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SCIENTIFIC INDUSTRIES INC
Form 10-Q
February 10, 2017

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

FORM 10-Q

(Mark One)

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

For quarterly period ended December 31, 2016

TRANSITION REPORT UNDER SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 0-6658

SCIENTIFIC INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

Delaware

04-2217279

(State or other jurisdiction of incorporation or organization)

(IRS Employer Identification No.)

80 Orville Drive, Suite 102, Bohemia, New York

11716

(Address of principal executive offices)

(Zip Code)

(631)567-4700

(Registrant's telephone number, including area code)

Not Applicable

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

Indicate by check whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act 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, a non-accelerated filer, or a small reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "small reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated Filer

Non-accelerated filer

Smaller reporting company (X)

(Do not check if a smaller reporting company)

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

Yes No

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The number of shares outstanding of the issuer's common stock par value, \$0.05 per share, as of February 3, 2017 was 1,489,112 shares.

TABLE OF CONTENTS

PART I - FINANCIAL INFORMATION

ITEM 1 CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED):

| | Page |
|--|-------|
| | <hr/> |
| Condensed Consolidated Balance Sheets | 1 |
| Condensed Consolidated Statements of Operations | 2 |
| Condensed Consolidated Statements of Comprehensive Income (Loss) | 3 |
| Condensed Consolidated Statements of Cash Flows | 4 |
| Notes to Condensed Consolidated Financial Statements | 5 |
| ITEM 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS | 13 |
| ITEM 4 CONTROLS AND PROCEDURES | 16 |
| PART II - OTHER INFORMATION | |
| ITEM 6 EXHIBITS AND REPORTS ON FORM 8-K | 16 |
| SIGNATURE | 17 |
| EXHIBITS | 18 |

PART I-FINANCIAL INFORMATION
Item 1. Financial Statements

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SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
ASSETS

| | September 30, 2016 | June 30, 2016 |
|---|-----------------------|------------------|
| Current Assets: | | |
| Cash and cash equivalents | \$ 897,100 | \$ 1,245,000 |
| Investment securities | 290,900 | 290,100 |
| Trade accounts receivable, net | 1,668,000 | 1,231,900 |
| Inventories | 2,125,000 | 2,412,100 |
| Prepaid expenses and other current assets | 122,500 | 47,200 |
| Deferred taxes | 127,500 | 140,600 |
| | 5,231,000 | 5,366,900 |
| Property and equipment at cost, net | 220,200 | 251,100 |
| Intangible assets, net | 758,300 | 897,600 |
| Goodwill | 705,300 | 705,300 |
| Other assets | 52,500 | 52,500 |
| Deferred taxes | 277,500 | 275,900 |
| | \$7,244,800 | \$7,549,300 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current Liabilities: | | |
| Accounts payable | \$ 300,200 | \$ 342,400 |
| Customer advances | 17,000 | - |
| Bank line of credit | 250,000 | - |
| Notes payable, current portion | 6,500 | 6,400 |
| Dividends payable | 44,700 | - |
| Accrued expenses and taxes, current portion | 510,300 | 849,700 |
| Contingent consideration, current portion | 161,800 | 136,500 |
| | 1,290,500 | 1,335,000 |
| Notes payable, less current portion | 9,200 | 12,500 |
| Contingent consideration payable, less current portion | 67,100 | 209,800 |
| Accrued expenses, less current portion | - | 60,000 |
| | 1,366,800 | 1,617,300 |
| Shareholders' equity: | | |
| Common stock, \$.05 par value; authorized 7,000,000 shares; 1,508,914 outstanding at | | |
| December 31, 2016 and June 30, 2016 | 75,400 | 75,400 |
| Additional paid-in capital | 2,499,500 | 2,498,500 |
| Accumulated other comprehensive income (loss) | (6,000) | 900 |
| Retained earnings | 3,361,500 | 3,409,600 |
| | 5,930,400 | 5,984,400 |
| Less common stock held in treasury, at cost, 19,802 shares | 52,400 | 52,400 |

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| | | |
|--|-------------|-------------|
| Total shareholders' equity | 5,878,000 | 5,932,000 |
| Total liabilities and shareholders' equity | \$7,244,800 | \$7,549,300 |
| | ===== | ===== |

See notes to unaudited condensed consolidated financial statements

1

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

| | For the Three Month Periods Ended December 31, | | For the Six Month Periods Ended December 31, | |
|---|--|-------------|--|-------------|
| | 2016 | 2015 | 2016 | 2015 |
| Revenues | \$2,683,800 | \$2,028,200 | \$4,242,900 | \$3,472,600 |
| Cost of revenues | 1,888,900 | 1,190,500 | 2,778,400 | 2,039,800 |
| Gross profit | 794,900 | 837,700 | 1,464,500 | 1,432,800 |
| Operating Expenses: | | | | |
| General & administrative | 409,200 | 395,700 | 821,600 | 803,900 |
| Selling | 224,200 | 227,200 | 440,900 | 394,200 |
| Research & development | 105,000 | 84,100 | 220,400 | 169,500 |
| Total operating expenses | 738,400 | 707,000 | 1,482,900 | 1,367,600 |
| Income (loss) from operations | 56,500 | 130,700 | (18,400) | 65,200 |
| Other income (expense): | | | | |
| Interest income | 8,800 | 5,000 | 9,100 | 5,400 |
| Other | 400 | 1,400 | 5,700 | (3,300) |
| Interest expense | (900) | (14,000) | (1,100) | (22,100) |
| Total other income, (expense), net | 8,300 | (7,600) | 13,700 | (20,000) |
| Income (loss) before income tax expense (benefit) | 64,800 | 123,100 | (4,700) | 45,200 |
| Income tax expense (benefit): | | | | |
| Current | 20,900 | 40,900 | (15,400) | 40,900 |
| Deferred | (1,400) | (12,200) | 14,100 | (30,000) |
| Total income tax expense (benefit) | 19,500 | 28,700 | (1,300) | 10,900 |
| Net income (loss) | \$ 45,300 | \$ 94,400 | (\$ 3,400) | \$ 34,300 |
| | ===== | ===== | ===== | ===== |

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| | | | | |
|--|--------|--------|--------|--------|
| Basic and diluted earnings per common share | \$.03 | \$.06 | \$.00 | \$.02 |
| Cash dividends declared per common share | \$.03 | \$ - | \$.03 | \$ - |

See notes to unaudited condensed consolidated financial statements

2

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

| | For the Three Month Periods Ended December 31, | | For the Six Month Periods Ended December 31, | |
|--|--|-----------|--|-----------|
| | 2016 | 2015 | 2016 | 2015 |
| Net income (loss) | \$ 45,300 | \$ 94,400 | (\$ 3,400) | \$ 34,300 |
| Other comprehensive income (loss): | | | | |
| Unrealized holding loss on investments arising during period, net of tax | (8,000) | (1,100) | (6,900) | (4,900) |
| Comprehensive income (loss) | \$ 37,300 | \$ 93,300 | (\$ 10,300) | \$ 29,400 |
| | ===== | ===== | ===== | ===== |

See notes to unaudited condensed consolidated financial statements

3

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

| | For the Three Month Periods Ended December 31, | For the Six Month Periods Ended December 31, |
|--|--|--|
| | 2016 | 2015 |
| Operating activities: | | |
| Net income (loss) | | (\$ 3,400) \$ 34,300 |
| Adjustments to reconcile net income (loss) | | |

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| | | |
|--|------------|-------------|
| to net cash used in operating activities: | | |
| Loss on asset disposal | - | 2,700 |
| Loss on sale of investments | (2,600) | - |
| Depreciation and amortization | 189,500 | 210,800 |
| Deferred income tax benefit expense | 14,100 | (30,000) |
| Stock-based compensation | 1,000 | 1,200 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (436,100) | 211,600 |
| Inventories | 287,100 | (1,048,800) |
| Prepaid expenses and other | | |
| current assets | (75,300) | 13,000 |
| Accounts payable | (42,200) | 144,500 |
| Customer advances | 17,000 | 33,700 |
| Accrued expenses and taxes | (399,400) | 259,600 |
| | <hr/> | <hr/> |
| Total adjustments | (446,900) | (201,700) |
| | <hr/> | <hr/> |
| Net cash used in operating | | |
| activities | (450,300) | (167,400) |
| | <hr/> | <hr/> |
| Investing activities: | | |
| Redemption of investment securities, | | |
| available-for-sale | 11,100 | - |
| Purchase of investment securities, | | |
| available-for-sale | (18,700) | (2,700) |
| Capital expenditures | (4,700) | (8,400) |
| Purchase of other intangible assets | (14,700) | (5,700) |
| | <hr/> | <hr/> |
| Net cash used in | | |
| investing activities | (27,000) | (16,800) |
| | <hr/> | <hr/> |
| Financing activities: | | |
| Line of credit proceeds | 250,000 | 470,000 |
| Payment of contingent consideration | (117,400) | (100,900) |
| Principal payments on note payable | (3,200) | - |
| | <hr/> | <hr/> |
| Net cash provided by financing | | |
| activities | 129,400 | 369,100 |
| | <hr/> | <hr/> |
| Net increase (decrease) in cash | | |
| and cash equivalents | (347,900) | 184,900 |
| | <hr/> | <hr/> |
| Cash and cash equivalents, | | |
| beginning of year | 1,245,000 | 482,000 |
| | <hr/> | <hr/> |
| Cash and cash equivalents, end of period | \$ 897,100 | \$ 666,900 |
| | ===== | ===== |

Supplemental disclosures:

Cash paid during the period for:

| | | |
|--------------|------------|-----------|
| Income taxes | \$ 186,000 | \$ 18,500 |
| Interest | 1,100 | 4,400 |

See notes to unaudited condensed consolidated financial statements

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

General: The accompanying unaudited interim condensed consolidated financial statements are prepared pursuant to the Securities and Exchange Commission's rules and regulations for reporting on Form 10-Q. Accordingly, certain information and footnotes required by accounting principles generally accepted in the United States for complete financial statements are not included herein. The Company believes all adjustments necessary for a fair presentation of these interim statements have been included and that they are of a normal and recurring nature. These interim statements should be read in conjunction with the Company's financial statements and notes thereto, included in its Annual Report on Form 10-K, for the fiscal year ended June 30, 2016. The results for the three and six months ended December 31, 2016, are not necessarily an indication of the results for the full fiscal year ending June 30, 2017.

1. Summary of significant accounting policies:

Principles of consolidation:

The accompanying consolidated financial statements include the accounts of Scientific Industries, Inc., Scientific Packaging Industries, Inc., an inactive wholly-owned subsidiary, Altamira Instruments, Inc. ("Altamira"), a Delaware corporation and wholly-owned subsidiary, and Scientific Bioprocessing, Inc. ("SBI"), a Delaware corporation and wholly-owned subsidiary, (all collectively referred to as the "Company"). All material intercompany balances and transactions have been eliminated.

2. New Accounting Pronouncements:

In March 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting" (ASU 2016-09). Areas for simplification in this update involve several aspects of accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for interim and annual reporting periods beginning after December 15, 2016, with early application permitted. The Company is currently evaluating the timing, impact and method of applying this guidance on its consolidated financial statements.

In February 2016, the FASB issued authoritative guidance that requires lessees to account for most leases on their balance sheets with the liability being equal to the present value of the lease payments. The right-of-use asset will be based on the lease liability adjusted for certain costs such as direct costs. Lease expense will be recognized similar to current accounting guidance with operating leases resulting in a straight-line expense and financing leases resulting in a front-loaded expense similar to the current accounting for capital leases. This guidance become effective for the Company's fiscal 2020 first quarter, with early adoption permitted.

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This guidance must be adopted using a modified retrospective transition approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements, and provides for certain practical expedients. The Company is currently evaluating the timing, impact and method of applying this guidance on its consolidated financial statements.

In November 2015, the FASB issued new guidance simplifying the balance sheet classification of deferred taxes. The new guidance requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The current requirement that deferred tax liabilities and assets of a tax-paying component of an entity be offset and presented as a single amount is not affected by the new guidance. The guidance is effective for public companies for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted as of the beginning of an interim or annual reporting period. The new guidance may be applied either prospectively to all deferred tax liabilities and assets or retrospectively to all periods presented. The Company does not expect the adoption to have a material impact on its financial condition, results of operations or cash flows.

In July 2015, the FASB issued ASU No. 2015-11, "Inventory: Simplifying the Measurement of Inventory", that requires inventory not measured using either the last in, first out (LIFO) or the retail inventory method to be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable cost of completion, disposal and transportation. The new standard will be effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and will be applied prospectively. Early adoption is permitted. The Company does not expect the adoption to have a material impact on its financial condition, results of operations or cash flows.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers amending revenue recognition requirements for multiple-deliverable revenue arrangements. This update provides guidance on how revenue is recognized to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for the goods or services. This determination is made in five steps: (i) identify the contract with the customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when (or as) the entity satisfies a performance obligation. In July 2015, the FASB deferred the effective date to fiscal years beginning after December 15, 2018 and early adoption of the standard is permitted, but not before the original effective date of December 15, 2017. The Company is evaluating the effect this guidance will have on the consolidated financial statements and related disclosures.

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6

3. Segment Information and Concentrations:

The Company views its operations as three segments: the manufacture and marketing of standard benchtop laboratory equipment for research in university, hospital and industrial laboratories sold primarily through laboratory equipment distributors ("Benchtop Laboratory Equipment"), the manufacture and marketing of custom-made catalyst research instruments for universities, government laboratories, and chemical and petrochemical companies sold on a direct basis ("Catalyst Research Instruments") and the marketing and production of bioprocessing systems for laboratory research in the biotechnology industry sold directly to customers and through distributors ("Bioprocessing Systems").

Segment information is reported as follows (foreign sales are principally to customers in Europe and Asia):

| | Benchtop Laboratory Equipment | Catalyst Research Instruments | Bio- processing Systems | Corporate and Other | Conso- lidated |
|---------------------------------------|-------------------------------------|-------------------------------------|-------------------------------|---------------------------|-------------------|
| Three months ended December 31, 2016: | | | | | |
| Revenues | \$1,466,800 | \$1,192,100 | \$ 24,900 | \$ - | \$2,683,800 |
| Foreign Sales | 751,800 | 10,300 | - | - | 762,100 |
| Income (Loss) from | | | | | |
| Operations | 62,600 | 26,600 | (32,700) | - | 56,500 |
| Assets | 4,131,400 | 1,982,800 | 434,700 | 695,900 | 7,244,800 |
| Long-Lived Asset | | | | | |
| Expenditures | 5,200 | - | 5,800 | - | 11,000 |
| Depreciation and | | | | | |
| Amortization | 76,700 | 4,500 | 12,600 | - | 93,800 |

| | Benchtop Laboratory Equipment | Catalyst Research Instruments | Bio- processing Systems | Corporate and Other | Conso- lidated |
|---------------------------------------|-------------------------------------|-------------------------------------|-------------------------------|---------------------------|-------------------|
| Three months ended December 31, 2015: | | | | | |
| Revenues | \$1,583,500 | \$ 414,500 | \$ 30,200 | \$ - | \$2,028,200 |
| Foreign Sales | 764,400 | 105,500 | - | - | 869,900 |
| Income (Loss) from | | | | | |
| Operations | 187,700 | (10,100) | (32,900) | (14,000) | 130,700 |
| Assets | 4,352,600 | 2,319,200 | 728,800 | 578,300 | 7,978,900 |
| Long-Lived Asset | | | | | |
| Expenditures | 1,900 | - | 5,700 | - | 7,600 |
| Depreciation and | | | | | |
| Amortization | 74,200 | 7,000 | 24,400 | - | 105,600 |

Approximately 55% and 53% of net sales of benchtop laboratory equipment

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(30% and 41% of total revenues) for the three month periods ended December 31, 2016 and 2015, respectively, were derived from the Company's main product, the Vortex-Genie 2(R) mixer, excluding accessories.

7

Approximately 21% and 19% of net sales of benchtop laboratory equipment (11% and 15% of total net revenues) were derived from Torbal brand products for the three months ended December 31, 2016 and 2015, respectively.

Two customers accounted in the aggregate for approximately 17% and 14% of the net sales of the Benchtop Laboratory Equipment Operations (9% and 11% of total net revenues) for the three months ended December 31, 2016 and 2015, respectively. Sales of catalyst research instruments generally comprise a few very large orders averaging at least \$100,000 per order to a limited number of customers, who differ from order to order. Sales to three and two customers (one of which is the same) represented approximately 99% and 92% of the Catalyst Research Instrument Operations' net sales, respectively, and 44% and 19% of total revenues for the three months ended December 31, 2016 and 2015, respectively.

| | Benchtop Laboratory Equipment | Catalyst Research Instruments | Bio- processing Systems | Corporate and Other | Conso- lidated |
|-------------------------------------|-------------------------------------|-------------------------------------|-------------------------------|---------------------------|-------------------|
| Six months ended December 31, 2016: | | | | | |
| Revenues | \$2,923,600 | \$1,269,600 | \$ 49,700 | \$ - | \$4,242,900 |
| Foreign Sales | 1,313,000 | 15,100 | - | - | 1,328,100 |
| Income (Loss) from | | | | | |
| Operations | 164,000 | (115,000) | (67,400) | - | (18,400) |
| Assets | 4,131,400 | 1,982,800 | 434,700 | 695,900 | 7,244,800 |
| Long-Lived Asset | | | | | |
| Expenditures | 13,600 | - | 5,800 | - | 19,400 |
| Depreciation and | | | | | |
| Amortization | 153,400 | 11,100 | 25,000 | - | 189,500 |

| | Benchtop Laboratory Equipment | Catalyst Research Instruments | Bio- processing Systems | Corporate and Other | Conso- lidated |
|-------------------------------------|-------------------------------------|-------------------------------------|-------------------------------|---------------------------|-------------------|
| Six months ended December 31, 2015: | | | | | |
| Revenues | \$2,846,500 | \$ 567,500 | \$ 58,600 | \$ - | \$3,472,600 |
| Foreign Sales | 1,363,400 | 113,300 | - | - | 1,476,700 |
| Income (Loss) from | | | | | |
| Operations | 242,400 | (92,200) | (62,900) | (22,100) | 65,200 |
| Assets | 4,352,600 | 2,319,200 | 728,800 | 578,300 | 7,978,900 |
| Long-Lived Asset | | | | | |
| Expenditures | 8,400 | - | 5,700 | - | 14,100 |
| Depreciation and | | | | | |
| Amortization | 148,000 | 13,900 | 48,900 | - | 210,800 |

Approximately 52% and 50% of net sales of benchtop laboratory equipment (36% and 41% of total revenues) for the six month periods ended December 31, 2016 and 2015, respectively, were derived from the segment's main product, the

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Vortex-Genie 2(R) mixer, excluding accessories.

Two benchtop laboratory equipment customers, accounted in the aggregate for approximately 16% and 13% of the segment's net sales for the six month periods ended December 31, 2016 and 2015, and 11% of total revenues for both periods.

8

Approximately 23% and 20% of net sales of benchtop laboratory equipment (16% of total revenues for both periods) were derived from Torbal brand products for the six months ended December 31, 2016 and 2015, respectively.

For the six month periods ended December 31, 2016 and 2015, catalyst research each of the six month periods, accounted for approximately 97% and 88% of the segment's net sales and 29% and 14% of total revenues, respectively.

4. Fair Value of Financial Instruments:

The FASB defines the fair value of financial instruments as the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements do not include transaction costs.

The accounting guidance also expands the disclosure requirements around fair value and establishes a fair value hierarchy for valuation inputs. The hierarchy prioritizes the inputs into three levels based on the extent to which inputs used in measuring fair value are observable in the market. Each fair value measurement is reported in one of the three levels, which is determined by the lowest level input that is significant to the fair value measurement in its entirety. These levels are described below:

Level 1 Inputs that are based upon unadjusted quoted prices for identical instruments traded in active markets.

Level 2 Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly.

Level 3 Prices or valuation that require inputs that are both significant to the fair value measurement and unobservable.

The following tables set forth by level within the fair value hierarchy the Company's financial assets that were accounted for at fair value on a recurring basis at December 31, 2016 and June 30, 2016 according to the valuation techniques the Company used to determine their fair values:

| | Fair Value Measurements Using Inputs Considered as | | | |
|------------------------------------|---|------------|---------|-------|
| Fair Value at December 31, 2016 | Level 1 | Level 2 | Level 3 | |
| | _____ | _____ | _____ | _____ |
| Assets: | | | | |
| Cash and cash equivalents | \$ 897,100 | \$ 897,100 | \$ - | \$ - |
| Available for sale securities | 290,900 | 290,900 | - | - |

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| | | | | |
|--------------------------|--------------------|--------------------|-------------|-------------|
| Total | <u>\$1,188,000</u> | <u>\$1,188,000</u> | <u>\$ -</u> | <u>\$ -</u> |
| | ===== | ===== | ===== | ===== |
| Liabilities: | | | | |
| Contingent consideration | \$ 228,900 | \$ - | \$ - | \$228,900 |
| | ===== | ===== | ===== | ===== |

9

Fair Value Measurements Using Inputs Considered as

| | Fair Value at June 30, 2016 | Level 1 | Level 2 | Level 3 |
|-------------------------------|--------------------------------|-----------------------------|-----------------------------|-----------------------------|
| | <u> </u> | <u> </u> | <u> </u> | <u> </u> |
| Assets: | | | | |
| Cash and cash equivalents | \$1,245,000 | \$1,245,000 | \$ - | \$ - |
| Available for sale securities | 290,100 | 290,100 | - | - |
| Total | <u>\$1,535,100</u> | <u>\$1,535,100</u> | <u>\$ -</u> | <u>\$ -</u> |
| | ===== | ===== | ===== | ===== |
| Liabilities: | | | | |
| Contingent consideration | \$ 346,300 | \$ - | \$ - | \$346,300 |
| | ===== | ===== | ===== | ===== |

The following table sets forth an analysis of changes during the six months ended December 31, 2016, Level 3 financial liabilities of the Company:

| | |
|-----------------------------------|------------------|
| Beginning balance, June 30, 2016 | \$346,300 |
| Payments | (117,400) |
| Ending Balance, December 31, 2016 | <u>\$228,900</u> |
| | ===== |

Investments in marketable securities classified as available-for-sale by security type at December 31, 2016 and June 30, 2016 consisted of the following:

| | Cost | Fair Value | Unrealized Holding Gain (Loss) |
|-----------------------|-----------------------------|-----------------------------|--------------------------------|
| | <u> </u> | <u> </u> | <u> </u> |
| At December 31, 2016: | | | |
| Available for sale: | | | |
| Equity securities | \$ 36,500 | \$ 48,500 | \$ 12,000 |
| Mutual funds | 260,400 | 242,400 | (18,000) |
| | <u>\$ 296,900</u> | <u>\$ 290,900</u> | <u>\$ (6,000)</u> |
| | ===== | ===== | ===== |
| | | | |
| | Cost | Fair Value | Unrealized Holding Gain (Loss) |

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At June 30, 2016:

| | | | |
|---------------------|-------------------|-------------------|---------------|
| Available for sale: | | | |
| Equity securities | \$ 29,300 | \$ 40,700 | \$ 11,400 |
| Mutual funds | 259,900 | 249,400 | (10,500) |
| | <u>\$ 289,200</u> | <u>\$ 290,100</u> | <u>\$ 900</u> |
| | ===== | ===== | ===== |

5. Inventories:

Inventories for financial statement purposes are based on perpetual inventory records at December 31, 2016 and based on a physical count as of June 30, 2016. Components of inventory are as follows:

| | | |
|-----------------|----------------------|--------------------|
| | December 31, 2016 | June 30, 2016 |
| Raw Materials | \$1,365,900 | \$1,529,800 |
| Work in process | 392,600 | 425,300 |
| Finished Goods | 366,500 | 457,000 |
| | <u>\$2,125,000</u> | <u>\$2,412,100</u> |
| | ===== | ===== |

10

6. Earnings (loss) per common share:

Basic earnings (loss) per common share are computed by dividing net income (loss) by the weighted-average number of shares outstanding. Diluted earnings per common share include the dilutive effect of stock options, if any.

Earnings (loss) per common share was computed as follows:

| | | | | |
|--|--|------------------|---|------------------|
| | For the Three Month Periods Ended December 31, | | For the Six Month Period Ended December 31, | |
| | 2016 | 2015 | 2016 | 2015 |
| Net income (loss) | <u>\$ 45,300</u> | <u>\$ 94,400</u> | <u>(\$ 3,400)</u> | <u>\$ 34,300</u> |
| Weighted average common shares outstanding | 1,489,112 | 1,489,112 | 1,489,112 | 1,489,112 |
| Dilutive securities | - | - | - | - |
| Weighted average dilutive common shares outstanding | <u>1,489,112</u> | <u>1,489,112</u> | <u>1,489,112</u> | <u>1,489,112</u> |
| Basic and diluted earnings (loss) per common share | <u>\$.03</u> | <u>\$.06</u> | <u>(\$.00)</u> | <u>\$.02</u> |
| | ===== | ===== | ===== | ===== |

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Approximately 43,500 and 38,500 shares of the Company's Common Stock issuable upon the exercise of outstanding stock options were excluded from the calculation of diluted earnings per common share for the three and six month periods ended December 31, 2016 and 2015, respectively, because the effect would be anti-dilutive.

7. Goodwill and Other Intangible Assets:

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired in connection with the Company's acquisitions. Goodwill amounted to \$705,300 as of December 31, 2016 and June 30, 2016, all of which is expected to be deductible for tax purposes.

The components of other intangible assets are as follows:

| | Useful Lives | Cost | Accumulated Amortization | Net |
|---|-----------------|--------------------|-----------------------------|-------------------|
| At December 31, 2016: | | | | |
| Technology, trademarks | 5/10 yrs. | \$ 722,800 | \$ 510,900 | \$ 211,900 |
| Trade names | 6 yrs. | 140,000 | 66,100 | 73,900 |
| Websites | 5 yrs. | 210,000 | 119,000 | 91,000 |
| Customer relationships | 9/10 yrs. | 357,000 | 274,800 | 82,200 |
| Sublicense agreements | 10 yrs. | 294,000 | 150,700 | 143,300 |
| Non-compete agreements | 5 yrs. | 384,000 | 267,300 | 116,700 |
| Intellectual Property, Research & Development (IPR&D) | 3 yrs. | 110,000 | 103,900 | 6,100 |
| Other intangible assets | 5 yrs. | 192,700 | 159,500 | 33,200 |
| | | <u>\$2,410,500</u> | <u>\$1,652,200</u> | <u>\$ 758,300</u> |
| | | ===== | ===== | ===== |

11

| | Useful Lives | Cost | Accumulated Amortization | Net |
|---|-----------------|--------------------|-----------------------------|-------------------|
| At June 30, 2016: | | | | |
| Technology, trademarks | 5/10 yrs. | \$ 722,800 | \$ 468,800 | \$ 254,000 |
| Trade names | 6 yrs. | 140,000 | 54,400 | 85,600 |
| Websites | 5 yrs. | 210,000 | 98,000 | 112,000 |
| Customer relationships | 9/10 yrs. | 357,000 | 261,600 | 95,400 |
| Sublicense agreements | 10 yrs. | 294,000 | 136,000 | 158,000 |
| Non-compete agreements | 5 yrs. | 384,000 | 239,100 | 144,900 |
| Intellectual Property, Research & Development (IPR&D) | 3 yrs. | 110,000 | 85,500 | 24,500 |
| Other intangible assets | 5 yrs. | 177,900 | 154,700 | 23,200 |
| | | <u>\$2,395,700</u> | <u>\$1,498,100</u> | <u>\$ 897,600</u> |
| | | ===== | ===== | ===== |

Total amortization expense was \$76,200 and \$87,500 for the three months ended December 31, 2016 and 2015, respectively and \$154,100 and \$173,800 for the six months ended December 31, 2016 and 2015, respectively. As of

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December 31, 2016, estimated future amortization expense related to intangible assets is \$143,300 for the remainder of the fiscal year ending June 30, 2017, \$288,500 for fiscal 2018, \$210,600 for fiscal 2019, \$45,100 for fiscal 2020, \$43,500 for fiscal 2021 and \$27,300 thereafter.

12

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES

Item 2. Management's Discussion and Analysis or Plan of Operations

Certain statements contained in this report are not based on historical facts, but are forward-looking statements that are based upon various assumptions about future conditions. Actual events in the future could differ materially from those described in the forward-looking information. Numerous unknown factors and future events could cause such differences, including but not limited to, product demand, market acceptance, impact of competition, the ability to reach final agreements, the ability to finance and produce to customers' specifications catalyst research instruments, and to develop marketable bioprocessing systems, adverse economic conditions, and other factors affecting the Company's business that are beyond the Company's control. Consequently, no forward-looking statement can be guaranteed.

We undertake no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise.

Liquidity and Capital Resources

Cash and cash equivalents decreased by \$347,900 to \$897,100 as of December 31, 2016 from \$1,245,000 as of June 30, 2016.

Net cash used in operating activities was \$450,300 for the six months ended December 31, 2016 compared to \$167,400 used during the six months ended December 31, 2015. The current year period reflected a loss as compared to income in the prior year period, higher accounts receivable balances, increased prepayments to vendors, and lower accounts payable and decreased accrued expense items, partially offset by lower inventories. Cash used in investing activities was \$27,000 for the six months ended December 31, 2016 compared to \$16,800 for the six months ended December 31, 2015 primarily due to fixed asset and intangibles purchases. Cash provided by financing activities was \$129,300 for the six months ended December 31, 2016 compared to \$184,900 for the six months ended December 31, 2015 primarily due to lower amounts of line of credit proceeds and higher contingent consideration payments.

The Company's working capital decreased by \$91,400 to \$3,940,500 at December 31, 2016 from \$4,031,900 at June 30, 2016.

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The Company has two lines of credit through June 2017 with First National Bank of Pennsylvania - an Export-Related Revolving Line of Credit which is guaranteed by the Export-Import Bank of the United States which provides for export-related borrowings of up to \$200,000, bearing interest at prime plus 1% and an annual fee of 1.75% and a second one-year Demand Line of Credit which provides for borrowings of up to \$300,000 for regular working capital needs, bearing interest at prime, currently 3.75%. Advances on both lines are secured by a pledge of the Company's assets including inventory, accounts, chattel paper, equipment and general intangibles of the Company. As of December 31, 2016 the Company had \$250,000 outstanding which was paid in January 2017.

Management believes that the Company will be able to meet its cash flow needs during the next 12 months from its available financial resources which include its cash and investment securities, lines of credit, and operations.

13

Results of Operations

Financial Overview

The Company recorded income before income tax expense of \$64,800 and \$123,100 for the three month periods ended December 31, 2016 and 2015, respectively; and loss before income tax benefit of \$4,700 and income before income tax expense of \$45,200 for the six month periods ended December 31, 2016 and 2015, respectively primarily due to lower gross profit amounts generated by the Benchtop Laboratory Equipment Operations and higher operating expenses. The results reflect non-cash amounts for depreciation and amortization of \$93,800 and \$189,500 for the three and six months ended December 31, 2015 compared to \$105,600 and \$210,800 respectively.

The Three Months Ended December 31, 2016 Compared With the Three Months Ended December 31, 2015

Net revenues for the three months ended December 31, 2016 increased by \$655,600 (32.3%) to \$2,683,800 from \$2,028,200 for the three months ended December 31, 2015, primarily as a result of a \$777,600 increase in sales of catalyst research instruments, partially offset by decreases of \$116,700 and \$5,300 in sales and revenues of benchtop laboratory equipment and bioprocessing products. Sales of the benchtop laboratory equipment products generally are pursuant to many small purchase orders from distributors, while catalyst research instruments are sold pursuant to a small number of larger orders, typically averaging over \$100,000 each, resulting in significant swings in revenues. The backlog of orders for catalyst research instruments was \$397,300 at December 31, 2016 compared to \$3,102,000 as of December 31, 2015, the majority of which are anticipated to be delivered by June 30, 2017.

The gross profit percentage for the three months ended December 31, 2016 decreased to 29.6% compared to 41.3% for the year earlier three month period primarily due to lower gross profit margins by the Catalyst Research Instrument Operations due to sales mix.

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General and administrative expenses for the three month comparative periods ended December 31, 2016 and December 31, 2015 increased by \$13,500 (3.4%) to \$409,200 from \$395,700 primarily due to various expenses incurred by the Benchtop Laboratory Equipment Operations.

Selling expenses for the three months ended December 31, 2016 amounted to \$224,200 compared to \$227,200 for the three months ended December 31, 2015.

Research and development expenses for the three months ended December 31, 2016 increased \$20,900 (24.9%) to \$105,000 from \$84,100 for the three months ended December 31, 2015, primarily the result of increased new product development by the Company's Benchtop Laboratory Equipment Operations and the Bioprocessing Systems Operations.

Total other income (expense), net for the three month period ended December 31, 2016 increased by \$15,900 to \$8,300 from (\$7,600) for the three month period ended December 31, 2015 due to decreased interest expense as a result of less borrowings.

14

For the three months ended December 31, 2016, income tax expense was \$19,500 compared to \$28,700 for the three months ended December 31, 2015 due to the decreased income for the period.

As a result, the net income for the three months ended December 31, 2016 was \$45,300 compared to \$94,400 for the three months ended December 31, 2015.

The Six Months Ended December 31, 2016 Compared With the Six Months Ended December 31, 2015

Net revenues for the six months ended December 31, 2016 increased by \$770,300 (22.2%) to \$4,242,900 compared to \$3,472,600 for the six months ended December 31, 2015, primarily due to increases of \$702,100 and \$77,100 in sales of catalyst research instruments and benchtop laboratory equipment, respectively, partially offset by a \$8,900 decrease in revenues of the Bioprocessing Systems Operations. Sales of benchtop laboratory equipment products generally are comprised of many small purchase orders from distributors, while sales of catalyst research instruments are comprised of a small number of large orders, typically averaging over \$100,000 each, resulting in significant swings in revenues.

The gross profit percentage for the six months ended December 31, 2016 decreased to 34.5% compared to 41.3% for the six months ended December 31, 2015, primarily due to lower gross profit margins by the Catalyst Research Instrument Operations due to sales mix.

General and administrative expenses increased by \$17,700 (2.2%) to \$821,600 for the six months ended December 31, 2016 from \$803,900 for the comparable period of the prior year, primarily due to various expenses incurred by the Benchtop Laboratory Equipment Operations.

Selling expenses for the six months ended December 31, 2016 increased by \$46,700 (11.8%) to \$440,900 from \$394,200 for the six months ended December 31, 2015, primarily due to online advertising for the Benchtop Laboratory

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Equipment Operations.

Research and development expenses for the six months ended December 31, 2016 increased by \$50,900 (30.0%) to \$220,400 compared to \$169,500 for the six months ended December 31, 2015, primarily the result of increased new product development by the Company's Benchtop Laboratory Equipment Operations and the Bioprocessing Systems Operations.

Total other income (expense), net, for the six month period ended December 31, 2016 increased to \$13,700 from (\$20,000) for the six months ended December 31, 2015 primarily due to decreased interest expense and miscellaneous income items.

For the six month period ended December 31, 2016 the income tax benefit was \$1,300 compared to income tax expense of \$10,900 for the comparable period of the prior fiscal year due to the loss during the current year period compared to income in the prior year.

As a result, the net loss for the six months ended December 31, 2016 was \$3,400 compared to net income of \$34,300 for the six months ended December 31, 2015.

15

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this report, based on an evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934), the Chief Executive and Chief Financial Officer of the Company has concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in its Exchange Act reports is recorded, processed, summarized and reported within the applicable time periods specified by the SEC's rules and forms. The Company also concluded that information required to be disclosed in such reports is accumulated and communicated to the Company's management, including its principal executive and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting. There was no change in the Company's internal controls over financial reporting that occurred during the most recently completed fiscal quarter that materially affected or is reasonably likely to materially affect the Company's internal controls over financial reporting.

Part II - OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

| (a) Exhibit Number: | Description |
|---------------------|-------------|
|---------------------|-------------|

| | |
|------|---|
| 31.1 | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
|------|---|

| | |
|------|--|
| 32.1 | Certification of Chief Executive Officer and Chief Financial |
|------|--|

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Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K:

Report dated November 15, 2016 reporting under Item 8.01.

Report dated January 15, 2017 reporting under Item 8.01.

16

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES

SIGNATURE

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Scientific Industries, Inc.
Registrant

/s/ Helena R. Santos

Helena R. Santos
President, Chief Executive Officer
and Treasurer
Principal Executive, Financial and
Accounting Officer

Date: February 10, 2017

