

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

NOCOPI TECHNOLOGIES INC/MD/  
Form 10QSB  
August 13, 2004

U.S. SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

Form 10-QSB

(Mark One)

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

For the quarterly period ended June 30, 2004.

TRANSITION REPORT PURSUANT TO SECTIONS 13 OR 15(d) OF THE  
SECURITIES EXCHANGE ACT OF 1934.

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 0-20333

NOCOPI TECHNOLOGIES, INC.

-----  
(Exact name of small business issuer as  
specified in its charter)

MARYLAND

87-0406496

-----  
(State or other jurisdiction of  
incorporation or organization)

-----  
(IRS Employer Identification No.)

9C Portland Road, West Conshohocken, PA 19428

-----  
(Address of principal executive offices)

(610) 834-9600

-----  
(Issuer's telephone number)

Check whether the issuer has (1) filed all reports required to be filed by  
Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such  
shorter period that the registrant was required to file such reports), and (2)  
has been subject to such filing requirements for the past 90 days. Yes  No

State the number of shares outstanding of each of the issuer's classes of  
common equity, as of August 1, 2004: Common stock, par value \$.01 per share:  
45,972,241 shares.

Transitional Small Business Disclosure Format (check one): Yes  No

NOCOPI TECHNOLOGIES, INC.

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

INDEX

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

Statements of Operations for Three and Six Months  
Ended June 30, 2004 and June 30, 2003

Balance Sheet at June 30, 200

Statements of Cash Flows for Six Months Ended June 30, 2004  
and June 30, 2003

Notes to Financial Statements

Item 2. Management's Discussion and Analysis  
of Financial Condition and Results of Operations

Item 3. Controls and Procedures

Part II. OTHER INFORMATION

Item 1. Legal Proceedings

Item 2. Changes in Securities and use of Proceeds

Item 3. Defaults Upon Senior Securities

Item 4. Submission of matters to a Vote of Security Holders

Item 5. Other Information

Item 6. Exhibits and Reports on Form 8-K

SIGNATURES

INDEX TO EXHIBITS

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Nocopi Technologies, Inc.  
Statements of Operations  
(unaudited)

Three Months ended June 30	
2004	2003
-----	-----

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Revenues		
Licenses, royalties and fees	\$ 95,300	\$ 78,600
Product and other sales	49,000	75,400
	-----	-----
	144,300	154,000
Cost of sales		
Licenses, royalties and fees	28,700	42,700
Product and other sales	22,300	36,400
	-----	-----
	51,000	79,100
	-----	-----
Gross profit	93,300	74,900
Operating expenses		
Research and development	42,000	49,400
Sales and marketing	38,000	31,900
General and administrative (exclusive of legal expenses)	104,800	60,300
Legal expenses	28,900	30,200
	-----	-----
	213,700	171,800
	-----	-----
Loss from operations	(120,400)	(96,900)
Other income (expenses)		
Interest income	--	200
Interest expense and bank charges	(3,300)	(3,500)
Net proceeds from arbitration settlement	--	932,700
	-----	-----
	(3,300)	929,400
	-----	-----
Net earnings (loss)	(\$123,700)	\$832,500
	=====	=====
Basic and diluted earnings (loss) per common share	(\$ .00)	\$.02
Weighted average common shares outstanding	45,972,241	45,972,241

\*The accompanying notes are an integral part of these financial statements.

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Current assets		
Cash and cash equivalents		\$
Accounts receivable less \$15,000 allowance		
Arbitration settlement receivable		
Prepaid and other		
		---
Total current assets		
Fixed assets		
Leasehold improvements		
Furniture, fixtures and equipment		
		---
Less: accumulated depreciation		
		---
Other assets		
Arbitration settlement receivable		
		---
Total assets		\$
		===
	Liabilities and Stockholders' Deficiency	
Current liabilities		
Demand loans		
Accounts payable		
Accrued expenses		
Deferred revenue		
		---
Total current liabilities		
Stockholders' deficiency		
Common stock, \$.01 par value		
Authorized - 75,000,000 shares		
Issued and outstanding - 45,972,241 shares		
Paid-in capital		11
Accumulated deficit		(12,
		---
		(
		---
Total liabilities and stockholders' deficiency		\$
		===

\*The accompanying notes are an integral part of these financial statements

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Operating Activities

Net earnings (loss) (\$2  
Adjustments to reconcile net earnings (loss) to cash from operating activities  
Depreciation  
Compensation expense - stock option grants

(INCREASE) DECREASE IN ASSETS

ACCOUNTS RECEIVABLE  
Arbitration settlement receivable  
Prepaid and other  
Increase (decrease) in liabilities  
Accounts payable and accrued expenses  
Deferred revenue

Cash provided by (used in) operating activities

Investing Activities

Additions to fixed assets  
Investment in affiliate

Cash provided by (used in) investment activities

Financing Activities

Demand loans

Cash provided by investment activities

Increase (decrease) in cash and cash equivalents  
Cash and cash equivalents - beginning of period

Cash and cash equivalents - end of period

\*The accompanying notes are an integral part of these financial statements

3

NOCOPI TECHNOLOGIES, INC.  
-----

NOTES TO FINANCIAL STATEMENTS  
(UNAUDITED)

NOTE 1. FINANCIAL STATEMENTS

The accompanying unaudited condensed financial statements have been prepared by Nocopi Technologies, Inc. (the Company). These statements

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

include all adjustments (consisting only of normal recurring adjustments) which management believes necessary for a fair presentation of the statements and have been prepared on a consistent basis using the accounting policies described in the summary of Accounting Policies included in the Company's 2003 Annual Report on Form 10-KSB. Certain financial information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the accompanying disclosures are adequate to make the information presented not misleading. The Notes to Financial Statements included in the 2003 Annual Report on Form 10-KSB should be read in conjunction with the accompanying interim financial statements. The interim operating results for the three and six months ended June 30, 2004 may not be necessarily indicative of the operating results expected for the full year.

### NOTE 2. GOING CONCERN

Since its inception, the Company has incurred significant losses and, as of June 30, 2004, had accumulated losses of \$12,247,200. For the years ended December 31, 2003 and 2002, the Company's losses from operations were \$441,300 and \$915,200, respectively. In addition, the Company had negative working capital of \$750,500 at June 30, 2004. The Company may incur further operating losses and experience negative cash flow in the future. Achieving profitability and positive cash flow depends on the Company's ability to generate and sustain significant increases in revenues and gross profits from its traditional business. There can be no assurances that the Company will be able to generate sufficient revenues and gross profits to achieve and sustain profitability and positive cash flow in the future.

The receipt of cash in the aggregate amount of \$900,000 in June 2003 in conjunction with the settlement of its arbitration proceedings with Euro-Nocopi, S.A., an independent licensee, has permitted the Company to continue in operation to the current date. As a result of the settlement, the significant legal fees incurred in the arbitration have been eliminated. Additionally, the Company has reduced staff and, in 2003, completed its relocation to a new facility that it believes will enable the Company to further reduce its operating expenses. Management of the Company believes that it will need to obtain additional capital in the immediate future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases can be realized. The Company believes that without additional capital, whether in the form of debt, equity or both, it may be forced to cease operations during the third quarter of 2004.

4

### NOTE 3. SETTLEMENT OF ARBITRATION WITH AFFILIATE

In June 2003, the Company settled its arbitration proceeding commenced by Euro-Nocopi, S.A. (Euro). Under the terms of the settlement, Euro paid \$900,000 to Nocopi and will pay an additional \$200,000 in the future for back royalties and all other matters in dispute between the two companies, as well as the termination of Nocopi's 18% ownership of Euro. As part of the settlement, the Company and Euro entered into an amended and restated license pursuant to which the Company has agreed that Euro may continue to market the Company's technologies in Europe. The \$200,000 is being paid in four equal annual installments commencing

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

in March 2004. The Company recorded a net gain of \$932,700 and \$875,300, respectively, in the second quarter and first half of 2003 representing the proceeds of the settlement net of the Company's \$110,600 investment in Euro and legal expenses incurred during 2003 related to the arbitration.

For the first quarter of 2003 arbitration related legal expense of \$57,400 was reclassified from legal expenses to net proceeds from arbitration settlement.

### NOTE 4. DEMAND LOANS

The Company has unsecured loans from three individuals totaling \$149,900, including \$37,900 from the Company's Chairman of the Board, outstanding at June 30, 2004. The loans bear interest at seven per cent per year and are payable on demand. In the third quarter of 2004, the Company and the lenders discussed the conversion of the outstanding balance of the loans, together with accrued interest thereon, into shares of Common Stock of the Company. The lenders and the Company are currently negotiating the definitive terms of the conversion.

### NOTE 5. INCOME TAXES

There is no provision for income taxes for the three months and six months ended June 30, 2004 since Management has determined that the realization of the net deferred tax asset is not assured and has created a valuation allowance for the entire amount of such benefits.

### NOTE 6. STOCK OPTIONS ISSUED TO EMPLOYEES

The Company applies Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for the issuance of its stock options. Accordingly, no compensation cost has been recognized for its stock options issued during the six months ended June 30, 2004. Had compensation cost for the Company's issuance of vested stock options been determined based on the fair value at grant dates for options consistent with the method of SFAS No. 123, the Company's net loss would have been increased to the pro forma amounts indicated below. The net loss per share would not change. Fair value amounts were estimated using the Black-Scholes model with the following assumptions: no dividend yield, expected volatility of 60%, and a risk-free interest rate of 4% for the three and six months ended June 30, 2004. There were no options issued for the six months ended June 30, 2004.

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

		Three Months Ended June 30, 2004 -----	Six Mo June -----
Net loss	As reported	(\$123,700)	(\$
	Pro forma	(\$146,700)	(\$
Net loss per share	As reported	(\$ .00)	
	Pro forma	(\$ .00)	

6

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

FORWARD-LOOKING INFORMATION

The following Management's Discussion and Analysis of Results of Operations and Financial Condition should be read in conjunction with our audited Financial Statements and Notes thereto for the year ended December 31, 2003 included in our Annual Report on Form 10-KSB filed with the Securities and Exchange Commission.

The information in this discussion contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause our actual results, performance or achievements or industry results to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Such factors include those described in "Uncertainties That May Affect the Company, its Operating Results and Stock Price." The forward-looking statements included in this report may prove to be inaccurate. In light of the significant uncertainties inherent in these forward-looking statements, you should not consider this information to be a guarantee by us or any other person that our objectives and plans will be achieved. The Company does not undertake to publicly update or revise its forward-looking statements even if experience or future changes make it clear that any projected results (expressed or implied) will not be realized.



## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

### RESULTS OF OPERATIONS

The Company's revenues are derived from royalties paid by licensees of the Company's technologies, fees for the provision of technical services to licensees and from the direct sale of products incorporating the Company's technologies, such as inks, security paper and pressure sensitive labels, and equipment used to support the application of the Company's technologies, such as ink-jet printing systems. Royalties consist of guaranteed minimum royalties payable by the Company's licensees in certain cases and additional royalties which typically vary with the licensee's sales or production of products incorporating the licensed technology. Service fees and sales revenues vary directly with the number of units of service or product provided.

Since the Company's fixed costs have been reduced as a result of its relocation to a new location in 2003 and the Company believes that further fixed cost reductions may not be achievable, its operating results are substantially dependent on revenue levels. Because revenues derived from licenses and royalties carry a much higher gross profit margin than other revenues, operating results are also substantially affected by changes in the sources of revenues.

Both the absolute amounts of the Company's revenues and the mix among the various sources of revenue are subject to substantial fluctuation. The Company has a relatively small number of substantial customers rather than a large number of small customers. Accordingly, changes in the revenue received from a significant customer can have a substantial effect on the Company's total revenue and on its revenue mix and overall financial performance. Such changes may result from a customer's product development delays, engineering changes, changes in product marketing strategies and the like. In addition, certain customers have, from time to time, sought to renegotiate certain provisions of

7

their license agreements and, when the Company agrees to revise terms, revenues from the customer may be affected. The addition of a substantial new customer or the loss of a substantial existing customer may also have a substantial effect on the Company's total revenue, revenue mix and operating results.

Revenues for the second quarter of 2004 were \$144,300 compared to \$154,000 in the second quarter of 2003, a 6% decline. Licenses, royalties and fees increased by \$16,700, or 21%, to \$95,300 in the second quarter of 2004 from \$78,600 in the second quarter of 2003. The increase in licenses, royalties and fees is due primarily to the inception during the second half of 2003 and the first half of 2004 of license arrangements with three customers offset in part by the termination of one license agreement during the second half of 2003. Product sales were \$49,000 in the second quarter of 2004 compared to \$75,400 in the second quarter of 2003, a 35% decrease due primarily to lower sales of the Company's security paper and inks. For the first six months of 2004, revenues were \$284,900, 5% lower than revenues of \$298,900 in the first six months of 2003. Licenses, royalties and fees of \$172,900 in the first half of 2004 approximated the \$171,100 in the first half of 2003 due primarily to the inception of three new license arrangements over the preceding twelve months offset in part by the termination of licenses with three licensees during 2003. Product sales were \$112,000 in the first half of 2004 compared to \$127,800 in the first half of 2003, a 12% decline. The decrease in product sales reflects lower sales of the Company's line of security papers and inks during the first half of 2004 compared to the first half of 2003.

The Company's gross profit increased to \$93,300 in the second quarter

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

of 2004 or 64% of revenues from \$74,900 or 49% of revenues in the second quarter of 2003. Licenses, royalties and fees carry a substantially higher gross profit than product sales, which generally consist of supplies or other manufactured products which incorporate the Company's technologies or equipment used to support the application of its technologies. These items (except for inks which are manufactured by the Company) are generally purchased from third-party vendors and resold to the end-user or licensee and carry a significantly lower gross profit than licenses, royalties and fees. The higher gross profit in the second quarter of 2004 compared to the second quarter of 2003 results principally from an increase in revenues represented by licenses, royalties and fees as well as lower costs of production of the ink products used by licensees and paper purchased for resale. Additionally, the Company experienced lower rent and occupancy costs resulting from the move of the facility in the second half of 2003.

For the first six months of 2004, the gross profit was \$171,400, or 60% of revenues compared to \$152,400, or 51% of revenues, in the first half of 2003. The increase in the gross profit in both absolute dollars and percentage of revenues in the first half of 2004 compared to the first half of 2003 resulted from the same factors as the second quarter.

Research and development expenses decreased to \$42,000 in the second quarter of 2004 from \$49,400 in the second quarter of 2003. For the first six months of 2004, research and development expenses were \$94,000 compared to \$98,600 in the first half of 2003. The decrease in both the second quarter and first half of 2004 relates primarily to lower rent, occupancy and employee benefits expenses in 2004 compared to 2003.

Sales and marketing expenses were \$38,000 in the second quarter of 2004 compared to \$31,900 in the second quarter of 2003. The increase in the second quarter of 2004 compared to the second quarter of 2003 reflects marketing costs associated with the introduction of the Company's new Rub-n-Color product for the Educational and Toy Market. For the first six months of 2004, sales and

8

marketing expenses were \$83,000 compared to \$118,100 in the first six months of 2003. The decrease in the first half of 2004 relates primarily to the departure of a sales executive late in the first quarter of 2003 and lower consulting fees in the first half of 2004 compared to the first half of 2003 offset in part by marketing costs associated with the introduction of the Company's new Rub-n-Color product for the Educational and Toy Market

General and administrative expenses (exclusive of legal expenses) increased to \$104,800 in the second quarter of 2004 from \$60,300 in the second quarter of 2003. The increase in the second quarter of 2004 compared to the second quarter of 2003 is due primarily to \$58,000 in expenses recorded in connection with the issuance to members of the Company's Board of Directors and two consultants of 900,000 options to purchase shares of the Company's common stock during the second quarter of 2004 offset in part by lower rent, occupancy and public relations costs. For the first six months, general and administrative expenses (exclusive of legal expense) increased to \$160,500 in 2004 from \$144,100 in 2003 as a result as the same factors as the second quarter increase.

Legal expenses of \$28,900 in the second quarter of 2004 approximated the \$30,200 in the second quarter of 2003. Legal expenses for the first half of

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

2004 increased to \$62,300 from \$48,800 in the first half of 2003 due primarily to compliance with recently enacted securities legislation and regulations. The second quarter and first half 2003 legal fees associated with the Euro-Nocopi, S.A. arbitration proceedings which were settled in June 2003 were offset against the settlement proceeds.

Other income (expense) includes interest income on funds invested and interest expense on the Demand Loans. Net proceeds from arbitration settlement includes the net gain of \$932,700 and \$875,300, respectively, in the second quarter and first half of 2003 representing the proceeds of the arbitration settlement with Euro-Nocopi, S.A., net of the Company's \$110,600 investment in Euro-Nocopi, S.A. and legal expenses incurred during 2003 related to the arbitration.

The net loss of \$123,700 and \$235,100, respectively, in the second quarter and first half of 2004 compared to net earnings of \$832,500 and \$611,500, respectively, in the second quarter and first half of 2003 results primarily from the settlement of the arbitration proceedings with Euro-Nocopi, S.A. during the second quarter of 2003, the expense associated with the issuance of stock options to Directors and consultants in the second quarter of 2004, lower rent and occupancy costs due to the move to a new facility during 2003 and staff reductions during 2003.

### PLAN OF OPERATION, LIQUIDITY AND CAPITAL RESOURCES

The Company's cash and cash equivalents decreased to \$7,700 at June 30, 2004 from \$89,900 at December 31, 2003. The cash was used to fund operations over the six-month period.

The loss of a number of customers during the past three years and the loss of periodic fees under the license agreement with Euro-Nocopi, S.A. commencing in 2000 have had a material adverse effect on the Company's revenues and results of operations and upon its liquidity and capital resources. The receipt of \$900,000 in June 2003 in conjunction with the settlement of its arbitration proceedings with Euro-Nocopi, S.A. has permitted the Company to continue in operation to the current date. As a result of the settlement, a significant ongoing expense for related legal fees has been eliminated.

9

Additionally, the Company has reduced staff and, during the third quarter of 2003, completed its relocation to a new facility that it believes will enable the Company to further reduce its operating expenses. Management of the Company believes that it will need to obtain additional capital in the immediate future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases can be realized. The Company believes that without additional capital, in the form of debt, equity or both, it may be forced to cease operations during the third quarter of 2004.

The Company, in response to the ongoing adverse liquidity situation, has maintained a cost reduction program including staff reductions and curtailment of discretionary research and development and sales and marketing expenses, where possible.

### UNCERTAINTIES THAT MAY AFFECT THE COMPANY, ITS OPERATING RESULTS AND STOCK PRICE

The Company's operating results and stock price are dependent upon a

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

number of factors, some of which are beyond the Company's control. These include:

Inability to Continue in Operation Without Immediate New Equity Investment. The Company had a negative working capital of \$750,500 at June 30, 2004 and experienced negative cash flow from operations of \$81,400 in the six months ended June 30, 2004. Additionally, it experienced negative cash flow from operations of \$78,800 (including \$900,000 received in settlement of its arbitration proceedings with Euro-Nocopi, S.A.) in the year ended December 31, 2003. Management of the Company believes that while certain staff reductions initiated in 2003 and the move of the Company's operations to a new facility, which was completed during 2003, will reduce the Company's negative cash flow, it anticipates that the negative cash flow will continue until it can achieve revenue increases. Management believes that it will need to obtain additional capital in the immediate future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases can be realized. There can be no assurances that the Company will be successful in obtaining sufficient additional capital, or if it does, that the additional capital will enable the Company to improve its business so as to have a material positive effect on the Company's operations and cash flow. The Company believes that without additional capital, in the form of debt, equity or both, it may be forced to cease operations during the third quarter of 2004. It is uncertain whether the Company's assets will retain any value if the Company ceases operations. There are no assurances that the Company will be able to secure additional equity investment before it may be forced to cease operations.

Possible Inability to Develop New Business. Even if the Company is able to raise cash through additional capital or otherwise, it must quickly improve its operating cash flow. Because the Company has already significantly reduced its operating expenses, Management believes that any significant improvement in the Company's cash flow must result from increases in its revenues from traditional sources and from new revenue sources. The Company's ability to develop new revenues may depend on the extent of both its marketing activities and its research and development activities. There are no assurances that the resources the Company, even with additional capital, can devote to marketing and to research and development will be sufficient to increase the Company's revenues to levels resulting in positive cash flow.

Inability to Obtain Raw Materials and Products for Resale. The Company's adverse financial condition has required it to significantly defer payments due vendors who supply raw materials and other components of the Company's security inks,

security paper that the Company purchases for resale and professional and other services. As a result, the Company is on credit hold with certain of its suppliers and is required to pay cash in advance of shipment to others. Delays in shipments to customers caused by the Company's inability to obtain materials on a timely basis and the possibility that certain current vendors may permanently discontinue to supply the Company with needed products could impact the Company's ability to service its customers and adversely affect its customer and licensee relationships. Management of the Company believes that, without significant capital investment in the very near term, the Company will not be able to maintain acceptable relationships with its vendors and professional service providers. There are no assurances that the Company will be able to secure sufficient capital investment to maintain its vendor accounts on satisfactory terms.

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Uneven Pattern of Quarterly and Annual Operating Results. The Company's revenues, which are derived primarily from licensing and royalties, are difficult to forecast due to the long sales cycle of the Company's technologies, the potential for customer delay or deferral of implementation of the Company's technologies, the size and timing of inception of individual license agreements, the success of the Company's licensees and strategic partners in exploiting the market for the licensed products, modifications of customer budgets, and uneven patterns of royalty revenue and product orders. As the Company's revenue base is not substantial, delays in finalizing license contracts, implementing the technology to initiate the revenue stream and customer ordering decisions can have a material adverse effect on the Company's quarterly and annual revenue expectations and, as the Company believes that further reductions in the fixed component of the Company's operating expenses may not be achievable, income expectations will be subject to a similar adverse outcome.

Volatility of Stock Price. The market price for the Company's common stock has historically experienced significant fluctuations and may continue to do so. The Company has, since its inception, operated at a loss and has not produced revenue levels traditionally associated with publicly traded companies. The Company's common stock is not listed on a national or regional securities exchange and, consequently, the Company receives limited publicity regarding its business achievements and prospects, few securities analysts and traders follow it and it is thinly traded. The market price may be affected by announcements of new relationships or modifications to existing relationships. The stock prices of many developing public companies, particularly those with small capitalizations, have experienced wide fluctuations not necessarily related to operating performance. Such fluctuations may adversely affect the market price of the Company's common stock.

Intellectual Property. The Company relies on a combination of protections provided under applicable international patent, trademark and trade secret laws. It also relies on confidentiality, non-analysis and licensing agreements to establish and protect its rights in its proprietary technologies. While the Company actively attempts to protect these rights, the Company's technologies could possibly be compromised through reverse engineering or other means. In addition, the Company's ability to enforce its intellectual property rights through appropriate legal action has been and will continue to be limited by the Company's adverse liquidity. There can be no assurances that the Company will be able to protect the basis of its technologies from discovery by unauthorized third parties or to preclude unauthorized persons from conducting activities that infringe on the Company's rights. The Company's adverse liquidity situation has also impacted its ability to obtain patent protection on its intellectual property and to maintain protection on previously issued patents. The Company has paid approximately \$7,000 in patent maintenance fees that are due during

11

2004 as advised by its patent counsel. There can be no assurances that the Company will be able to continue to prosecute new patents and maintain issued patents. As a result, the Company's customer and licensee relationships could be adversely affected and the value of the Company's technologies and intellectual property (including their value upon a liquidation of the Company) could be substantially diminished.

### OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements.

### RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

## Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

In December 2002, the FASB issued Statement of Financial Accounting Standard No. 148 ("SFAS 148"), Accounting for Stock-Based Compensation - Transition and Disclosure. SFAS 148 provides alternative methods of transition for voluntary change to the fair value based method of accounting for stock-based employee compensation. SFAS 148 also requires prominent disclosure in the "Summary of Significant Accounting Policies" of both annual and interim financial statements about the method used on reported results. The Company has adopted the disclosure requirements of SFAS 148 for the 2003 fiscal year. Adoption of this statement has affected the location of the Company's disclosure in the consolidated financial statements, but will not impact the Company's results of operation or financial position unless the Company changes to the fair value method of accounting for stock-based employee compensation.

On April 22, 2003, the FASB announced its decision to require all companies to expense the fair value of employee stock options. Companies will be required to measure the cost according to the fair value of the options. Although the new guidelines have not yet been released, it is expected that they will be finalized soon and be effective in 2004. When final rules are announced, the Company will assess the impact to its financial statements.

The following recently issued accounting pronouncements are currently not applicable to the Company.

In January 2003, subsequently revised December 2003, the FASB issued FASB Interpretation No. 46 ("FIN 46"), Consolidation of Variable Interest Entities - An Interpretation of AARB No. 51. FIN 46 requires that if any entity has a controlling financial interest in a variable interest entity, the assets, liabilities and results of activities of the variable interest entity should be included in the consolidated financial statements of the entity. FIN 46 provisions are effective for all arrangements entered into after January 31, 2003. FIN 46 provisions are required to be adopted for the first period ending after December 15, 2004 for a small business issuer.

In May 2003, the FASB issued Statement of Financial Accounting Standard No. 150 ("SFAS 150"), Accounting for Certain Financial Instruments With Characteristics of Both Liabilities and Equity. SFAS 150 clarifies the accounting for certain financial instruments with characteristics of both liabilities and equity and requires those instruments be classified as liabilities on the balance sheet. Previously, many of those financial statements were classified as equity. SFAS 150 is effective for financial instruments entered into or modified after May 31, 2003 and otherwise is effective at the beginning of the first interim period beginning after June 15, 2003.

### ITEM 3. DISCLOSURE CONTROLS AND PROCEDURES

The Company has carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company that is required to be included in the Company's periodic filings with the Securities and Exchange Commission. There have been no significant changes in the Company's internal controls or, to the Company's knowledge, in other factors that could significantly affect those internal

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

controls subsequent to the date the Company carried out its evaluation.

13

PART II - OTHER INFORMATION

- Item 1. Legal Proceedings
- Not Applicable
- Item 2. Changes in Securities
- Not Applicable
- Item 3. Defaults Upon Senior Securities
- Not Applicable
- Item 4. Submission of Matters to a Vote of Security Holders
- Not Applicable
- Item 5. Other Information
- Not Applicable
- Item 6. Exhibits and Reports on Form 8-K
- (a) Exhibits
- 31.1 Certificate of Chief Executive Officer required by Rule 13a-14(a).
- 31.2 Certificate of Chief Financial Officer required by Rule 13a-14(a).
32. Certificate of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- (b) Reports on Form 8-K
- The Registrant filed the following Current Reports on Form 8-K during the quarter ended June 30, 2004.
- April 20, 2004 - Press Release dated April 20, 2004

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

May 11, 2004 - Press Release dated May 11, 2004

14

SIGNATURES

Pursuant to the requirement 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.

NOCOPI TECHNOLOGIES, INC.

DATE: August 13, 2004

/s/ Michael A. Feinstein, M.D.  
-----

Michael A Feinstein, M.D.  
Chairman of the Board

/s/ Rudolph A. Lutterschmidt  
-----

Rudolph A. Lutterschmidt  
Vice President & Chief Financial Officer

15

EXHIBIT INDEX

- 31.1 Certificate of Chief Execution Officer pursuant to Rule 13a 0 14(a) and 15d - 14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certificate of Chief Financial Officer pursuant to Rule 13a 0 14(a) and 15d - 14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32. Certificate pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.



