHT(TM) MRI scanners during the first six months of fiscal 2007 as compared to six orders for UPRIGHT(TM) MRI scanners during the first six months of fiscal 2006.

We believe the decrease in product sales revenues reflect the large variation in sales revenue that is typical of the sale of high unit cost capital equipment, which variation is characteristic of Fonar's 28 year experience selling MRI scanning systems.

Service and repair revenues increased by 16.4%, from $2.1 million for the second quarter of fiscal 2006 to $2.4 million for the second quarter of fiscal 2007.

Service and repair revenues increased by 23.4% from $4.0 million for the first six months of fiscal 2006 to $5.0 million for the first six months of fiscal 2007.

The increases in service and repair revenues are occurring because after the warranty on the MRI scanner expires, the owner will ordinarily enter into a service contract with us to assure continued coverage. We anticipate that for this reason there will continue to be increases in service revenues as warranties on installed scanners expire over time.

Costs related to product sales decreased by 36.4% from $3.7 million in the second quarter of fiscal 2006 to $2.4 million in the second quarter of 2007, reflecting the corresponding decrease in product sales revenues. Costs related to providing service decreased by 14.1% from $1.4 million in the second quarter of fiscal 2006 to $1.2 million in the second quarter of 2007, notwithstanding the increase in service revenues.

Costs related to product sales decreased by 36.3% from $7.8 million in the first six months of fiscal 2006 to $5.0 million in the first six months of 2007, reflecting the corresponding decrease in product sales revenues. Costs related to providing service decreased by 8.1% from $2.8 million in the first six months of fiscal 2006 to $2.5 million in the first six months of 2007, notwithstanding the increase in service revenues.

In brief, costs are incurred concurrently with revenues in accordance with the percentage of completion method.

Service and repair revenues increased at a materially higher rate than the costs related to providing service and repairs. In fact, such costs decreased by 8.1% from $2.8 million for the first half of fiscal 2006 to $2.5 million for the first half of fiscal 2007. Service contract prices are fixed for the term of the contract, which are usually for a term of one year. We believe that an important factor in keeping service costs down is our ability to monitor the performance

of customers' scanners from our facilities in Melville on a daily basis and to detect and repair any irregularities before more serious problems result. We also believe the low cost of providing service reflects the high quality of our products.

Overall, our operating loss for our medical equipment segment was $10.6 million for the first six months of fiscal 2007 as compared to operating loss of $10.6 million for the first six months of fiscal 2006.

HMCA revenues increased in the second quarter of fiscal 2007, by 3.1% to $3.1 million from $3.0 million for the second quarter of fiscal 2006. For the first six months of fiscal 2007, HMCA revenues decreased by 16.1% to $5.9 million from $7.1 million for the first six months of fiscal 2006. HMCA is seeking to increase revenues from the MRI facilities by continuing its program of replacing older scanners at the sites we manage with UPRIGHT(TM) MRI scanners. We now manage ten sites, as compared to eight sites at December 31, 2005, equipped with UPRIGHT(TM) MRI scanners. HMCA experienced an operating loss of $878,000 for the first six months of fiscal 2007 compared to operating loss of $3.0 million for the first six months of fiscal 2006. The greater loss in the first six months of fiscal 2006 was principally the result of a payment of $1.6 million for the termination of two employment agreements in connection with the sale by HMCA of its physical therapy and rehabilitation facility management business and the loss of revenues resulting from the sale of that business during the first quarter of fiscal 2006.

HMCA cost of revenues for the second quarter of fiscal 2007 decreased to $2.2 million as compared to $2.4 million for the second quarter of fiscal 2006. HMCA cost of revenues for the first six months of fiscal 2007 decreased to $4.2 million as compared to $5.2 million for the first six months of fiscal 2006. Rental costs were reduced in fiscal 2007 while repairs and amortization costs where higher in fiscal 2006.

On February 8, 2006, the Deficit Reduction Act of 2005 ("DRA") was signed into law by President George W. Bush. The DRA, which went into effect in the beginning of calendar 2007, places caps on Medicare and Medicaid payment rates for most imaging services, including MRI and CT, furnished in physicians' offices and other non-hospital based settings. Under the cap, payments for these imaging services can not exceed the hospital outpatient payment rates for those services. This change applies to services furnished by the professional corporations managed by HMCA on or after January 1, 2007. Although the professional corporations managed by HCMA bill for scans on a "global" basis, which means a single fee per scan, the limitation is applicable only to the technical component of the services, which is the payment or portion of the payment attributable to the non-professional services. If the fee for the technical component of the service (without including geographic adjustments) exceeds the hospital outpatient payment amount for the service (also without including geographic adjustments), under the Physician Fee Schedule, then the payment would be limited to the Physician Fee Schedule rate. Based on our scan volume for 2006, our estimate of the implementation of the reimbursement reduction contained in the DRA may have the impact of reducing our management fee revenues by approximately $800,000 annually. We believe that the UPRIGHT(TM) MRI is uniquely designed to facilitate increased volumes to compensate any reductions due to the DRA. The UPRIGHT(TM) MRI with multiple positions is dynamic MRI as compared with the static conventional recumbent-only single position MRI.

Currently, a statute in the State of Florida requires all drivers licensed in the State of Florida to carry a $10,000 no-fault insurance policy covering personal injury protection benefits. This statute is due to expire in October 2007 unless it is extended by legislative action. Management does not believe that the expiration of this statute will have a material impact on our consolidated financial position or results of consolidated operations.

While we have prepared certain estimates of the impact of the above discussed changes and possible changes, it is not possible to fully quantify their impact on our business. There can be no assurance that the impact of these changes will not be greater than estimated or that any future health care legislation or reimbursement changes will not adversely affect our business.

Sale of Physical Therapy and Rehabilitation Facility Management Business

Notwithstanding our continuing efforts to increase revenues from the management of MRI scanning facilities, HMCA's revenues declined because of the sale of its business of managing physical therapy and rehabilitation practices. The sale was completed in fiscal 2006 on July 28, 2005. This sale was made in connection with HMCA's decision to focus on the management of diagnostic imaging facilities.

The sale was made pursuant to an asset purchase agreement to Health Plus Management Services, L.L.C., which we also refer to as Health Plus. There is no material relationship between Health Plus and Fonar, HMCA, or any of their respective subsidiaries, directors or officers, or associates of any such person. The two principals of Health Plus were employed by HMCA up to the time of the closing of the transaction. In consideration for the termination of their employment agreements, these two individuals each became entitled to receive $800,000. In addition, each became entitled to receive $200,000 for billing and collection services to be provided on behalf of HMCA with respect to a portion of the accounts receivable of certain physical therapy and rehabilitation facilities which arose during the period when we were engaged in the management of those facilities. The $1,000,000 payable to each of these individuals was payable at our option in shares of Fonar common stock.

The purchase price under the asset purchase agreement was $6.6 million, payable pursuant to a promissory note in 120 monthly installments commencing on August 28, 2005. The first twelve installments are interest only and the remaining 108 payments will consist of equal installments of principal and interest in the amount of $76,014 each. The note is subject to prepayment provisions to the extent Health Plus resells all or part of the assets and business or utilizes the assets sold as collateral in any debt financing. A loss from the sale of $143,598 has been recorded during the quarter ended September 30, 2005. The note provides for interest at 5% per annum. The $6.6 million note was valued at $6,078,068 as a result of a discount for the below market interest rate.

As our consolidated revenues decreased by 27.2% to $7.7 million for the second quarter of fiscal 2007 from $10.5 million for the second quarter of fiscal 2006, the total costs and expenses decreased by 18.7% to $13.1 million for the second quarter of fiscal 2007 from $16.1 million for the second quarter of fiscal 2006. For the first six months of fiscal 2007 the consolidated revenues decreased by 25.3% to $15.5 million from $20.7 million for the first six months of fiscal 2006, the total costs and expenses decreased by 21.4% to $26.9 million for the first six months of fiscal 2007 from $34.3 million for the first six months of fiscal 2006.

Selling, general and administrative expenses decreased by 7.9% from $12.2 million in the first six months of fiscal 2007 from $13.3 million in the first six months of fiscal 2006. The compensatory element of stock issuances decreased by 88.7% from $1.1 million in the first six months of fiscal 2006 to $121,000 in the first six months of fiscal 2007 which is now included in selling general and administrative expenses. This primarily reflected a lesser use of Fonar's stock in lieu of cash to pay employees, consultants and professionals for services.

Research and development expenses decreased by 21.2 % to $2.8 million for

the first six months of fiscal 2007 as compared to $3.6 million for the first six months of fiscal 2006.

Interest expense in the first six months of fiscal 2007 decreased by 12.2% to $144,000 from $164,000 for the first six months of fiscal 2006.

Inventories decreased by 10.3% to $6.3 million at December 31, 2006 as compared to $7.1 million at June 30, 2006 as the Company's product sales revenues decreased and we decreased our purchase of raw materials and components.

Costs and estimated earnings in excess of billings on uncompleted contracts decreased by 95.7% to $127,000 at December 31, 2006 from $3.0 million at June 30, 2006. This decrease resulted from our receipt of installment payments upon delivery to customers whose sites were prepared to receive deliveries.

Management fee and medical receivables and accounts receivable decreased by 0.8% to $17.1 million at December 31, 2006 from $17.2 million at June 30, 2006, primarily due to collections on the Company's medical receivables offset by an increase in accounts receivable from the medical segment.

Our operating loss and net loss were $11.5 million and $11.6 million, respectively, for the first six months of fiscal 2007 as compared to operating and net losses of $13.6 million and $13.7 million, respectively, for the first six months of fiscal 2006.

The overall trends reflected in the results of operations for the first six months of fiscal 2007 are a decrease in revenues from product sales, as compared to the first six months of fiscal 2006 ($4.5 million for the first six months of fiscal 2007 as compared to $8.4 million for the first six months of fiscal 2006), and a decrease in MRI equipment segment revenues relative to HMCA revenues ($9.5 million or 62% from the MRI equipment segment as compared to $5.9 million or 38% from HMCA, for the first six months of fiscal 2007, as compared to $13.6 million or 66% from the MRI equipment segment and $7.1 million or 34%, from HMCA, for the first six months of fiscal 2006). In addition, we experienced a decrease in unrelated party sales relative to related party sales in our medical equipment product sales ($4.5 million or 97% to unrelated parties and $142,000 or 3% to related parties for the first six months of fiscal 2007 as compared to $5.8 million, or 70% to unrelated parties and $2.5 million or 30% to related parties for the first six months of fiscal 2006).

We are committed to reversing the trends we have experienced in the first six months in fiscal 2007. Nevertheless, factors beyond our control, such as the timing and rate of market growth which depend on economic conditions, payor reimbursement rates and policies, and unexpected expenditures or the timing of such expenditures, make it impossible to forecast future operating results. We believe we are pursuing the correct policies which should prove successful in improving the Company's operating results.

The Company's UPRIGHT MRI(TM), and Fonar-360(TM) MRI scanners, together with the Company's works-in-progress, are intended to significantly improve the Company's competitive position.

The Company's UPRIGHT(TM) MRI scanner, which operates at 6000 gauss (.6 Tesla) field strength, allows patients to be scanned while standing or reclining. As a result, for the first time, MRI is able to be used to show abnormalities and injuries under full weight-bearing conditions, particularly the spine and joints. A floor-recessed elevator brings the patient to the height appropriate for the targeted image region. A custom- built adjustable bed will allow patients to sit or lie on their backs, sides or stomachs at any angle. Full-range-of-motion studies of the joints in virtually any direction will be possible, an especially promising feature for sports injuries.

The UPRIGHT(TM) MRI will also be useful for MRI directed neuro-surgical procedures as the surgeon would have unhindered access to the patient's head when the patient is supine with no restrictions in the vertical direction. This easy-entry, mid-field-strength scanner should be ideal for trauma centers where a quick MRI-screening within the first critical hour of treatment will greatly improve patients' chances for survival and optimize the extent of recovery.

The Fonar 360(TM) is an enlarged room sized magnet in which the floor, ceiling and walls of the scan room are part of the magnet frame. This is made possible by Fonar's patented Iron-Frame(TM) technology which allows the Company's engineers to control, contour and direct the magnet's lines of flux in the patient gap where wanted and almost none outside of the steel of the magnet where not wanted. Consequently, this scanner allows surgeons and other interventional physicians to walk inside the magnet and achieve 360 degree access to the patient to perform interventional procedures.

The Fonar 360(TM) is presently marketed as a diagnostic scanner and is sometimes referred to as the Open Sky(TM) MRI. In its Open Sky(TM) version, the Fonar 360(TM) serves as an open patient friendly scanner which allows 360 degree access to the patient on the scanner bed. To optimize the patient-friendly character of the Open Sky(TM) MRI, the walls, floor, ceiling and magnet poles are decorated with landscape murals. The patient gap is twenty inches and the magnetic field strength, like that of FONAR's UPRIGHT(TM) MRI, is 0.6 Tesla.

In the future, we expect the Fonar 360(TM) to function as an interventional MRI. The enlarged room sized magnet and 360 access to the patient afforded by the Fonar 360(TM) would permit surgeons to walk into the magnet and perform interventions on the patient inside the magnet. Most importantly the exceptional quality of the MRI image and its capacity to exhibit tissue detail on the image, can then be obtained real time during the procedure to guide the interventionalist. Thus surgical instruments, needles, catheters, endoscopes and the like could be introduced directly into the human body and guided to the malignant lesion by means of the MRI image. The number of inoperable lesions should be greatly reduced by the availability of this new capability. Most importantly treatment can be carried directly to the target tissue. The interventional features of the Fonar 360(TM) are expected to be implemented by Oxford Nuffield Orthopedic Center in Oxford U.K. in the near future. A full range of MRI compatible surgical instruments using ceramic cutting tools and beryllium-copper materials are available commercially.

The Company expects marked demand for its most commanding MRI products, the UPRIGHT(TM) MRI and the Fonar 360(TM), first for their exceptional features in patient diagnosis and treatment. These scanners additionally provide improved image quality and higher imaging speed because of their higher field strength of ..6 Tesla. The geometry of the UPRIGHT(TM) MRI as compared to a single coil, or multiple coils on only one axis and its transverse magnetic field enables the use of two detector rf coils operating in quadrature which increases the UPRIGHT(TM) MRI signal to noise ratio by 40%, providing a signal to noise ratio equal to a .84T recumbent only MRI scanner.

Liquidity and Capital Resources

Cash, cash equivalents and marketable securities decreased from $9.5 million at June 30, 2006 to $8.7 million at December 31, 2006. Principal uses of cash during the first six months of fiscal 2007 included capital expenditures for property and equipment of $164,000, repayment of long-term debt and capital lease obligations in the amount of $94,000, capitalized software development costs of $340,000 and capitalized patent and copyright costs of $235,000, and a decrease in accounts payable of $957,000.

Marketable securities approximated $3.7 million as at December 31, 2006, as compared to $4.9 million at June 30, 2006. This reduction represents the maturation of marketable securities which have not been reinvested and the proceeds of which are available to fund operations if needed. At December 31, 2006, our investments in U.S. Government obligations were $1.8 million, our investments in corporate and government agency bonds were $1.5 million and our investments in certificates of deposit and deposit notes were $400,000. The investments made have had the intended effect of maintaining a stable investment portfolio.

Cash used in operating activities for the first six months of fiscal 2007 approximated $235,000. Cash used in operating activities was attributable primarily to the net loss of $11.6 million and the decrease in accounts payable of $957,000, which were offset by a decrease in costs and estimated earnings in excess of billings on uncompleted contracts of $2.8 million, a decrease in inventories of $730,000 and the issuance of stock for compensation, costs and expenses in lieu of cash in the amount of $1.9 million.

Cash provided by investing activities for the first six months of fiscal 2007 approximated $606,000. The principal source of cash from investing activities during the first six months of fiscal 2007 consisted of the sale of marketable securities of $1.3 million, offset by expenditures for property and equipment of approximately $164,000 and capitalized software and patent costs of approximately $575,000.

Cash provided by financing activities for the first six months of fiscal 2007 approximated $36,000. The sources of cash from financing activities were net proceeds from exercises of stock options and warrants of $50,000, repayment of notes receivable from employee stockholders of $182,000, and net proceeds from the sale of stock of $373,000. The principal uses of cash in financing activities during the first six months of fiscal 2007 consisted of repayment of principal on long-term debt and capital lease obligations of approximately $94,000 and distributions to holders of minority interests of $475,000.

FONAR CORPORATION AND SUBSIDIARIES

The Company's obligations and the periods in which they are scheduled to become due are set forth in the following table:

(000's OMITTED)

Obligation	Total	Due in Less than 1 year	Due in 1-3 years	Due in 4-5 years	Due after 5 years
Long-term debt	$ 552	$ --	$ --	$ --	$ 552
Capital lease Obligation	760	243	384	133	--
Operating Leases	8,203	2,417	3,350	1,108	1,328
Total cash Obligations	$ 9,515	$ 2,660	$ 3,734	$ 1,241	$ 1,880

Total liabilities increased by 14.1% to $29.8 million at December 31, 2006 from $26.1 million at June 30, 2006.

We experienced a decrease in long-term debt from $1.2 million at June 30, 2006 to $1.1 million at December 31, 2006, an increase in unearned revenue on service contracts from $4.8 million to $5.9 million at June 30, 2006 to December 31, 2006, a decrease in billings in excess of costs and estimated earnings on uncompleted contracts from $3.1 million at June 30, 2006 to $1.8 million at December 31, 2006, a decrease in accounts payable from $4.9 million at June 30, 2006 to $3.9 million at December 31, 2006, an increase in customer advances from $5.5 million at June 30, 2006 to $10.1 at December 31, 2006.

As of December 31, 2006, the total of $6.4 million in other current liabilities included primarily accrued salaries and payroll taxes of $1.0 million, accrued royalties of $634,000 and excise and sales taxes of $2.4 million.

Our working capital approximated $6.1 million as of December 31, 2006, as compared to working capital of $14.2 million as of June 30, 2006, decreasing by 57.1%. This resulted principally from an increase in customer advances of $4.6 million ($5.5 million at June 30, 2006 as compared to $10.1 million at December 31, 2006), a decrease of cost and estimated earnings in excess of billings on uncompleted contracts of $2.8 million ($3.0 million at June 30, 2006 as compared to $127,000 at December 31, 2006) along with a decrease in inventories of $730,000 ($7.1 million at June 30, 2006 as compared to $6.3 million at December 31, 2006).

With respect to current liabilities, the current portion of long-term debt increased from $234,000 at June 30, 2006 to $243,000 at December 31, 2006, and billings in excess of costs and estimated earnings on uncompleted contracts decreased from $3.1 million at June 30, 2006 to $1.8 million at December 31, 2006. Customer advances increased from $5.5 million at June 30, 2006 to $10.1 million at December 31, 2006 and accounts payable decreased from $4.9 million at June 30, 2006 to $3.9 million at December 31, 2006.

In order to conserve our capital resources, we have issued common stock under our stock bonus and stock option plans to compensate employees and non-employees for services rendered, but to a materially lesser extent than in previous years. In the first six months of fiscal 2007, the compensatory element of stock issuances was $121,000 as compared to $1.1 million for the first six months of fiscal 2006. Utilization of equity in lieu of cash compensation improved our liquidity since it increased cash available for other expenditures. In addition, we used stock to pay $ 1.6 million for the termination of two employment agreements terminated in connection with the sale of HMCA's physical therapy and rehabilitation facility management business in the first three months of fiscal 2006.

Fonar's capital resources are expected to improve as Fonar's MRI scanner products gain wider market recognition and acceptance and produce increased product sales. The Company is focusing on increased advertising and marketing to increase demand for its products.

Inventories decreased by $730,000 ($7.1 million at June 30, 2006 as compared to $6.3 million at December 31, 2006) resulting from a decrease in the purchasing of raw materials and components and in filling our backlog of orders.

Fonar has not committed to making additional capital expenditures in the 2007 fiscal year other than its intention to continue research and development expenditures at current levels.

Our business plan calls for a continuing emphasis on providing our customers with enhanced equipment service and maintenance capabilities and delivering state-of-the-art, innovative and high quality equipment upgrades at competitive prices.

Our principal source of liquidity has been cash flows provided by operations. We currently expect this to continue. At December 31, 2006, we had working capital of $6.1 million. For the six months ended December 31, 2006, we incurred a net loss of $11.6 million which included non-cash charges of $3.4 million.

In order to conserve our capital resources we have and will continue to issue, from time to time, common stock and stock options to compensate employees and non-employees for services rendered. The Company is focusing on increased advertising and marketing campaigns and distribution programs to increase the demand for Fonar's products. Management anticipates that Fonar's capital resources will improve as Fonar's MRI scanner products gain wider market recognition and acceptance resulting in increased product sales. If we are not successful with our current marketing efforts to increase sales, then we could experience a shortfall in the cash necessary to sustain operations at their current levels.

Given our December 31, 2006 cash and marketable securities balance of $8.7 million and our forecasted cash requirements, we anticipate that our existing capital resources, funds generated from operations and funds expected to be received from note repayments, will be sufficient to satisfy our cash flow requirements through at least December 31, 2007. Based upon current results of operations, we believe we will either need to increase sales, reduce expenses or seek other sources of funds through the issuance of equity or debt financing in order to maintain sufficient funds available to operate subsequent to December 31, 2007.

The Company received written notification from The Nasdaq Stock Market on December 22, 2005 that the bid price of its common stock for the prior 30 consecutive trading days had closed below the minimum $1.00 per share required for continued listing under Nasdaq Marketplace Rule 4310(c)(4) (the "Rule"). Pursuant to Nasdaq Marketplace Rule 4310(c)(8)(D), the Company had been provided an initial period of 180 calendar days, or until June 20, 2006, to regain compliance but since Fonar was then in compliance with NASDAQ's other listing requirements, an extension to December 18, 2006 was granted.

On December 19, 2006 the Company received a Nasdaq Staff Determination indicating that the Company still fails to comply with the minimum bid price requirement for continued listing set forth in the Rule and that its securities are therefore, subject to delisting from the Nasdaq Capital Market. The Company has requested a hearing before a Nasdaq Listing Qualifications Panel to review the Staff Determination which has been scheduled for February 15, 2007. There can be no assurance the Panel will grant the Company's request.

FONAR CORPORATION AND SUBSIDIARIES

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Our investments are in fixed rate instruments. Below is a tabular presentation of the maturity profile of the fixed rate instruments held by us at December 31, 2006.

INTEREST RATE SENSITIVITY
PRINCIPAL AMOUNT BY EXPECTED MATURITY
WEIGHTED AVERAGE INTEREST RATE

Year of Maturity	Investments in Fixed Rate Instruments	Weighted Average Interest Rate

12/31/07	$ 0	0.00%
12/31/08	1,150,000	3.63%
12/31/09	1,998,062	3.61%
12/31/10	600,000	2.37%
Total:	$ 3,748,062	
Fair Value at 12/31/06	$ 3,615,602	

All of our revenue, expense and capital purchasing activities are transacted in United States dollars.

See Note 13 to the consolidated Financial Statements in our Form 10-K as of and for the year ended June 30, 2006 for information on long-term debt.

Item 4. Controls and Procedures

(a) Evaluation of disclosure controls and procedures.

The Company maintains controls and procedures designed to ensure that information required to be disclosed in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission. Based upon their evaluation of those controls and procedures performed as of the end of the period covered by this report, the principal executive and acting principal financial officer of the Company concluded that disclosure controls and procedures were effective.

(b) Change in internal controls.

The Company continues to enhance its controls and procedures related to the financial reporting process, improvements that were established during the latter part of fiscal 2005. This included hiring an outside consultant to assist with technical accounting and reporting issues, developing more standardized closing procedures and implementing a more formal process for documenting the weekly management meetings to review operating performance and results.

There have been no changes in our internal control over financial reporting that occurred during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

FONAR CORPORATION AND SUBSIDIARIES

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings: There were no material changes in litigation for the first six months of fiscal 2007.

Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds: None

Item 3 - Defaults Upon Senior Securities: None

Item 4 - Submission of Matters to a Vote of Security Holders: None

Item 5 - Other Information: None

Item 6 - Exhibits and Reports on Form 8-K: Exhibit 31.1 Certification See Exhibits Exhibit 32.1 Certification See Exhibits 8-K (earnings press release) filed on September 15, 2006 8-K (earnings press release) filed on November 13, 2006 8-K (Nasdaq Staff Determination) filed on December 21, 2006

FONAR CORPORATION AND SUBSIDIARIES

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 thereunto duly authorized.

FONAR CORPORATION
(Registrant)

By: /s/ Raymond V. Damadian
Raymond V. Damadian
President & Chairman

Dated:February 9, 2007