

SCIENTIFIC INDUSTRIES INC

Form 10-Q

May 15, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018

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

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

Commission file number 0-6658

SCIENTIFIC INDUSTRIES, INC.

(Exact Name of Registrant in Its Charter)

Delaware

(State or other jurisdiction of incorporation or organization)

04-2217279

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

80 Orville Drive, Suite 102, Bohemia, New York

(Address of principal executive offices)

11716

(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 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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes

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

Large accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company)

Accelerated filer

Smaller reporting company

Emerging Growth

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

The number of shares outstanding of the registrant’s common stock, par value \$.05 per share (“Common Stock”) as of May 1, 2018 is 1,494,112 shares.



SCIENTIFIC INDUSTRIES, INC.

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

## ASSETS

	March 31, 2018	June 30, 2017
Current assets:	(Unaudited)	
Cash and cash equivalents	\$678,600	\$1,025,100
Investment securities	309,100	295,500
Trade accounts receivable, less allowance for doubtful accounts of \$11,600 at March 31, 2018 and June 30, 2017	1,406,700	1,179,000
Inventories	2,701,600	1,961,200
Prepaid expenses and other current assets	92,300	80,300
Total current assets	5,188,300	4,541,100
Property and equipment, net	223,100	199,300
Intangible assets, net	399,200	579,000
Goodwill	705,300	705,300
Trade accounts receivable, less current portion	245,400	245,400
Other assets	52,500	52,500
Deferred taxes	544,500	505,100
Total assets	\$7,358,300	\$6,827,700

## LIABILITIES AND SHAREHOLDERS' EQUITY

## Current liabilities:

Accounts payable	\$394,400	\$139,200
Accrued expenses, current portion	398,200	491,000
Bank line of credit	40,000	-
Customer advances	356,000	-
Contingent consideration, current portion	215,000	175,700
Notes payable, current portion	6,900	6,700
Total current liabilities	1,410,500	812,600
Accrued expenses, less current portion	60,000	60,000
Notes payable, less current portion	600	5,800
Contingent consideration payable, less current portion	385,000	121,300

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Total liabilities	1,856,100	999,700
Shareholders' equity:		
Common stock, \$.05 par value; authorized 7,000,000 shares; issued 1,513,914 shares outstanding at March 31, 2018 and June 30, 2017	75,700	75,700
Additional paid-in capital	2,542,500	2,515,900
Accumulated other comprehensive loss	(4,400)	(3,500)
Retained earnings	2,940,800	3,292,300
	5,554,600	5,880,400
Less common stock held in treasury at cost, 19,802 shares	52,400	52,400
Total shareholders' equity	5,502,200	5,828,000
Total liabilities and shareholders' equity	\$7,358,300	\$6,827,700

See notes to unaudited condensed consolidated financial statements



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

	For the Three Month Period Ended March 31,	For the Three Month Period Ended March 31,	For the Nine Month Period Ended March 31,	For the Nine Month Period Ended March 31,
	2018	2017	2018	2017
Revenues	\$2,099,300	\$1,910,900	\$5,272,600	\$6,153,800
Cost of revenues	1,331,500	1,054,800	3,287,300	3,833,200
Gross profit	767,800	856,100	1,985,300	2,320,600
Operating expenses:				
General and administrative	470,200	435,100	1,306,600	1,256,700
Selling	263,800	223,900	679,500	664,800
Research and development	117,700	114,100	379,700	334,500
Total operating expenses	851,700	773,100	2,365,800	2,256,000
Income (loss) from operations	(83,900)	83,000	(380,500)	64,600
Other income (expense):				
Interest income	-	1,100	5,600	10,100
Other income, net	500	-	1,900	5,700
Interest expense	(500)	(1,200)	(1,100)	(2,200)
Total other income (expense), net	-	(100)	6,400	13,600
Income (loss) before income tax expense (benefit)	(83,900)	82,900	(374,100)	78,200
Income tax expense (benefit):				
Current	9,700	38,900	17,800	23,400
Deferred	(55,900)	(21,600)	(40,400)	(7,400)
Total income tax expense (benefit)	(46,200)	17,300	(22,600)	16,000
Net income (loss)	\$(37,700)	\$65,600	\$(351,500)	\$62,200

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Basic earnings (loss) per common share	\$(.03)	\$.04	\$(.24)	\$.04
Diluted earnings (loss) per common share	\$(.03)	\$.04	\$(.24)	\$.04
Cash dividends declared per common share	\$-	\$.03	\$-	\$.03

See notes to unaudited condensed consolidated financial statements.



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

	For the Three Month Period Ended March 31,	For the Three Month Period Ended March 31	For the Nine Month Period Ended March 31,	For the Nine Month Period Ended March 31,
	2018	2017	2018	2017
Net income (loss)	\$(37,700)	\$65,600	\$(351,500)	\$62,200
Other comprehensive income (loss):				
Unrealized holding gain (loss) arising during period net of tax	(5,100)	1,300	(900)	(5,600)
Comprehensive income (loss)	\$(42,800)	\$66,900	\$(352,400)	\$56,600

See notes to unaudited condensed consolidated financial statements.



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

	For the Nine Month Period Ended March 31,	For the Nine Month Period Ended March 31,
	2018	2017
Operating activities:		
Net income (loss)	\$(351,500)	\$62,200
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Gain on sale of investment	-	(3,200)
Depreciation and amortization	230,100	276,500
Deferred income tax expense	(39,400)	(7,400)
Income tax benefit of stock options exercised	8,000	-
Stock-based compensation	18,600	1,300
Change in fair value of contingent consideration	445,700	-
Changes in operating assets and liabilities:		
Trade accounts receivable	(227,700)	149,600
Inventories	(740,400)	206,200
Prepaid expenses and other current assets	(12,000)	(25,900)
Accounts payable	255,200	700
Long term accounts receivable	-	(245,400)
Customer advances	356,000	107,900
Accrued expenses	(92,800)	(317,700)
Total adjustments	201,300	142,600
Net cash provided by (used in) operating activities	(150,200)	204,800
Investing activities:		
Redemption of investment securities, available-for-sale	-	11,100
Purchase of investment securities, available -for -sale	(14,500)	(18,700)
Capital expenditures	(70,500)	(18,200)
Purchase of intangible assets	(3,600)	(12,800)
Net cash used in investing activities	(88,600)	(38,600)
Financing activities:		
Line of credit proceeds	40,000	250,000
Line of credit repayments	-	(250,000)
Payments for contingent consideration	(142,700)	(166,100)

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Cash dividend declared and paid	-	(44,500)
Proceeds from exercise of stock options	-	15,500
Principal payments on notes payable	(5,000)	(4,800)
Net cash used in financing activities	(107,700)	(199,900)
Net decrease in cash and cash equivalents	(346,500)	(33,700)
Cash and cash equivalents, beginning of year	1,025,100	1,245,000
Cash and cash equivalents, end of period	\$678,600	\$1,211,300
Cash paid during the period for:		
Income taxes	\$16,000	\$213,500
Interest	1,100	2,200

See notes to unaudited condensed consolidated financial statements



SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARIES  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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, 2017. The results for the three months and nine months ended March 31, 2018, are not necessarily an indication of the results for the full fiscal year ending June 30, 2018.

## 1. Summary of Significant Accounting Policies

### Principles of Consolidation

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

### Recent Accounting Pronouncements

In January 2016, the Financial Accounting Standards Board ("FASB") issued ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities". The update addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. For public business entities, the amendments in this update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. Early adoption is permitted only for certain portions of the ASU related to financial liabilities. The Company is currently evaluating the impact of the provisions of this new standard on the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842). The FASB issued this update to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The updated guidance is effective for annual periods beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption of the update is permitted. The Company is currently evaluating the effect of the new standard.

In April 2016, the FASB issued ASU No. 2016-10, "Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing (Topic 606)". In March 2016, the FASB issued ASU No. 2016-08, "Revenue from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net) (Topic 606)". These amendments provide additional clarification and implementation guidance on the previously issued ASU 2014-09, "Revenue from Contracts with Customers". The amendments in ASU 2016-10 provide clarifying guidance on materiality of performance obligations; evaluating distinct performance obligations; treatment of shipping and handling costs; and determining whether an entity's promise to grant a license provides a customer with either a right to use an entity's intellectual property or a right to access an entity's intellectual property. The amendments in ASU

2016-08 clarify how an entity should identify the specified good or service for the principal versus agent evaluation and how it should apply the control principle to certain types of arrangements. The adoption of ASU 2016-10 and ASU 2016-08 is to coincide with an entity's adoption of ASU 2014-09. The Company has performed a review of the requirements of the new guidance and has identified which of its revenue streams will be within the scope of ASC 606. The Company has applied the five-step model of the new standard to a selection of contracts within each of its revenue streams and has compared the results to its current accounting practices. Based on this analysis, the Company does not currently expect a material impact on the Company's consolidated financial statements. The Company is expecting to utilize the modified retrospective transition method of adoption. The Company is continuing to work through the remaining steps of the adoption plan to facilitate adoption effective July 1, 2018. As part of this, the Company is assessing changes that might be necessary to information technology systems, processes, and internal controls to capture new data and address changes in financial reporting. The Company will be revising its revenue recognition accounting policy and expanding revenue disclosures to reflect the requirements of ASC 606, which include disclosures related to the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Additionally, qualitative and quantitative disclosures are required about customer contracts, significant judgements and assets recognized from the costs to obtain or fulfill a contract.

In May 2016, the FASB issued ASU No. 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients", which narrowly amended the revenue recognition guidance regarding collectability, noncash consideration, presentation of sales tax and transition and is effective during the same period as ASU 2014-09. The Company is currently evaluating the effect of the standard.

In August 2016, the FASB issued ASU 2016-15, "Classification of Certain Cash Receipts and Cash Payments". This update provides guidance on how to record eight specific cash flow issues. This update is effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted and a retrospective transition method to each period should be presented. The Company is currently evaluating the effect of this update on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, "Statement of Cash Flows (Topic 230)", requiring that the statement of cash flows explain the change in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. This guidance is effective for fiscal years, and interim reporting periods therein, beginning after December 15, 2017 with early adoption permitted. The provisions of this guidance are to be applied using a retrospective approach which requires application of the guidance for all periods presented. The adoption of this ASU had no impact on the Company's Condensed Consolidated Statements of Cash Flows.



### Adopted Accounting Pronouncements

In November 2015, the FASB issued ASU No. 2015-17, "Income Taxes: Balance Sheet Classification of Deferred Taxes" ("ASU 2015-17") which was effective for fiscal years beginning December 15, 2016 (fiscal 2018 for the Company). ASU 2015-17 required that deferred tax assets and liabilities be net and classified as noncurrent on the balance sheet rather than presenting deferred taxes into current and noncurrent amounts. The Company adopted ASU 2015-07 effective for the first fiscal quarter of the year ending June 30, 2018. The Company applied the new guidance on a retrospective basis, resulting in a reclassification of current deferred tax assets totaling \$129,000 against long term deferred tax assets in the Company's Condensed Consolidated Balance Sheet as of June 30, 2017. The adoption of this ASU had no impact on the Company's Condensed Consolidated Statement of Operations.

On December 22, 2017, the Staff of the Securities and Exchange Commission issued Staff Accounting Bulletin No. 118, "Income Tax Accounting Implications of the Tax Cuts and Jobs Act, or SAB 118," which addresses situations where the accounting under the FASB, Accounting Standards Codification No. 740, Income Taxes, or ASC 740 is incomplete for certain income tax effects of Public Law No. 115-97, commonly referred to as the Tax Cuts and Jobs Act, or the 2017 Tax Act, by the time an entity issues its financial statements for the fiscal period that includes the date the 2017 Tax Act was enacted.

Under ASC 740, entities are required to adjust current and deferred tax assets and liabilities for the effects of changes in tax laws or rates at their date of enactment. However, pursuant to SAB 118, if an entity does not have the necessary information available, prepared, or analyzed for certain income tax effects of the 2017 Tax Act at the time an entity's financial statements are issued, an entity shall apply ASC 740 based on the provisions of the tax laws that were in effect immediately prior to the enactment of the 2017 Tax Act. If the accounting for certain income tax effects of the 2017 Tax Act is incomplete, but an entity can determine a reasonable estimate for those effects, an entity can record provisional amounts during a measurement period, which ends on the earlier of when an entity has obtained, prepared, and analyzed the information necessary to complete the accounting requirements of ASC 740 and December 22, 2017.

The 2017 Tax Act includes significant changes to the U.S. income tax system. The 2017 Tax Act contains numerous provisions impacting the Company, the most significant of which reduces the Federal corporate statutory rate from 35% to 21%. The Company is a fiscal-year end taxpayer and is required to use a blended statutory federal tax rate, inclusive of the Federal rate change enacted on December 22, 2017 to compute its effective rate for the three and six months ended December 31, 2017. The various provisions under the 2017 Tax Act most relevant to the Company have been considered in the preparation of the financial statements as of March 31, 2018. However, the Company had not completed its accounting for the tax effects of the enactment of 2017 Tax act. The Company's provision for income taxes for the three and nine months ended March 31, 2018 is based on reasonable estimates of the effects of its implementation and existing deferred tax balances. The Company estimates it will record a one-time non-cash charge of approximately \$30,000 for the fiscal year ended June 30, 2018 due to an estimated reduction in deferred tax assets as a result of the reduction in the Federal tax rate. We expect to complete our accounting during the one year measurement period from the enactment date.

### Reclassification

Accounts receivable of \$245,400 was reclassified from current to long-term assets on the balance sheet as of June 30, 2017 to conform to the current period's presentation.



## 2. 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 and laboratory and pharmacy balances and scales (“Benchtop Laboratory Equipment Operations”), 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 Operations”) and the design and marketing of bioprocessing systems and products and related royalty income (“Bioprocessing Systems”).

Segment information is reported as follows:

	Benchtop Laboratory Equipment	Catalyst Research Instruments	Bioprocessing Systems	Corporate And Other	Consolidated
Three Months Ended March 31, 2018:					
Revenues	\$1,550,700	\$110,700	\$437,900	\$-	\$2,099,300
Foreign Sales	620,200	105,400	-	-	725,600
Income (Loss) From Operations	78,200	(74,400)	(87,700)	-	(83,900)
Assets	3,930,600	1,680,800	893,300	853,600	7,358,300
Long-Lived Asset Expenditures	4,500	-	-	-	4,500
Depreciation and Amortization	67,400	(800)	9,400	-	76,000

	Benchtop Laboratory Equipment	Catalyst Research Instruments	Bioprocessing Systems	Corporate And Other	Consolidated
Three Months Ended March 31, 2017:					
Revenues	\$1,410,800	\$359,800	\$140,300	\$-	\$1,910,900

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Foreign Sales	611,400	37,100	-	-	648,500
Income (Loss) From Operations	88,900	(82,400)	76,500	-	83,000
Assets	4,170,900	1,822,200	485,700	719,200	7,198,000
Long-Lived Asset Expenditures	4,600	-	7,000	-	11,600
Depreciation and Amortization	73,500	1,600	12,000	-	87,100

Approximately 53% and 54% of net benchtop laboratory equipment sales (39% and 40% of total revenues) for the three month periods ended March 31, 2018 and 2017, respectively, were derived from the Company's main product, the Vortex-Genie 2 mixer, excluding accessories.

Approximately 21% of total benchtop laboratory equipment sales (16% of total revenues) were derived from the Torbal Scales Division for both the three months ended March 31, 2018 and 2017, respectively.

For the three months ended March 31, 2018 and 2017, respectively, two customers accounted in the aggregate for approximately 17% and 15% of net sales of the Benchtop Laboratory Equipment Operations (13% and 11% of the Company's total revenues).

Sales of catalyst research instruments generally comprise a few very large orders averaging approximately \$50,000 per order to a limited number of customers, who differ from order to order. Sales to two and two different customers during the three months ended March 31, 2018 and 2017, accounted for approximately 89% and 76% of the Catalyst Research Instrument Operations' revenues and 5% and 14% of the Company's total revenues, respectively.



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	Benchtop Laboratory Equipment	Catalyst Research Instruments	Bioprocessing Systems	Corporate And Other	Consolidated
Nine Months Ended March 31, 2018:					
Revenues	\$4,436,300	\$293,000	\$543,300	\$-	\$5,272,600
Foreign Sales	1,937,800	114,400	-	-	2,052,200
Income (Loss) From Operations	106,300	(361,900)	(124,900)	-	(380,500)
Assets	3,930,600	1,680,800	893,300	853,600	7,358,300
Long-Lived Asset Expenditures	69,700	1,900	2,500	-	74,100
Depreciation and Amortization	199,300	2,700	28,100	-	230,100

	Benchtop Laboratory Equipment	Catalyst Research Instruments	Bioprocessing Systems	Corporate And Other	Consolidated
Nine Months Ended March 31, 2017:					
Revenues	\$4,334,400	\$1,629,400	\$190,000	\$-	\$6,153,800
Foreign Sales	1,924,400	52,200	-	-	1,976,600
Income (Loss) From Operations	252,900	(197,400)	9,100	-	64,600
Assets	4,170,900	1,822,200	485,700	719,200	7,198,000
Long-Lived Asset Expenditures	18,200	-	12,800	-	31,000
Depreciation and	226,900	12,600	37,000	-	276,500

## Amortization

Approximately 51% and 53% of net benchtop laboratory equipment sales (43% and 37% of total revenues) for the nine month periods ended March 31, 2018 and 2017, respectively, were derived from the Company's main product, the Vortex-Genie 2 mixer, excluding accessories.

Approximately 22% and 23% of total benchtop laboratory equipment sales (19% and 16% of total revenues) were derived from the Torbal Scales Division for the nine months ended March 31, 2018 and 2017, respectively. For the nine months ended March 31, 2018 and 2017, respectively, two customers accounted in the aggregate for approximately 16% of net sales of the Benchtop Laboratory Equipment Operations (14% and 11% of the Company's total revenues).

Sales of catalyst research instruments generally comprise a few very large orders averaging approximately \$50,000 per order to a limited number of customers, who differ from order to order. Sales to three and four customers during the nine months ended March 31, 2018 and 2017, accounted for approximately 79% and 92% of the Catalyst Research Instrument Operations' revenues and 4% and 24% of the Company's total revenues, respectively.

### 3. 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.



In valuing assets and liabilities, the Company is required to maximize the use of quoted market prices and minimize the use of unobservable inputs. The Company calculated the fair value of its Level 1 and 2 instruments based on the exchange traded price of similar or identical instruments where available or based on other observable instruments. These calculations take into consideration the credit risk of both the Company and its counterparties. The Company has not changed its valuation techniques in measuring the fair value of any financial assets and liabilities during the period.

The fair value of the contingent consideration obligations are based on a probability weighted approach derived from the estimates of earn-out criteria and the probability assessment with respect to the likelihood of achieving those criteria. The measurement is based on significant inputs that are not observable in the market, therefore, the Company classifies this liability as Level 3 in the following tables.

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 March 31, 2018 and June 30, 2017 according to the valuation techniques the Company used to determine their fair values:

Fair Value Measurements Using  
Inputs Considered as

Fair Value at March 31, 2018    Level 1    Level 2    Level 3

Assets:

Cash and cash equivalents	\$678,600	\$678,600	\$-	\$-
Available-for- sale securities	309,100	309,100	-	-
<b>Total</b>	<b>\$987,700</b>	<b>\$987,700</b>	<b>\$-</b>	<b>\$-</b>

Liabilities:

Contingent consideration	\$600,000	\$-	\$-	\$600,000
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Fair Value Measurements Using  
Inputs Considered as

Fair Value at June 30, 2017    Level 1    Level 2    Level 3

Assets:

Cash and cash equivalents	\$1,025,100	\$1,025,100	\$-	\$-
Available-for-sale securities	295,500	295,500	-	-
Total	\$1,320,600	\$1,320,600	\$-	\$-

Liabilities:

Contingent consideration	\$297,000	\$-	\$-	\$297,000
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The following table sets forth an analysis of changes during the nine months ended March 31, 2018 and 2017 in Level 3 financial liabilities of the Company:

	2018	2017
Beginning balance	\$297,000	\$346,300
Increase in contingent consideration liability	445,700	-
Payments	(142,700)	(166,100)
Ending balance	\$600,000	\$180,200



Investments in marketable securities classified as available-for-sale by security type at March 31, 2018 and June 30, 2017 consisted of the following:

	Cost	Fair Value	Unrealized Holding Gain (Loss)
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At March 31, 2018:

Available-for-sale:

Equity securities	\$45,700	\$63,300	\$17,600
Mutual funds	267,800	245,800	(22,000)
	\$313,500	\$309,100	\$(4,400)

	Cost	Fair Value	Unrealized Holding Gain (Loss)
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At June 30, 2017:

Available-for-sale:

Equity securities	\$37,000	\$50,800	\$13,800
Mutual funds	262,000	244,700	(17,300)
	\$299,000	\$295,500	\$(3,500)

#### 4. Inventories

Inventories are valued at the lower of cost (determined on a first-in, first-out basis) or net realizable value, and have been reduced by an allowance for excess and obsolete inventories. The estimate is based on managements review of inventories on hand compared to estimated future usage and sales. Cost of work-in-process and finished goods inventories include material, labor, and manufacturing overhead.

	March 31, 2018	June 30, 2017
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Raw materials	\$1,525,400	\$1,373,800
Work-in-process	831,000	166,500
Finished goods	345,200	420,900

\$2,701,600

\$1,961,200

## 5. 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 at March 31, 2018 and June 30, 2017, 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 March 31, 2018:				
Technology, trademarks	5/10 yrs.	\$662,800	\$595,300	\$67,500
Trade names	6 yrs.	140,000	95,300	44,700
Websites	5 yrs.	210,000	171,500	38,500
Customer relationships	9/10 yrs.	357,000	291,400	65,600
Sublicense agreements	10 yrs.	294,000	187,400	106,600
Non-compete agreements	5 yrs.	384,000	334,500	49,500
IPR&D	3 yrs.	110,000	110,000	-
Other intangible assets	5 yrs.	198,000	171,200	26,800
		\$2,355,800	\$1,956,600	\$399,200



	Useful Lives	Cost	Accumulated Amortization	Net
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At June 30, 2017:

Technology, trademarks	5/10 yrs.	\$662,800	\$541,100	\$121,700
Trade names	6 yrs.	140,000	77,800	62,200
Websites	5 yrs.	210,000	140,000	70,000
Customer relationships	9/10 yrs.	357,000	281,400	75,600
Sublicense agreements	10 yrs.	294,000	165,400	128,600
Non-compete agreements	5 yrs.	384,000	294,000	90,000
IPR&D	3 yrs.	110,000	110,000	-
Other intangible assets	5 yrs.	194,500	163,600	30,900
		\$2,352,300	\$1,773,300	\$579,000

Total amortization expense was \$61,200 and \$69,900 for the three months ended March 31, 2018 and 2017, respectively and \$183,400 and \$224,000 for the nine months ended March 31, 2018 and 2017, respectively. As of March 31, 2018, estimated future amortization expense related to intangible assets is \$60,200 for the remainder of the fiscal year ending June 30, 2018, \$185,800 for fiscal 2019, \$65,400 for fiscal 2020, \$48,000 for fiscal 2021, \$27,000 for fiscal 2022, and \$12,800 thereafter.

#### 6. Earnings (Loss) Per Common Share

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

	For the Three Month Period Ended March 31, 2018	For the Three Month Period Ended March 31, 2017	For the Nine Month Period Ended March 31, 2018	For the Nine Month Period Ended March 31, 2017
Net income (loss)	\$(37,700)	\$65,600	\$(351,500)	\$62,200
Weighted average common shares outstanding	1,494,112	1,492,334	1,494,112	1,490,189
Effect of dilutive securities	-	38	-	1,309
Weighted average dilutive common shares outstanding	1,494,112	1,492,372	1,494,112	1,491,498

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Basic earnings (loss) per common share	\$(.03)	\$.04	\$(.24)	\$.04
Diluted earnings (loss) per common share	\$(.03)	\$.04	\$(.24)	\$.04

Approximately 82,000 and 33,500 shares of the Company's common stock issuable upon the exercise of outstanding options were excluded from the calculation of diluted earnings per common share for the three and nine month periods ended March 31, 2018 and 2017, respectively, because the effect would be anti-dilutive.



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

**Forward-Looking statements.** 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, success of marketing strategy, success of expansion efforts, impact of competition, adverse economic conditions, and other factors affecting the Company's business that are beyond the Company's control, which are discussed elsewhere in this report. Consequently, no forward-looking statement can be guaranteed. The Company undertakes no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise. This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the Company's financial statements and the related notes included elsewhere in this report.

**Overview.** The Company reflected a loss before income tax benefit of \$83,900 for the three months ended March 31, 2018 compared to income before tax expense of \$82,900 for the three months ended March 31, 2017, primarily due to increase in contingent consideration liability resulting from increased royalty revenues for the Bioprocessing Systems Operations. The Company reflected a loss before income tax benefit of \$374,100 for the nine months ended March 31, 2018 compared to income before income tax expense of \$78,200 for the nine months ended March 31, 2017 mainly due to the increase in contingent consideration liability for the Bioprocessing Systems Operations and reduced income from the Catalyst Research Instruments Operations resulting from decreased catalyst research instrument sales. The results reflected total non-cash amounts for depreciation, amortization and contingent consideration liability adjustments totaling \$521,700 and \$675,800 for the three and nine month periods ended March 31, 2018 compared to \$87,100 and \$276,500 for the corresponding three and nine month periods in 2017.

### Results of Operations.

#### The Three months ended March 31, 2018 Compared with The Three Months Ended March 31, 2017

Net revenues for the three months ended March 31, 2018 increased \$188,400 (9.9%) to \$2,099,300 from \$1,910,900 for the three months ended March 31, 2017, reflecting an increase of \$297,600 in royalty revenues earned by the Bioprocessing Systems Operations, \$139,900 increase in net sales of benchtop laboratory equipment, partially offset by a \$249,100 decrease in catalyst research instruments sales due to decreased orders from Original Equipment Manufacturer ("OEM") customers and lack of large orders. As of March 31, 2018, the order backlog for catalyst research instruments was \$1,175,800, all of which is expected to be shipped during fiscal year ending June 30, 2018, compared to \$431,200 as of March 31, 2017.

The overall gross profit percentage for the three months ended March 31, 2018 was 36.6% compared to 44.8% for the three months ended March 31, 2017 due to adjustment for increased contingent consideration from increased royalty revenues for the Bioprocessing Systems Operations.

General and administrative expenses increased by \$35,100 (8.1%) to \$470,200 for the three months ended March 31, 2018 compared to \$435,100 for the three months ended March 31, 2017 due to various incremental increases across the three operational segments.

Selling expenses for the three months ended March 31, 2018 increased \$39,900 (17.8%) to \$263,800 from \$223,900 for the three months ended March 31, 2017, due to higher selling and marketing expenses by the Benchtop Laboratory Equipment Operations primarily for new products.

Research and development expenses amounted to \$117,700 for the three months ended March 31, 2018 and \$114,100 for the three months ended March 31, 2017.

The Company reflected an income tax benefit of \$46,200 for the three months ended March 31, 2018 compared to income tax expense of \$17,300 for the three months ended March 31, 2017, primarily due to the loss for the period.

As a result of the foregoing, the Company recorded a net loss of \$37,700 for the three months ended March 31, 2018 compared to net income of \$65,600 for the three months ended March 31, 2017.

The Nine months ended March 31, 2018 Compared with The Nine months ended March 31, 2017

Net revenues for the nine months ended March 31, 2018 decreased \$881,200 (14.3%) to \$5,272,600 from \$6,153,800 for the nine months ended March 31, 2017, reflecting a decrease of \$1,336,400 in net sales of catalyst research instruments due to decreased orders from OEM customers and lack of large orders during the beginning of the year, partially offset by an increase of \$101,900 in sales of benchtop laboratory equipment and \$353,300 increase in bioprocessing royalties earned.

The overall gross profit percentage for both the nine months ended March 31, 2018 and 2017 was 37.7%.

General and administrative expenses for the nine months ended March 31, 2018 increased \$49,900 (4.0%) to \$1,306,600 compared to \$1,256,700 for the nine months ended March 31, 2017 due to various incremental increases across the three operational segments.

Selling expenses for the nine months ended March 31, 2018 increased \$14,700 (2.2%) to \$679,500 from \$664,800 for the nine months ended March 31, 2017, due to higher selling and marketing expenses by the Benchtop Laboratory Equipment Operations primarily for new products.

Research and development expenses increased by \$45,200 (13.5%) to \$379,700 for the nine months ended March 31, 2018 compared to \$334,500 for the nine months ended March 31, 2017, primarily due to increased new product development costs incurred by the Benchtop Laboratory Equipment Operations related to the Torbal Scales Division.

Total other income decreased by \$7,200 (52.9%) to \$6,400 for the nine months ended March 31, 2018 from \$13,600 for the nine months ended March 31, 2017 due to a gain on a sale of investment securities last year.



The Company reflected an income tax benefit of \$22,600 for the nine months ended March 31, 2018 compared to \$16,000 tax expense for the nine months ended March 31, 2017, primarily due to the loss for the period.

As a result of the foregoing, the Company recorded a net loss of \$351,500 for the nine months ended March 31, 2018 compared to net income of \$62,200 for the nine months ended March 31, 2017.

Liquidity and Capital Resources. Cash and cash equivalents decreased by \$346,500 to \$678,600 as of March 31, 2018 from \$1,025,100 as of June 30, 2017 primarily due to increased inventories partially offset by customer advances.

Net cash used in operating activities was \$150,200 for the nine months ended March 31, 2018 compared to \$204,800 provided during the nine months ended March 31, 2017. The current period reflected increased inventories due to new products and work in process for catalyst research instruments partially offset by an adjustment to the fair value of contingent consideration liability and customer advances. Net cash used in investing activities was \$88,600 for the nine months ended March 31, 2018 compared to \$38,600 used during the nine months ended March 31, 2017 principally due to new capital equipment purchased during the current year period by the Benchtop Laboratory Equipment Operations. The Company used \$107,700 in financing activities in the nine months ended March 31, 2018 compared to \$199,900 in the nine months ended March 31, 2017, principally because the Company paid a dividend last year, and paid more in contingent consideration in last year's same period.

The Company's working capital amounted to \$3,777,800 as of March 31, 2018 and \$3,728,500, as of June 30, 2017.

The Company has a Demand Line of Credit through June 2018 with First National Bank of Pennsylvania which provides for borrowings of up to \$300,000 for regular working capital needs, bearing interest at prime, currently 4.75%. Advances on the line, are secured by a pledge of the Company's assets including inventory, accounts, chattel paper, equipment and general intangibles of the Company. As of March 31, 2018 \$40,000 which was borrowed by our subsidiary, Altamira Instruments, was outstanding under such line.

Management believes that the Company will be able to meet its cash flow needs during the 12 months ending June 30, 2018 from its available financial resources including its line of credit, its cash and investment securities, and operations.



Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this report, the Company's management performed an evaluation of the effectiveness of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on this evaluation, the Chief Executive and Chief Financial Officer of the Company has concluded that the Company's disclosure controls and procedures were not effective as of March 31, 2018, because of the identification of a material weakness in internal control over financial reporting which related to the accounting for the fair market value of a contingent consideration liability related to its Bioprocessing Systems Operations. Notwithstanding the material weakness that existed as of March 31, 2018, the Chief Executive and Chief Financial Officer of the Company has concluded that the financial statements included in this Quarterly Report on Form 10-Q present fairly, in all material respects, the financial position, results of operations, and cash flows of the Company and its subsidiaries in conformity with accounting principles generally accepted in the United States of America ("GAAP").

PART II – OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

Exhibit Number	Description
<u>31.1</u>	<u>Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u>
<u>32.1</u>	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Reports on Form 8-K: None



SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

SCIENTIFIC INDUSTRIES, INC.

Date: May 15, 2018 (Registrant)

/s/ Helena R. Santos

Helena R. Santos

President, Chief Executive Officer, Treasurer

Chief Financial and Principal Accounting Officer