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DYNABAZAAR INC
Form 10-Q
May 15, 2007

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

FORM 10-Q

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

For the Quarterly Period Ended March 31, 2007

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 000-29423

DYNABAZAAR, INC.

(Exact name of registrant as specified in its charter)

Delaware

04-3351937

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

888 Seventh Ave., 17th Floor, New York, NY 10019
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code:
(212) 974-5730

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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer Accelerated Filer Non-accelerated Filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares outstanding of the registrant's common stock as of May 11, 2007 was 23,691,756

DYNABAZAAR, INC.

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INDEX

PART I. FINANCIAL INFORMATION

| | |
|--|----|
| ITEM 1. FINANCIAL STATEMENTS | 1 |
| Condensed Consolidated Balance Sheets as of March 31, 2007 (unaudited) and December 31, 2006 | 1 |
| Condensed Consolidated Statements of Operations for the three months ended March 31, 2007 (unaudited) and 2006 (unaudited) | 2 |
| Condensed Consolidated Statements of Cash Flows for the three months ended March 31, 2007 (unaudited) and 2006 (unaudited) | 3 |
| Notes to Condensed Consolidated Financial Statements (unaudited) | 4 |
| ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS | 13 |
| ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK | 18 |
| ITEM 4. CONTROLS AND PROCEDURES | 19 |

PART II. OTHER INFORMATION

| | |
|---------------------------|----|
| ITEM 1. LEGAL PROCEEDINGS | 19 |
| ITEM 6. EXHIBITS | 21 |

| | |
|------------|----|
| SIGNATURES | 21 |
|------------|----|

ITEM 1. FINANCIAL STATEMENTS

DYNABAZAAR, INC. AND SUBSIDIARIES CONDENSED CONSOLIDATED BALANCE SHEETS (in thousands)

| | March 31, 2007 (unaudited) | December 31, 2006 (audited) |
|---|----------------------------------|-----------------------------------|
| | ----- | ----- |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 2,770 | \$ 2,938 |
| Accounts receivable, net of allowance for doubtful accounts of \$9 and \$10 in 2007 and 2006 respectively | 2,535 | 2,053 |
| Inventory, net | 3,765 | 3,738 |
| Prepaid expenses | 483 | 496 |
| | ----- | ----- |
| Total current assets | 9,553 | 9,225 |
| Fixed assets | 134 | 92 |
| Trade Name | 1,587 | 1,587 |
| Other intangibles, net | 2,867 | 2,903 |
| Deposits | 4 | 4 |
| Long-term prepaid expenses | 600 | 694 |
| | ----- | ----- |
| Total assets | \$ 14,745 | \$ 14,535 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |

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| | | |
|---|-----------|-----------|
| Current liabilities: | | |
| Accounts payable | \$ 1,490 | \$ 1,436 |
| Accrued expenses and other current liabilities | 148 | 185 |
| Line of credit | 953 | 729 |
| | ----- | ----- |
| Total current liabilities | 2,591 | 2,350 |
| Long term liability | 2,225 | 2,225 |
| Commitments and Contingency | | |
| Stockholders' equity: | | |
| Common stock, \$0.001 par value; 90,000,000 shares authorized; 29,726,385 shares issued at March 31, 2007 and December 31, 2006, respectively | | |
| | 30 | 30 |
| Additional paid-in capital | 151,757 | 151,757 |
| Accumulated other comprehensive income, net | 260 | 260 |
| Accumulated deficit | (137,648) | (137,617) |
| | ----- | ----- |
| | 14,399 | 14,430 |
| Less: Common stock held in treasury, at cost; 6,034,629 at March 31, 2007 and December 31, 2006 | (4,470) | (4,470) |
| | ----- | ----- |
| Total stockholders' equity | 9,929 | 9,960 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$ 14,745 | \$ 14,535 |
| | ===== | ===== |

See accompanying notes to condensed consolidated financial statements.

1

DYNABAZAAR, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in thousands, unaudited)

| | Three Months Ended March 31, | |
|--|---------------------------------|----------|
| | 2007 | 2006 |
| | ----- | ----- |
| Revenues | \$ 4,208 | \$ -- |
| Cost of goods sold | 3,328 | -- |
| | ----- | ----- |
| Gross profit | 880 | -- |
| Operating expenses, general and administrative | 934 | 215 |
| | ----- | ----- |
| Income (loss) from operations | (54) | (215) |
| | ----- | ----- |
| Interest income | 35 | 103 |
| Interest expense | (12) | |
| | ----- | ----- |
| | 23 | 103 |
| | ----- | ----- |
| Net income (loss) | \$ (31) | \$ (112) |
| | ===== | ===== |

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| | | |
|--|-----------|-----------|
| Net income (loss) per share: | | |
| Basic | \$ (0.00) | \$ (0.00) |
| | ===== | ===== |
| Diluted | \$ (0.00) | \$ (0.00) |
| | ===== | ===== |
| Weighted average number of common shares outstanding: | | |
| Basic | 23,692 | 23,410 |
| | ===== | ===== |
| Diluted | 23,692 | 23,410 |
| | ===== | ===== |

See accompanying notes to condensed consolidated financial statements.

2

DYNABAZAAR, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands; unaudited)

| | Three Months Ended March 31, | |
|--|---------------------------------|----------|
| | 2007 | 2006 |
| | ----- | ----- |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net Loss | \$ (31) | \$ (112) |
| Adjustments to reconcile net income (loss) to net cash used in operating activities | | |
| Depreciation and amortization | 76 | -- |
| Provision for doubtful accounts | (1) | |
| Issuance of stock options | -- | 19 |
| Change in cash attributable to changes in operating assets and liabilities | | |
| Accounts receivable | (481) | -- |
| Inventories | (27) | -- |
| Prepaid expense | 13 | (38) |
| Long term prepaid expenses | 94 | 83 |
| Accounts payable | 54 | -- |
| Accrued expense and other current liabilities | (37) | (72) |
| | ----- | ----- |
| Net cash used in operating activities | (340) | (120) |
| | ----- | ----- |
| NET CASH FLOWS USED IN INVESTING ACTIVITIES, PURCHASE OF FIXED ASSETS | (52) | -- |
| | ----- | ----- |
| NET CASH PROVIDED BY FINANCING ACTIVITIES, Proceeds from (payments for) line of credit, net | 224 | -- |
| | ----- | ----- |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (168) | (120) |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 2,938 | 9,125 |
| | ----- | ----- |
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 2,770 | \$ 9,005 |
| | ===== | ===== |
| SUPPLEMENTAL DISCLOSURE CASH FLOW INFORMATION: | | |
| Cash paid for interest | \$ 12 | \$ |
| | ===== | ===== |

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| | | | | |
|--------------|-------|----|-------|----|
| Income taxes | \$ | -- | \$ | -- |
| | ===== | | ===== | |

3

DYNABAZAAR, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1 - THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

THE COMPANY

OVERVIEW

Dynabazaar, Inc. (the "Company") was incorporated in the State of Delaware in February 1997 as "Fairmarket, Inc." Through September 3, 2003, the Company was an online auction and promotions technology service provider that enabled marketers to create results-oriented rewards programs and helped commerce companies automate the process of selling their excess inventory online to wholesale and retail buyers. On September 4, 2003, the Company sold substantially all of its operating assets to eBay, Inc. ("eBay") for consideration of \$4.5 million in cash under the terms and conditions of an asset purchase agreement the Company entered into with eBay on June 20, 2003. Following the closing of the asset sale, the Company changed its name from "Fairmarket, Inc." to "Dynabazaar, Inc."

In connection with the cessation of the Company's online auction business, the Company relocated its principal executive offices as of January 1, 2004 to 888 Seventh Avenue, 17th Floor, New York, New York 10019, an office maintained by Barington Capital Group, L.P. ("Barington"), a limited partnership whose general partner is a corporation of which James Mitarotonda is Chairman, President and Chief Executive Officer. Mr. Mitarotonda was previously the Company's President and Chief Executive Officer. He submitted his resignation, effective as of the close of business on April 20, 2007. He continues to serve as a director of the Company.

From January 2003 until June 20, 2006, the Company did not operate any business and was settling its remaining claims and liabilities while reviewing alternatives for the use or disposition of our remaining assets.

The Company's common stock trades on the NASDAQ OTC Bulletin Board under the symbol "FAIM.OB". The Company's common stock was quoted on the NASDAQ National Market, but was delisted on June 24, 2004.

On March 30, 2007, the Company entered into an amendment to the administrative services agreement with Barington, effective as of January 1, 2007. Under the amended agreement, which runs through December 31, 2007, Barington is to continue to be paid a fee of \$7,500 per month for performing certain administrative, accounting and other services on behalf of the Company until the closing of the transactions contemplated by the Amended and Restated Merger Agreement at which point the fee is to increase to a rate of \$10,000 per month.

4

NOTE 1 - THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONT:

As previously disclosed in a Form 8-K filed by the Company on April 23, 2007,

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James A. Mitarotonda delivered to the secretary of Dynabazaar, Inc. (the "Company") notice of his resignation as President and Chief Executive Officer of the Company, effective as of the close of business on April 20, 2007. Mr. Mitarotonda, who will continue to serve as a director of the Company, had no disagreements with the Company on any matters related to the Company's operations, policies or practices. The Board of Directors of the Company thanks Mr. Mitarotonda for his dedicated service and valued contributions to the Company.

On April 20, 2007, the Board of Directors of the Company appointed Sebastian E. Cassetta to serve as the Company's President and Chief Executive Officer, effective as of the close of business on April 20, 2007.

On January 5, 2007, the Company entered into an agreement and plan of merger (the "Merger Agreement") with L Q Corporation, Inc., a Delaware Corporation, and LQ Merger Corp., a Delaware corporation and wholly-owned subsidiary of the Company ("LMC"), which Merger Agreement was amended and restated on February 26, 2007 (the "Amended and Restated Merger Agreement"). The Amended and Restated Merger Agreement provides that, upon the terms and subject to the conditions set forth in such agreement, LMC will merge with and into L Q Corporation, Inc. with L Q Corporation, Inc. continuing as the surviving corporation and a wholly-owned subsidiary of the Company.

Under the terms of the Amended and Restated Merger Agreement, L Q Corporation stockholders will receive 3.68 shares of Dynabazaar common stock for each share of L Q Corporation common stock they hold. Upon completion of the merger, L Q Corporation stockholders will hold approximately 34% of the combined company and our stockholders will hold approximately 66% of the combined company on a fully-diluted basis. It is anticipated that the combined company's shares will continue to trade on the Over-The-Counter Bulletin Board.

Both the Company's and L Q Corporation's Board of Directors approved the Amended and Restated Merger Agreement in accordance with the recommendation of the special committees of independent directors formed by the Board of Directors of each company to evaluate the transaction.

The transaction is subject to stockholder approval and other customary conditions and is expected to be completed during the second half of 2007. A special meeting of stockholders of the Company will be announced in the near future to obtain stockholder approval of the transaction.

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION (\$ IN THOUSANDS)

The accompanying condensed consolidated financial statements of the Company for the three months ended March 31, 2007 and 2006 are unaudited and have been prepared on a basis substantially consistent with our audited consolidated financial statements for the year ended December 31, 2006. The condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information. Consequently, these statements do not include all disclosures normally required by generally accepted accounting principles for annual financial statements. These condensed consolidated interim financial statements should be read in conjunction with our audited consolidated financial statements for the year ended December 31, 2006, which are contained in our Annual Report on Form 10-K filed with the Securities and Exchange Commission (the "SEC") on April 4, 2007 and the amended 10-K filed on April 17, 2007. The condensed consolidated interim financial statements, in the opinion of management, reflect all adjustments (including all normal recurring accruals) necessary to present fairly the Company's financial position, results of operations and cash flows for the interim periods ended March 31, 2007 and 2006. The results of operations for the

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interim periods are not necessarily indicative of the results of operations to be expected for the fiscal year.

5

I NOTE 1 - THE COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES CONT:

CASH AND CASH EQUIVALENTS (\$ IN THOUSANDS)

The Company considers all highly-liquid debt instruments with original maturities of three months or less to be cash equivalents, including highly rated money market funds with daily liquidity. At March 31, 2007, and throughout the three month period, balances of cash at financial institutions exceeded the federally insured limit. The Company has not experienced any losses in such accounts and believes it is not subject to any significant credit risk on cash and cash equivalents. The following schedule summarizes the estimated fair value of the Company's cash and cash equivalents:

| | March 31, 2007 (unaudited) | December 31, 2006 |
|----------------------------|-------------------------------|----------------------|
| | ----- | ----- |
| Cash and cash equivalents: | | |
| Cash | \$ 26 | \$ 72 |
| Money market funds | 2,744 | 2,866 |
| | ----- | ----- |
| | \$ 2,770 | \$ 2,938 |
| | ===== | ===== |

CONCENTRATION OF CREDIT RISK (\$ IN THOUSANDS)

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of cash and cash equivalents, short term investments and accounts receivable. Substantially all of the Company's cash and cash equivalents are invested in a highly liquid money market fund.

FAIR VALUE OF FINANCIAL INSTRUMENTS (\$ IN THOUSANDS)

The Company's financial instruments, including cash and cash equivalents, accounts receivable and accrued expenses payable are carried at cost. The Company's financial instruments approximate fair value due to their relatively short maturities. The Company does not hold or issue financial instruments for trading purposes.

PRINCIPLES OF CONSOLIDATION

The condensed consolidated financial statements include the accounts of our direct and indirect wholly-owned subsidiaries Costar and VSTC. Significant intercompany transactions and balances have been eliminated.

INCOME TAXES

Effective January 1, 2007, the Company adopted the provisions of the Financial Accounting Standards Board ("FASB") Interpretation No. 48, "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109" ("FIN 48"). There were no unrecognized tax benefits as of January 1, 2007 and as of March 31, 2007. FIN 48 prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more-likely-than-not to be sustained upon

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examination by taxing authorities. The Company recognizes accrued interest and penalties related to unrecognized tax benefits as income tax expense. No amounts were accrued for the payment of interest and penalties at January 1, 2007. There was no change to this balance at March 31, 2007. Management is currently unaware of any issues under review that could result in significant payments, accruals or material deviations from its position. The adoption of the provisions of FIN 48 did not have a material impact on the Company's financial position, results of operations and cash flows.

STOCK-BASED COMPENSATION

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards ("SFAS") No.123(R) Accounting for Stock-Based Compensation. Among other items, SFAS No. 123(R) requires companies to record compensation expense for share-based awards issued to employees and directors in exchange for services provided. The amount of the compensation expense is based on the estimated fair value of the awards on their grant dates and is recognized over the applicable vesting period.

6

The fair value of stock options is determined using an option-pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock and the expected dividends on it, and the risk free interest rate over the expected life of the option.

The Company adopted SFAS No.123(R) using the modified prospective transition method, which requires the application of the accounting standard to all share-based awards issued on or after January 1, 2006, and any outstanding share-based awards that were issued but not vested as of January 1, 2006.

In the three months ended March 31, 2007 and 2006, the Company recognized stock-based compensation expense of \$0 and \$19, respectively, in its condensed consolidated financial statements. This amount includes compensation expense for fully vested stock options granted subsequent to January 1, 2006 based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R).

7

DYNABAZAAR, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 2 - ACQUISITION:

On June 20, 2006, Costar Video Systems, LLC ("Costar") and Video Solutions Technology Center, LLC ("VSTC"), the Company's direct and indirect wholly owned subsidiaries, completed the acquisition (the "Acquisition") of substantially all of the assets of Southern Imaging, Inc., a Texas corporation ("Southern Imaging"), and Video Solutions Technology Center, Inc., a Nevada corporation ("Video Solutions"), pursuant to the transactions contemplated by the asset purchase agreement, dated as of June 20, 2006, by and between Southern Imaging, Video Solutions, the shareholders of Southern Imaging, Costar and VSTC. However, the acquisition is being accounted for as if it was effectively completed on June 30, 2006. Results of operations of Southern Imaging and Video Solutions are included in the consolidated financial statements since June 30, 2006.

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Costar, the Company's wholly-owned subsidiary which acquired Southern Imaging's assets, designs, sources and distributes video and imaging products for the security and industrial markets. VSTC, a wholly owned subsidiary of Costar which acquired the assets of Video Solutions, provides product design and development, technical support and repair services for Costar. Estimated consideration for the Acquisition is up to approximately \$9.6 million, consisting of the issuance at closing of 200,000 shares of our common stock, a cash payment of approximately \$3.8 million (including a finders fee payment of approximately \$154,000, payment of \$108,000 to Barington and the payoff of shareholder loans of approximately \$612,000) less the value of the 200,000 shares of Dynabazaar common stock, the assumption of certain liabilities of approximately \$3.5 million, and deferred consideration of up to \$4 million in cash, contingent upon Costar and VSTC achieving certain levels of sales and EBITDA after the closing, through 2009 of which \$2,225 is recorded as a long-term liability. On September 29, 2006, the 200,000 shares of Dynabazaar common stock were issued.

The Company has incorporated contingent consideration into the structure of the acquisition in June 2006. This arrangement generally results in the payment of additional consideration to the sellers upon the satisfaction of certain events.

The additional cash payments or share issuances are contingent consideration accounted for under the Emerging Issues Task Force ("EITF") No. 95-8. "Accounting for Contingent Consideration Paid to the Shareholders of an Acquired Enterprise in a Purchase Business Combination", and is considered to be additional purchase consideration and will be accounted for as part of the purchase price of the firms when the outcome of the contingency is determinable beyond a reasonable doubt. The sum of the amounts assigned to assets acquired and liabilities assumed (e.g. fair values) exceeded the cost of the acquired entity by \$2,225 therefore contingent consideration was recorded for that amount. Contingent consideration in these circumstances may be recorded pursuant to paragraph 46 of Statement of Financial Accounting Standards ("SFAS") No. 141 "Business Combinations."

There were no material relationships between the Company or its affiliates and any of the parties to the Asset Purchase Agreement, other than in respect of such agreement.

8

DYNABAZAAR, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 2 - ACQUISITION CONT:

Allocation of Purchase Price

Allocated to:

| | |
|-----------------------------|----------|
| Trade name | \$ 1,587 |
| Other intangibles | 3,066 |
| Cash | 240 |
| Prepays | 105 |
| Deposits | 4 |
| Accounts receivables, net | 1,875 |
| Inventory | 2,623 |
| Property and equipment, net | 95 |
| | ----- |
| Total | 9,595 |

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| | |
|----------------------------|----------|
| Liabilities Assumed: | |
| Accounts payable and other | (1,634) |
| Revolver facilities | (1,863) |
| Issuance of common stock | (74) |
| Long term liability | (2,225) |
| | ----- |
| Net purchase price | \$ 3,800 |
| | ===== |

Intangible assets arose from the Costar acquisition. The aggregate of the estimated purchase price plus acquisition costs of an estimated \$9.6 million exceeded the fair market value for all identifiable net assets. An independent appraisal was conducted of all intangible assets (including, but not limited to, distribution agreements, customer lists, patents, trademarks and trade names, etc.) received as a result of the acquisition of Costar.

Pro Forma Income Statement

The following unaudited pro forma information presents results of operations of the Company as if the acquisition of Costar occurred as of January 1, 2006: (\$ in thousands)

| | Quarter Ended March 31, 2006 ----- |
|---|--|
| Net Sales | \$ 4,219 |
| Cost of goods sold | (3,340) |
| | ----- |
| Gross profit | 879 |
| General and administrative expenses | 883 |
| | ----- |
| Net loss from operations | (4) |
| Interest income | 103 |
| Pro forma adjustment in interest income | (33) (a) |
| Pro forma adjustment amortization of intangible assets acquired | (67) (b) |
| | ----- |
| Net loss | \$ (1) |
| | ===== |
| Net income (loss) per share - as reported | \$ (0.00) |
| Net income (loss) per share - pro forma | \$ (0.00) |
| Weighted-average shares | 23,410 |

9

NOTE 2 - ACQUISITION CONT:

(a) Interest income has been reduced based on cash balances that would have existed had the acquisition occurred at the beginning of the period.

(b) Amortization represents annual charges to amortization expense for the intangible assets acquired which are the subject to amortization.

Although prepared on a basis consistent with the Company's consolidated financial statements, these unaudited pro forma results do not purport to be indicative of the actual results of operations of the combined companies which would have been achieved had these events occurred at the beginning of the periods presented nor are they indicative of future results.

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NOTE 3 - INTANGIBLE ASSETS, NET: (\$ in thousands)

The intangible assets acquired as a result of the Southern Imaging and Video Solutions acquisition have been adjusted in the prior year as a result of the completion of an independent appraisal, adjustments to the estimated fair values of the assets acquired, and post closing adjustments to the purchase price. The components of intangible assets acquired as a result of the acquisition are as follows:

| | March 31, 2007 (unaudited) | |
|-------------------------------|----------------------------------|------------------------|
| | Gross Carrying Amount | Accumulat Amortizat |
| Amortized intangible asset: | | |
| Other intangibles, net | \$3,066 | \$ 199 ===== |
| Unamortized intangible assets | | |
| Trade Name | 1,587 | |
| Total | \$4,653 ===== | |

Amortization expense for the three months ended March 31, 2007 was \$66. Estimated amortization expense applicable to amortizable intangible assets for each of the next 5 years is \$266. The estimated useful life for Existing Customer Relationships is 6 years.

NOTE 4 - NET INCOME (LOSS) PER SHARE:

The number of shares used to compute basic loss per share and diluted loss per share relates to additional shares to be issued upon the assumed exercise of stock options and warrants, net of shares hypothetically repurchased at the average market price with the proceeds of exercise. For the three months ended March 31, 2007 and 2006, basic and diluted net loss per common share is computed based on the weighted average number of common shares outstanding during the period because the effect of potential common equivalent shares would be anti-dilutive.

10

DYNABAZAAR, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 5 - LEGAL PROCEEDINGS:

We are a defendant in certain purported class action lawsuits filed by individual shareholders in the U.S. District Court for the Southern District of New York against certain of our former officers and directors, and various of the underwriters in our initial public offering ("IPO") and secondary offering. The lawsuits have been filed by individual shareholders who purport to seek class action status on behalf of all other similarly situated persons who

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purchased our common stock between July 8, 1999 and December 6, 2000. A consolidated amended class action complaint was filed on April 19, 2002. The complaint alleges that certain underwriters of the IPO solicited and received excessive and undisclosed fees and commissions in connection with that offering. The complaint further alleges that the defendants violated the federal securities laws by issuing a registration statement and prospectus in connection with our IPO which failed to accurately disclose the amount and nature of the commissions and fees paid to the underwriter defendants. On or about October 8, 2002, the Court entered an Order dismissing the claims asserted against certain individual defendants in the consolidated actions without any payment from these individuals or us. On or about February 19, 2003, the Court entered an Order dismissing with prejudice the claims asserted against us under Section 10(b) of the Exchange Act. As a result, the only claims that remain against us are those arising under Section 11 of the Securities Act. The parties have negotiated and executed a definitive settlement agreement. The proposed settlement provides that the class members in the class action cases brought against the participating issuer defendants will be guaranteed a recovery of \$1 billion by insurers of the participating issuer defendants. If recoveries totaling \$1 billion or more are obtained by the class members from the underwriter defendants, however, the monetary obligations to the class members under the proposed settlement will be satisfied. In addition, we and any other participating issuer defendants will be required to assign to the class members certain claims that they may have against the underwriters of their IPO's. The proposed settlement contemplates that any amounts necessary to fund the settlement or settlement-related expenses would come from participating issuers' directors and officers' liability insurance policy proceeds as opposed to funds of the participating issuer defendants themselves. A participating issuer defendant could be required to contribute to the costs of the settlement if that issuer's insurance coverage were insufficient to pay that issuer's allocable share of the settlement costs. If ultimately approved by the Court, the proposed settlement would result in the dismissal, with prejudice, of all claims in the litigation against us and all of the other issuer defendants who have elected to participate in the proposed settlement, together with the current or former officers and directors of participating issuers who were named as individual defendants. The proposed settlement does not provide for the resolution of any claims against the underwriter defendants, and the litigation as against those defendants is continuing. Consummation of the proposed settlement remains conditioned upon obtaining approval by the Court. By order entered on September 1, 2005, the Court granted preliminarily approval of the proposed settlement and directed that notice of the terms of the proposed settlement be provided to class members. Thereafter, the court held a fairness hearing, on April 24, 2006, at which objections to the proposed settlement were heard. The Court has yet to issue a ruling on the motion for final approval. On December 5, 2006, the Court of Appeals for the Second Circuit reversed the Court's order certifying a class in six test cases that were selected by the underwriter defendants and plaintiffs in the coordinated proceeding. On April 6, 2007, the Court of Appeals denied the plaintiffs' petition for rehearing of the Court's December 5, 2006 ruling but noted that the plaintiffs remain free to ask the District Court to certify a different class which might meet the standards for class certification that the Court of Appeals articulated in its December 5, 2006 decision. Because our proposed settlement with the plaintiffs involves the certification of the case against us as a class action for settlement purposes, it is unclear what impact, if any, the Second Circuit's class certification ruling will have on our case or the viability of the proposed settlement. In the event the settlement is not finalized, the Company believes that it has meritorious defenses to plaintiffs' claims and intends to defend the action vigorously.

The expense of defending this litigation may be significant. The amount of time to resolve these lawsuits is unpredictable and defending us may divert management's attention from the day-to-day operations of our business, which could adversely affect our business, results of operations and cash flows. In addition, an unfavorable outcome in such litigation could have a material

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adverse effect on our business, results of operations and cash flows.

11

DYNABAZAAR, INC. AND SUBSIDIARIES NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 6 - MAJOR CUSTOMERS AND SUPPLIERS:

For the quarter ended March 31, 2007, the Company had two customers that contributed 14.8% and 13.3% of sales revenue, for a total of \$623 and \$560 respectively. As of March 31, 2007, these same two customers owed 14.7% and 12.5% of the outstanding accounts receivable balance.

At March 31, 2007, the Company had two major suppliers that were owed approximately 51.7% of the total accounts payable, for a total of \$1,062 and \$673, respectively.

NOTE 7 - CREDIT LINE (\$ in thousands)

The Company maintains a line of credit with the Bank of Texas. The line has a limit of \$2.5 million and interest is charged on the outstanding balance at a variable rate, which was 8.25% at March 31, 2007. The line is secured by the Company's accounts receivable and inventories and the agreement requires the maintenance of financial ratios and monthly payments of accrued interest calculated on the outstanding balance. As of March 31, 2007 and December 31, 2006, \$953 and \$729 were outstanding under the line of credit.

12

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

THE COMPANY

OVERVIEW AND RECENT EVENTS

Dynabazaar, Inc. (the "Company", "Dynabazaar" or "we") was incorporated in the State of Delaware in February 1997 as "Fairmarket, Inc." Through September 3, 2003, we were an online auction and promotions technology service provider that enabled marketers to create results-oriented rewards programs and helped commerce companies automate the process of selling their excess inventory online to wholesale and retail buyers. On September 4, 2003, we sold substantially all of our operating assets to eBay, Inc. ("eBay") for consideration of \$4.5 million in cash under the terms and conditions of an asset purchase agreement we entered into with eBay on June 20, 2003. Following the closing of the asset sale, we changed our name from "Fairmarket, Inc." to "Dynabazaar, Inc."

In connection with the cessation of our online auction business, we relocated our principal executive offices as of January 1, 2004 to 888 Seventh Avenue, 17th Floor, New York, New York 10019, an office maintained by Barington Capital Group, L.P., a limited partnership whose general partner is a corporation of which James Mitarotonda is Chairman, President and Chief Executive Officer. Mr. Mitarotonda was previously the Company's President and Chief Executive Officer. He submitted his resignation, effective as of the close of business on April 20, 2007. He continues to serve as a director of the Company.

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From January 2003 until June 20, 2006, the Company did not operate any business and was settling its remaining claims and liabilities while reviewing alternatives for the use or disposition of our remaining assets.

The Company's common stock trades on the NASDAQ OTC Bulletin Board under the symbol "FAIM.OB". The Company's common stock was quoted on the NASDAQ National Market, but was delisted on June 24, 2004.

As previously disclosed in a Form 8-K filed by the Company on April 23, 2007, James A. Mitarotonda delivered to the secretary of Dynabazaar, Inc. (the "Company") notice of his resignation as President and Chief Executive Officer of the Company, effective as of the close of business on April 20, 2007. Mr. Mitarotonda, who will continue to serve as a director of the Company, had no disagreements with the Company on any matters related to the Company's operations, policies or practices. The Board of Directors of the Company thanks Mr. Mitarotonda for his dedicated service and valued contributions to the Company.

On April 20, 2007, the Board of Directors of the Company appointed Sebastian E. Cassetta to serve as the Company's President and Chief Executive Officer, effective as of the close of business on April 20, 2007.

Mr. Cassetta, 57, has served as the Chief Executive Officer of Costar Video Systems, LLC, a wholly-owned subsidiary of the Company, since June 2006. He has also served as a director, President and Chief Executive Officer of L Q Corporation, Inc. (OTCBB:LQCI) since May 2006. Mr. Cassetta was the Chairman and Chief Executive Officer of SmartServ Online, Inc., a company specializing in the delivery of content to desktop and wireless devices, from August 1992 to July 2003. Prior to that, he was the President of Burns and Roe Securacom Inc., a company specializing in engineering and large-scale systems integration, and a director and vice president of Brinks Inc., an international security company. He is a former Special Assistant to New York Governor and Vice President Nelson A. Rockefeller. Mr. Cassetta currently also serves as a Senior Managing Director and the Chief Operating Officer of Barington Capital Group, L.P. ("Barington"), a position he has held since August 2003.

On January 5, 2007, the Company entered into an agreement and plan of merger (the "Merger Agreement") with L Q Corporation, Inc., a Delaware Corporation, and LQ Merger Corp., a Delaware corporation and wholly-owned subsidiary of the Company ("LMC"), which Merger Agreement was amended and restated on February 26, 2007 (the "Amended and Restated Merger Agreement"). The Amended and Restated Merger Agreement provides that, upon the terms and subject to the conditions set forth in such agreement, LMC will merge with and into L Q Corporation, Inc. with L Q Corporation, Inc. continuing as the surviving corporation and a wholly-owned subsidiary of the Company, as further disclosed in Part I, Item 1 of the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 4, 2007, which disclosure is incorporated herein by reference.

Barington and certain of its affiliates which have joined with Barington in the filing of a statement on Schedule 13D, collectively own greater than 10% of the outstanding common stock of both the Company and L Q Corporation, Inc. The

Company is party to a services agreement under which Barington performs certain administrative, accounting and other services on the Company's behalf as further disclosed in Part III, Item 13 of Amendment No. 1 to the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission on April 17, 2007, which disclosure is incorporated herein by reference.

BUSINESS

Costar designs, sources and distributes video and imaging products for the security and industrial markets. The product line for the security market consists primarily of closed circuit television ("CCTV") cameras, while the product line for the industrial market is comprised of cameras and lenses utilized by biomedical and manufacturing companies.

The production of all units distributed by Costar is outsourced to contract manufacturers, and the majority of revenues are derived from sales of products under the Costar(TM) brand. The balance of Costar's business is generated from (a) a private label business and (b) the distribution of other companies' branded products.

Video Solutions provides product design and development, technical support and repair services for Costar.

BUSINESS ACQUISITION (\$ IN THOUSANDS)

On June 20, 2006, Costar Video Systems, LLC ("Costar") and Video Solutions Technology Center, LLC ("VSTC"), the Company's direct and indirect wholly owned subsidiaries, completed the acquisition (the "Acquisition") of substantially all of the assets of Southern Imaging, Inc., a Texas corporation ("Southern Imaging"), and Video Solutions Technology Center, Inc., a Nevada corporation ("Video Solutions"), pursuant to the transactions contemplated by the asset purchase agreement, dated as of June 20, 2006, by and between Southern Imaging, Video Solutions, the shareholders of Southern Imaging, Costar and VSTC. However, the acquisition is being accounted for as if it was effectively completed on June 30, 2006. Results of operations of Southern Imaging and Video Solutions are included in the consolidated financial statements since June 30, 2006.

Estimated consideration for the Acquisition is up to approximately \$9.6 million, consisting of the issuance at closing of 200,000 shares of our common stock, a cash payment of approximately \$3.8 million (including a finders fee payment of approximately \$154,000, payment of \$108,000 to Barington and the payoff of shareholder loans of approximately \$612,000) less the value of the 200,000 shares of Dynabazaar common stock, the assumption of certain liabilities of approximately \$3.5 million, and deferred consideration of up to \$4 million in cash, contingent upon Costar and VSTC achieving certain levels of sales and EBITDA after the closing, through 2009 of which \$2,225 is recorded as a long-term liability. On September 29, 2006, the 200,000 shares of Dynabazaar common stock were issued.

There were no material relationships between Registrant or its affiliates and any of the parties to the Asset Purchase Agreement, other than in respect of such agreement.

Allocation of Purchase Price

Allocated to:

| | |
|-------------------|----------|
| Other intangibles | \$ 3,066 |
| Trade name | 1,587 |

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| | |
|-----------------------------|----------|
| Cash | 240 |
| Prepays | 105 |
| Deposits | 4 |
| Accounts receivables, net | 1,875 |
| Inventory | 2,623 |
| Property and equipment, net | 95 |
| | ----- |
| Total | 9,595 |
| Liabilities Assumed: | |
| Accounts payable and other | (1,634) |
| Revolver facilities | (1,863) |
| Issuance of common stock | (74) |
| Long term liability | (2,225) |
| | ----- |
| Net purchase price | \$ 3,800 |
| | ===== |

Intangible assets arose from the Costar acquisition. The aggregate of the estimated purchase price plus acquisition costs of an estimated \$9.6 million exceeded the fair market value for all identifiable net assets. An independent appraisal was conducted of all intangible assets (including, but not limited to, distribution agreements, customer lists, patents, trademarks and trade names, etc.) received as a result of the acquisition of Costar.

CRITICAL ACCOUNTING POLICIES

In December 2001, the Securities and Exchange Commission (the "SEC") requested that all registrants discuss their most "critical accounting policies" in management's discussion and analysis of financial condition and results of operations. The SEC indicated that a "critical accounting policy" is one which is both important to the portrayal of the company's financial condition and results and requires management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

Our significant accounting policies are more fully described in Note 1, Summary of Significant Accounting Policies, to our consolidated financial statements included in this Quarterly Report on Form 10-Q.

16

RESULTS OF OPERATIONS

THREE MONTHS ENDED MARCH 31, 2007 AND 2006 (\$ IN THOUSANDS)

Net loss

For the three months ended March 31, 2007 and March 31, 2006, our net loss (loss) was \$(31) and \$(112), respectively. Net loss in 2006 reflects business activity prior to the acquisition of an operating company.

Revenue

For the three months ended March 31, 2007 and March 31, 2006, total revenue was \$4,208 and \$0, respectively. Total revenue for the three months ended March 31, 2007 is entirely attributable to the activities of our recently acquired subsidiaries Costar and Video Solutions.

Operating Expenses

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For the three months ended March 31, 2007, general and administrative expenses were \$934 compared to \$215 for the three months ended March 31, 2006. The increase is entirely attributable to the activities of our recently acquired subsidiaries Costar and Video Solutions.

| | |
|---|-------|
| Major expense categories were: (in thousands) | |
| Payroll related | \$429 |
| Rent | \$29 |
| Accounting and tax preparation | \$60 |
| Depreciation and amortization | \$77 |
| Directors and Officers insurance | \$94 |
| Advertising | \$53 |
| Contract professional services | \$42 |
| | ----- |
| | \$784 |
| | ===== |

For the three months ended March 31, 2007 and March 31, 2006, interest income was \$35 and \$103, respectively. The decrease is entirely attributable to the decrease in cash held in interest bearing bank accounts.

For the three months ended March 31, 2007 and 2006, interest expense was \$12 and \$0, respectively. The increase is entirely attributable to the Company's line of credit.

17

LIQUIDITY AND CAPITAL RESOURCES (\$ IN THOUSANDS)

At March 31, 2007, cash and cash equivalents totaled \$2,770.

Cash used in operating activities was \$340 for the three months ended March 31, 2007, compared to cash used of \$120 for the three months ended March 31, 2006. Cash used in operating activities for the period ended March 31, 2007 primarily reflects the activities of our recently acquired operating subsidiaries, Costar and Video Solutions. Major changes in operating assets and liabilities reflect an increase in accounts receivable of \$481 and an increase in accounts payable of \$54, offset by depreciation and amortization of \$76, prepaid expenses of \$13 and an increase in inventories of \$27.

Cash used in investing activities for the three months ended March 31, 2007 was \$52 compared to cash provided of \$0 for the three months ended March 31, 2006. The cash used represents the purchase of fixed assets.

Cash provided by financing activities for the three months ended March 31, 2007 was \$224, compared to \$0 for the period ended March 31, 2006. The cash provided for the three months ended March 31, 2007 reflects a draw on the line of credit with the Bank of Texas.

We believe that our existing cash and cash equivalents will be sufficient to meet our anticipated cash needs for working capital and capital expenditures in the near future.

FACTORS THAT MAY AFFECT RESULTS OF OPERATIONS AND FINANCIAL CONDITION

This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act, of 1934 as amended (the "Exchange Act"). You can identify forward-looking statements by the use of the words "believe," "expect," "anticipate," "intend,"

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"estimate," "assume" and other similar expressions which predict or indicate future events and trends and which do not relate to historical matters. You should not rely on forward-looking statements, because they involve known and unknown risks, uncertainties and other factors, some of which are beyond our control. Our actual results could differ materially from those set forth in the forward-looking statements.

Some of the factors that might cause these differences include those set forth in the Company's Annual Report on Form 10-K for the year ended December 31, 2006 which is incorporated herein by reference. You should carefully review all of these factors, and you should be aware that there may be other factors that could cause these differences. Forward-looking statements herein are based on information, plans and estimates at the date of this Form 10-Q, and we do not promise to update any forward-looking statements to reflect changes in underlying assumptions or factors, new information, future events or other changes.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

INVESTMENT PORTFOLIO

We do not use derivative financial instruments for investment purposes and only invest in financial instruments that meet high credit quality standards. Due to the conservative nature of our investments, we do not believe that we have a material exposure to interest rate risk.

18

ITEM 4. CONTROLS AND PROCEDURES

As required by Rule 13a-15(b) under the Exchange Act, as of the end of the period covered by this Quarterly Report, our management conducted an evaluation with the participation of our Chief Executive Officer and Chief Financial Officer of the effectiveness of our disclosure controls and procedures (as defined in Rule 13d-15(e) or Rule 15d-15(e) of the Exchange Act). In designing and evaluating our disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and our management necessarily was required to apply its judgment in evaluating and implementing possible controls and procedures. The effectiveness of our disclosure controls and procedures is necessarily limited by the staff and other resources available to us. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this Quarterly Report, our disclosure controls and procedures were effective to ensure that information required to be disclosed by us in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. No change in our internal control over financial reporting (as defined in Rule 13d-15(f) or Rule 15d-15(f) of the Exchange Act) occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting. In connection with these rules, we will continue to review and document our disclosure controls and procedures, including our internal controls and procedures for financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our business.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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We are a defendant in certain purported class action lawsuits filed by individual shareholders in the U.S. District Court for the Southern District of New York against certain of our former officers and directors, and various of the underwriters in our initial public offering ("IPO") and secondary offering. The lawsuits have been filed by individual shareholders who purport to seek class action status on behalf of all other similarly situated persons who purchased our common stock between July 8, 1999 and December 6, 2000. A consolidated amended class action complaint was filed on April 19, 2002. The complaint alleges that certain underwriters of the IPO solicited and received excessive and undisclosed fees and commissions in connection with that offering. The complaint further alleges that the defendants violated the federal securities laws by issuing a registration statement and prospectus in connection with our IPO which failed to accurately disclose the amount and nature of the commissions and fees paid to the underwriter defendants. On or about October 8, 2002, the Court entered an Order dismissing the claims asserted against certain individual defendants in the consolidated actions without any payment from these individuals or us. On or about February 19, 2003, the Court entered an Order dismissing with prejudice the claims asserted against us under Section 10(b) of the Exchange Act. As a result, the only claims that remain against us are those arising under Section 11 of the Securities Act. The parties have negotiated and executed a definitive settlement agreement. The proposed settlement provides that the class members in the class action cases brought against the participating issuer defendants will be guaranteed a recovery of \$1 billion by insurers of the participating issuer defendants. If recoveries totaling \$1 billion or more are obtained by the class members from the underwriter defendants, however, the monetary obligations to the class members under the proposed settlement will be satisfied. In addition, we and any other participating issuer defendants will be required to assign to the class members certain claims that they may have against the underwriters of their IPO's. The proposed settlement contemplates that any amounts necessary to fund the settlement or settlement-related expenses would come from participating issuers' directors and officers' liability insurance policy proceeds as opposed to funds of the participating issuer defendants themselves. A participating issuer defendant could be required to contribute to the costs of the settlement if that issuer's insurance coverage were insufficient to pay that issuer's allocable share of the settlement costs. If ultimately approved by the Court, the proposed settlement would result in the dismissal, with prejudice, of all claims in the litigation against us and all of the other issuer defendants who have elected to participate in the proposed settlement, together with the current or former officers and directors of participating issuers who were named as individual defendants. The proposed settlement does not provide for the resolution of any claims against the underwriter defendants, and the litigation as against those defendants is continuing. Consummation of the proposed settlement remains conditioned upon obtaining approval by the Court. By order entered on September 1, 2005, the Court granted preliminarily approval of the proposed settlement and directed that notice of the terms of the proposed settlement be provided to class members. Thereafter, the court held a fairness hearing, on April 24, 2006, at which objections to the proposed settlement were heard. The Court has yet to issue a ruling on the motion for final approval. On December 5, 2006, the Court of Appeals for the Second Circuit reversed the Court's order certifying a class in six test cases that were selected by the underwriter defendants and plaintiffs in the coordinated proceeding. On April 6, 2007, the Court of Appeals denied the plaintiffs' petition for rehearing of the Court's December 5, 2006 ruling but noted that the plaintiffs remain free to ask the District Court to certify a different class which might meet the standards for class certification that the Court of Appeals articulated in its December 5,

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2006 decision. Because our proposed settlement with the plaintiffs involves the certification of the case against us as a class action for settlement purposes, it is unclear what impact, if any, the Second Circuit's class certification ruling will have on our case or the viability of the proposed settlement. In the event the settlement is not finalized, the Company believes that it has meritorious defenses to plaintiffs' claims and intends to defend the action vigorously.

The expense of defending this litigation may be significant. The amount of time to resolve these lawsuits is unpredictable and defending us may divert management's attention from the day-to-day operations of our business, which could adversely affect our business, results of operations and cash flows. In addition, an unfavorable outcome in such litigation could have a material adverse effect on our business, results of operations and cash flows.

20

ITEM 6. EXHIBITS

- 31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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.

DYNABAZAAR, INC.

Date: May 15, 2007

By: /s/ Sebastian Cassetta

Sebastian Cassetta
Chief Executive Officer (Principal
Executive Officer)

Date: May 15, 2007

By: /s/ Melvyn Brunt

Melvyn Brunt
Chief Financial Officer (Principal
Financial and Accounting Officer)

21