

Edgar Filing: XSUNX INC - Form 10-Q

XSUNX INC  
Form 10-Q  
May 15, 2007

SECURITIES EXCHANGE COMMISSION  
Washington, D.C. 20549

Quarterly Report under Section 13 or 15(d) of  
The Securities Exchange Act of 1934

For Quarter Ended March 31, 2007

Commission file number: 000-29621

XSUNX, INC.

(Exact name of registrant as specified in its charter)

Colorado  
-----  
(State of incorporation)

84-1384159  
-----  
(I.R.S. Employer Identification No.)

65 Enterprise, Aliso Viejo, CA 92656  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number: (949) 330-8060

Securities registered pursuant to Section  
12(b) of the Act:

Title of each class: None Name of each exchange on which registered: N/A

Securities registered pursuant to Section 12(g) of the Act:

Title of each class: None

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 the filing requirements for at least the past 90 days. Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of May 15, 2007 the number of shares outstanding of the registrant's only class of common stock was 157,019,856.

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

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

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XSUNX, Inc,  
(A DEVELOPMENT STAGE COMPANY)

FINANCIAL STATEMENTS

March 31, 2007  
(UNAUDITED)

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JASPERS + HALL, PC  
CERTIFIED PUBLIC ACCOUNTANTS

-----  
9175 E. Kenyon Avenue, Suite 100  
Denver, CO 80237  
303-796-0099

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors  
XSUNX, INC.  
Aliso Viejo, CA

We have reviewed the accompanying balance sheet of XSUNX, INC. (a development stage company) as of March 31, 2007, and the related statements of operations, stockholders' equity (deficit), and cash flows for the three and six month periods then ended. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with standards of the Public Company Accounting Oversight Board (United States). The review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the consolidated financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying financial statements for them to be in conformity with accounting principles generally accepted in the United States.

/s/ Jaspers + Hall, PC  
Jaspers + Hall, PC  
Denver, CO  
May 10, 2007

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XSUNX, INC.  
(A Development Stage Company)  
Balance Sheets  
(Unaudited)

	Unaudited March 31, 2007
	-----
ASSETS:	
Current assets:	
Cash	\$ 2,401,
Prepaid Research and Development Expense	
Prepaid Professional Expense	290,
Prepaid Legal Expense	11,
	-----
Total current assets	2,703,
	-----
Fixed assets:	
Office & Misc. Equipment	32,
Research and Development Equipment	389,
Leasehold Improvement	89,
	-----
Total Fixed Assets	512,
Less Depreciation	(128,
	-----
Total fixed assets	383,
	-----
Other assets:	
Patents	40,
Security Deposit	4,
Accured Interest Earned	19,
Note Receivable	812,
Deferred Financing Costs	
Marketable Prototype	1,765,
	-----
Total other assets	2,641,
	-----
TOTAL ASSETS	\$ 5,728,
	=====
LIABILITIES AND STOCKHOLDERS' EQUITY:	
Current Liabilities:	
Accounts Payable	\$ 481,
Accrued Expenses	20,
	-----
Total current liabilities	501,
	-----
Stockholders' Equity:	

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Preferred Stock, par value \$0.01 per share; 50,000,000 shares authorized; no shares issued and outstanding	
Treasury Stock, no par value; 26,798,418 issued and outstanding	
Common Stock, no par value; 500,000,000 shares authorized; 157,019,856 shares issued and outstanding at March 31, 2007	13,278,
and 157,169,856 shares were issued and outstanding at September 30, 2006	
Common Stock Warrants	2,151,
Deficit accumulated during the development stage	(10,202,
	-----
Total stockholders' profit (deficit)	5,227,
	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 5,728,
	=====

See Accountants' Review Report

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XSUNX, INC.  
(A Development Stage Company)  
Statement of Operations  
(Unaudited)

	Three-Months Ended		Six-Months Ended		Feb. (Inc M 2
	March 31st		March 31st		
	2007	2006	2007	2006	
	-----	-----	-----	-----	-----
Revenue					
Service Income	\$ 6,880	\$ -	\$ 6,880	\$ 8,000	\$
Other Income	-	-	-	-	
	-----	-----	-----	-----	-----
Total Revenue	6,880	-	6,880	8,000	
	-----	-----	-----	-----	-----
Expenses:					
Advertising	18,223	90	43,470	439	\$
Bank Charges	204	115	229	179	
Conferences & Seminars	99	-	9,370	1,500	\$
Consulting	4,269	-	42,542	-	\$ 1,
Depreciation	16,714	27,647	34,667	27,647	\$
Directors' Fees	-	-	-	-	\$
Due Diligence	-	-	-	13,000	\$
Dues and Subscriptions	-	-	-	-	
Equipment Rental	-	-	-	-	
Filing Fees	-	9,225	2,497	9,225	
Impairment loss	-	-	-	-	\$
Insurance	31,049	-	34,585	-	\$
Legal & Accounting	41,252	35,009	109,577	68,609	\$
Licenses & Fees	50	-	70	-	
Loan Fees	-	-	-	-	\$
Meals & Entertainment	-	-	-	-	

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Miscellaneous			28	800	
Office Expenses	3,073	77	11,434	1,550	\$
Patent Fees		-		-	
Postage & Shipping	1,972	278	2,698	736	
Printing	1,968	3,797	6,382	6,740	\$
Public Relations	670	25,168	27,300	58,520	\$
Research & Development -					
Tech. License	109,236	238,409	320,331	403,012	\$ 1,
Rent	15,638	2,250	30,350	4,500	\$
Salaries	216,105	40,670	357,880	84,899	\$ 1,
Subscription Reports		109		193	
Taxes	504	-	504	-	
Telephone	6,478	2,109	12,288	3,499	\$
Transfer Agent Expense	100	80	383	230	\$
Travel, Meals & Entertainment	38,376	7,162	75,581	12,022	\$
Warrant Option Expense		-	364	951,250	\$ 2,
	-----	-----	-----	-----	-----
Total Operating Expenses	505,980	392,195	1,122,530	1,648,550	10,
	-----	-----	-----	-----	-----
Other Income (Expense)					
Interest Expense	364	160,500	364	160,500	\$
Interest Income	(51,515)	(1,224)	(84,769)	(1,224)	\$ (
Forgiveness of Debt	-	-	-	-	\$
	-----	-----	-----	-----	-----
Total Other Income/Expense	(51,151)	159,276	(84,405)	159,276	
	-----	-----	-----	-----	-----
Net (Loss)	\$ (447,949)	\$ (551,471)	\$ (1,031,245)	\$ (1,799,826)	\$ (10,
	=====	=====	=====	=====	=====
Per Share Information:					
Basic					
common shares outstanding	157,046,230	128,401,012	156,249,529	123,876,739	
	=====	=====	=====	=====	
Net Loss per Common Share	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.02)	
	=====	=====	=====	=====	
Fully Diluted					
common shares outstanding	165,748,397	136,603,179	164,951,696	132,078,906	
	=====	=====	=====	=====	
Net Loss per Common Share	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.02)	
	=====	=====	=====	=====	

See Accountants' Review Report

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XSUNX, INC.  
(A Development Stage Company)  
Statement of Stockholders' Equity (Deficit)  
March 31, 2007

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(Unaudited)

	Treasury Stock		Common Stock		Common Stock
	# of Shares	Amount	# of Shares	Amount	Warra
Inception February 25, 1997	-	-	-	-	
Issuance of stock for cash	-	-	15,880	217,700	
Issuance of stock to Founders	-	-	14,110	-	
Issuance of stock for consolidation	-	-	445,000	312,106	
Net Loss for Year	-	-	-	-	
Balance - September 30, 1997	-	-	474,990	529,806	
Issuance of stock for services	-	-	1,500	30,000	
Issuance of stock for cash	-	-	50,200	204,000	
Consolidation stock cancelled	-	-	(60,000)	(50,000)	
Net Loss for Year	-	-	-	-	
Balance - September 30, 1998	-	-	466,690	713,806	
Issuance of stock for cash	-	-	151,458	717,113	
Issuance of stock for services	-	-	135,000	463,500	
Net Loss for Year	-	-	-	-	
Balance - September 30, 1999	-	-	753,148	1,894,419	
Issuance of stock for cash	-	-	15,000	27,000	
Net Loss for year	-	-	-	-	
Balance - September 30, 2000	-	-	768,148	1,921,419	
Extinguishment of debt	-	-	-	337,887	
Net Loss for year	-	-	-	-	
Balance - September 30, 2001	-	-	768,148	2,259,306	
Net Loss for year	-	-	-	-	
Balance - September 30, 2002	-	-	768,148	2,259,306	
Issuance of stock for Assets	-	-	70,000,000	3	
Issuance of stock for Cash	-	-	9,000,000	225,450	
Issuance of stock for Debt	-	-	115,000	121,828	

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Issuance of stock for Expenses	-	-	115,000	89,939	
Issuance of stock for Services	-	-	31,300,000	125,200	
Net Loss for year	-	-	-	-	
	-----	-----	-----	-----	-----
Balance - September 30, 2003	-	-	111,298,148	2,821,726	
	-----	-----	-----	-----	-----
Issuance of stock for cash	-	-	2,737,954	282,670	
Issuance of Common Stock Warrants	-	-	-	-	1,200,
Net Loss for Year	-	-	-	-	
	-----	-----	-----	-----	-----
Balance - September 30, 2004			114,036,102	3,104,396	1,200,
	-----	-----	-----	-----	-----

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XSUNX, INC.  
(A Development Stage Company)  
Statement of Stockholders' Equity (Deficit)  
March 31, 2007

(Unaudited)

	Treasury Stock		Common Stock		Common Stock Warra
	# of Shares	Amount	# of Shares	Amount	
	-----	-----	-----	-----	-----
Issuance of stock for cash	-	-	6,747,037	531,395	
Issuance of stock for services	-	-	3,093,500	360,944	
Issuance of stock for collateral	26,798,418	-	-	-	
Net Loss for Year	-	-	-	-	
	-----	-----	-----	-----	-----
	26,798,418	-	123,876,639	3,996,735	1,200,
	-----	-----	-----	-----	-----
Issuance of stock for services	-	-	72,366	31,500	
Issuance of Common Stock Warrants	-	-	-	-	951,2
Issuance of stock for debenture conversion	-	-	21,657,895	5,850,000	
Issuance of stock for interest expense	-	-	712,956	241,383	
Issuance of stock for warrant conversion	-	-	10,850,000	3,171,250	
Net Loss for Year	-	-	-	-	
	-----	-----	-----	-----	-----
Balance September 30, 2006	26,798,418	-	157,169,856	13,290,868	2,151,
	-----	-----	-----	-----	-----
Net Loss for Period	-	-	-	-	
	-----	-----	-----	-----	-----
Balance - December 31, 2006	26,798,418	-	157,169,856	13,290,868	2,151,
	-----	-----	-----	-----	-----
Cancelation of Stock for Services Returned			(150,000)	(12,000)	



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Release of Security Collateral (26,798,418)

Balance March 31, 2007

-----	-----	-----	-----	-----	-----
-	\$ -	157,019,856	\$ 13,278,868	\$2,151	
=====	=====	=====	=====	=====	=====

All shares have been adjusted for the 1 for 20 reverse split.

See Accountants' Review Report

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XSUNX, INC.  
(A Development Stage Company)  
Statement of Cash Flows  
(Unaudited)

Indirect Method

	Six-Months Ended March 31,	
	2007	2006
	-----	-----
Cash Flows from Operating Activities:		
Net Loss	\$ (1,031,245)	\$ (1,799,826)
Issuance of Common Stock for Services	(12,000)	7,500
Issuance of Common Stock for Loan Inducement	-	-
Warrant Expense	-	-
Issuance of Stock for Interest	-	-
Depreciation	43,761	27,647
Written Off Equipment	-	-
Adjustments to reconcile net loss to cash used in operating activities:		
(Increase) Accounts Receivable	-	-
(Increase) Security Deposit	(1,700)	-
(Increase) in Prepaid Expense	46,582	(257,673)
Increase in Accrued Expenses	13,684	79,849
(Decrease) in Accounts Payable	(101,276)	1,150,342
	-----	-----
Net Cash Flows Used for Operating Activities	(1,042,194)	(792,161)
	-----	-----
Cash Flows from Investing Activities:		
Purchase of Equipment	(29,701)	(220,000)
Equipment Written Off	-	-
Note Receivable	(812,500)	-

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Accrued Interest earned	(19,288)	
Purchase of Intangible Assets	-	(1,775,000)
	-----	-----
Net Cash Flows Used for Investing Activities	(861,489)	(1,995,000)
	-----	-----
Cash Flows from Financing Activities:		
Proceeds from Notes Payable	-	(850,000)
Deferred Financing Costs	-	(500,000)
Proceeds from Debenture Conversion	-	5,000,000
Issuance of Common Stock for Warrants		951,250
Issuance of Common Stock for cash	-	2,979,330
	-----	-----
Net Cash Flows Provided by Financing Activities	-	7,580,580
	-----	-----
Net Increase (Decrease) in Cash	(1,903,683)	4,793,419
	-----	-----
Cash and cash equivalents - Beginning of period	4,305,105	175,869
	-----	-----
Cash and cash equivalents - End of period	\$ 2,401,422	\$ 4,969,288
	=====	=====
Supplemental Disclosure of Cash Flow Information		
Cash Paid During the Year for:		
Interest	\$ 364	\$ 160,500
	=====	=====
Income Taxes	\$ -	\$ -
	=====	=====
NON-CASH TRANSACTIONS		
Common stock issued in exchange for services	\$ (12,000)	\$ 7,500
	=====	=====

See Accountants' Review Report

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XSUNX, INC.  
(A Development Stage Company)  
Notes to Financial Statements  
March 31, 2007  
(Unaudited)

Note 1 - Presentation of Interim Information:

In the opinion of the management of XSUNX, Inc., the accompanying unaudited financial statements include all normal adjustments considered necessary to present fairly the financial position as of March 31, 2007 and the results of operations for the three and six-months ended March 31, 2007 and 2006 and for the period February 25, 1997 (inception) to March 31, 2007, and cash flows for the six-months ended March 31, 2007 and 2006 and the for the period February 25, 1997 (inception) to March 31, 2007. Interim results are not necessarily

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indicative of results for a full year.

The financial statements and notes are presented as permitted by Form 10-Q, and do not contain certain information included in the Company's audited financial statements and notes for the fiscal year ended September 30, 2006.

### Note 2 - Lease - Golden Suite:

As of July 1, 2006 a new lease was signed for the Golden Office in the amount of \$1,687.50 per month plus a fee of \$825.00 for utilities. This will increase to \$1,787.50 per month on 7/1/07 and \$1,790.00 per month on 7/1/08. The lease expires on 6/30/09.

### Note 3 - Technology Development and Licensing Agreement

On January 1, 2007, XSUNX, Inc. issued a secured, seven year, 10% note to Sencera, LLC in the amount up to \$1,500,000. Under the terms, the company provided Sencera, LLC with \$400,000 at the time of signing and \$137,500 per month for up to eight months. These funds are to be used to develop Technology and obtain licenses in agreement with the Technology Development and License Agreement between Sencera and XSUNX, Inc also signed on January 1, 2007. The note may be converted into a membership interest in Sencera, LLP and an extension of the license for a period of three years. The security consists of the license rights, the ability to exercise the conversion and all other rights and remedies provided by law. As of March 31, 2007 the current balance of the note receivable was \$812,500.00 plus accrued interest earned of \$19,288.

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XSUNX, INC.  
(A Development Stage Company)  
Notes to Financial Statements  
March 31, 2007  
(Unaudited)

### Note 4 - Settlement with Service Provider

In December 2006 the Company entered into a settlement agreement with a service provider in which the service provider returned to the Company 150,000 of the 300,000 shares of common stock issued to the service provider in the period ended March 31, 2005. The shares were received and cancelled effective January 2007. As a result of the return and cancellation of these shares the Company will record a credit to expenses in the amount of \$12,000 and a debit to paid in capital of \$12,000 for the period ending March 31, 2007. The \$12,000 dollars represents one half of the monetary value expensed by the Company in the period in which the shares were issued.

### Note 5 - Employment and Consulting Agreements

Effective January 1, 2007, XSUNX, Inc. entered into two year Employment Agreements with the following individuals:

Joseph Grimes	Chief Operating Officer	\$150,000.00
Jeff Huitt	Chief Financial Officer	\$135,000.00
Robert Wendt	Vice President of Engineering	\$150,000.00
Kurt Laetz	Vice President of Global Sales	\$120,000.00

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Effective January 26, 2007, XSUNX, Inc. entered into a two year Consulting and Advisory Agreement with Dr. John Moore to become the Chairman of the Company's Scientific Advisory Board.

Effective February 22, 2007, XSUNX, Inc. entered into a two year Consulting and Advisory Agreement with Dr. Edward Yu to become a member of the Company's Scientific Advisory Board.

The company authorized employment incentive option grants to the following employees on January 26th 2007 at an exercise price per share of \$0.46 with a first vesting date of April 1, 2007:

Joseph Grimes	500,000 Option Shares
Jeff Huitt	500,000 Option Shares
Robert Wendt	500,000 Option Shares

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XSUNX, INC.  
(A Development Stage Company)  
Notes to Financial Statements  
March 31, 2007  
(Unaudited)

The common vesting schedules for the above grantee's is:

- (a) The Option shall become exercisable in the amount of 50,000 shares upon the First Vesting Date. Thereafter, the Option shall vest and become exercisable at the rate of 50,000 Shares per calendar quarter up to a total of 400,000 shares.
- (b) This Option shall become exercisable in the amount of 50,000 shares for each of the first two sales/licensure of an XsunX system

Kurt Laetz 250,000 Option Shares

Kurt Laetz vesting schedule is:

- (c) The Option shall become exercisable in the amount of 15,000 shares upon the First Vesting Date. Thereafter, the Option shall vest and become exercisable at the rate of 15,000 Shares per calendar quarter.
- (d) During the second year of employment of Optionee by XsunX the Option will vest and become exercisable at the rate of 22,500 Shares per calendar quarter, or any apportioned amount thereof, during the term of the second year of employment by XsunX, Inc. of the Optionee.
- (e) This Option shall become exercisable in the amount of 50,000 shares for each of the first two sales/licensure of an XsunX system.

Consultant Option Grant. The Company authorized the issuance of an option grant

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on January 26, 2007 to a consultant in the amount of 150,000 option shares at an option exercise price of \$0.46 with a first vesting date of April 26, 2007 with following vesting schedule:

- (a) The Option shall become exercisable in the amount of 18,750 shares upon the First Vesting Date. Thereafter, the Option shall vest become exercisable at the rate of 18,750 Shares per calendar quarter, or any apportioned amount thereof, during the term of engagement by XsunX, Inc. of the Optionee.

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XSUNX, INC.  
(A Development Stage Company)  
Notes to Financial Statements  
March 31, 2007  
(Unaudited)

Consultant Option Grant. The Company authorized the issuance of an option grant on February 22, 2007 to a consultant in the amount of 100,000 option shares at an option exercise price of \$0.53 with a first vesting date of May 23, 2007 with following vesting schedule:

- (a) The Option shall become exercisable in the amount of 12,500 shares upon the First Vesting Date. Thereafter, the Option shall vest become exercisable at the rate of 12,500 Shares per calendar quarter, or any apportioned amount thereof, during the term of engagement by XsunX, Inc. of the Optionee.

### Note 6 - Stock Option Plan

The Company has adopted a Stock Option Plan to enable the company to obtain and retain the services of the types of Employees, Consultants and Directors who will contribute to the Company's long rang success and to provide incentives which are linked directly to increases in share value which will inure to the benefit of all stockholders of the Company. A total of 20,000,000 shares of common stock are authorized under the plan.

### Note 7 - Agreement to Purchase Assets

Effective March 23, 2007 XsunX, Inc. entered into a binding letter of intent with a manufacturer of photovoltaic products for the purchase of certain net assets of the manufacturer for the amount of five million dollars (\$5,000,000) USD in a cash transaction. The purpose of the letter of intent, and interest in the acquisition by XsunX, was driven by what XsunX anticipates is the opportunity to expand its current operations to include technologies and manufacturing capabilities for silicon wafer, conversion of wafers to solar cells, complete solar module manufacturing, and module mounting components. The operating assets are comprised of approximately twenty plus (20+) megawatts of annual polysilicon wafer manufacturing capabilities, and approximately fifteen (15) megawatts of solar cell and module manufacturing capabilities. While the wafer and cell conversion systems provide separate and distinct additions to the Company's product offering XsunX believes that the facilities back end module manufacture and assembly systems and reliability testing equipment provide an expansion opportunity for use by XsunX in the commercialization of its thin film technologies.

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On or about April 27, 2007 the Company was notified by the seller of a change in direction and decision not to honor the sales agreement. XsunX continues to work towards a successful completion of the transaction and has engaged legal counsel to assist in enforcing its rights under the agreement.

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XSUNX, INC.  
(A Development Stage Company)  
Notes to Financial Statements  
March 31, 2007  
(Unaudited)

### Note 8 - Planned Expansion of Business Operations

In March XsunX launched efforts to expand the scope of business development efforts to include the planned establishment of a solar energy module manufacturing facility to be located in the United States. The Company intends to employ the use of certain of its technologies, and those under license, for use in the manufacture and sale of finished solar energy products. The Company is planning the manufacturing line around a 5 megawatt modular design allowing operations to scale from 5 to 20 to 50 megawatts of production capacity in 2008, 2009, and 2010 respectively.

### Note 9 - Release of Security Collateral

The Company's obligations under a July 2005 and December 2005 Securities Purchase Agreements had provided as security substantially all of the Company's assets. As further security for its obligations there under, the Company had deposited into escrow 26,798,418 shares of Common Stock. In addition, Tom Djokovich, the Company's Chief Executive Officer, had granted a security interest in 925,000 shares of Common Stock that he owns to secure the Company's obligations under the July Agreement only. As of December 2006 XsunX had received notice from the secured party of the release of the security interest in the above listed security shares and assets. On January 18, 2007 the 26,798,418 security shares were cancelled.

### Note 10 - Subsequent Events

#### CONSULTING AGREEMENT

Effective April 23, 2007, XSUNX, Inc. entered into a two year Consulting and Advisory Agreement with Dr. Richard Ahrenkiel to become a member of the Company's Scientific Advisory Board.

The company authorized the issuance of an option grant on April 23, 2007 to a consultant in the amount of 100,000 option shares at an option exercise price of \$0.45 with a first vesting date of July 23, 2007 with following vesting schedule:

- (a) The Option shall become exercisable in the amount of 12,500 shares upon the First Vesting Date. Thereafter, the Option shall vest become exercisable at the rate of 12,500 Shares per calendar quarter, or any apportioned amount thereof, during the term of engagement by XsunX, Inc. of the Optionee.

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XSUNX, INC.  
(A Development Stage Company)  
Notes to Financial Statements  
March 31, 2007  
(Unaudited)

LEGAL EFFORT TO ENFORCE AGREEMENT

In connection with the Company's efforts to complete the purchase of certain solar product manufacturing assets as specified by a binding letter of intent between XsunX and the seller dated March 23, 2007, the Company filed a complaint against the seller and related entities in the United States District Court for the District of Massachusetts on May 10th, 2007, alleging breach of contract and other claims.

SALE AGREEMENT

The Company has entered into agreements for the sale of certain vacuum deposition technology equipment valued at \$41,800,000, excluding royalty payments based on per watt annualized production totals. The agreements, consisting of a systems sale and a royalty based manufacturing license agreement, provide for thin film photovoltaic production equipment and two product development tools specializing in the fabrication of micro-crystalline and amorphous thin film silicon solar cells. Manufacture of the product development tools is scheduled to begin in June 2007 upon receipt of initial payments from the buyer with delivery beginning in January 2008, and the balance of systems slated to begin deliveries in late 2008.

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

CAUTIONARY AND FORWARD LOOKING STATEMENTS

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In addition to statements of historical fact, this Form 10-Q contains forward-looking statements. The presentation of future aspects of XsunX, Inc. ("XsunX", the "Company" or "issuer") found in these statements is subject to a number of risks and uncertainties that could cause actual results to differ materially from those reflected in such statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management's analysis only as of the date hereof. Without limiting the generality of the foregoing, words such as "may", "will", "expect", "believe", "anticipate", "intend", or "could" or the negative variations thereof or comparable terminology are intended to identify forward-looking statements.

These forward-looking statements are subject to numerous assumptions, risks and uncertainties that may cause XsunX's actual results to be materially different from any future results expressed or implied by XsunX in those statements. Important facts that could prevent XsunX from achieving any stated goals include, but are not limited to, the following:

Some of these risks might include, but are not limited to, the following:

- (a) volatility or decline of the Company's stock price;
- (b) potential fluctuation in quarterly results;
- (c) failure of the Company to earn revenues or profits;
- (d) inadequate capital to continue or expand its business, inability to raise additional capital or financing to implement its business plans;
- (e) failure to commercialize its technology or to make sales;
- (f) rapid and significant changes in markets;
- (g) litigation with or legal claims and allegations by outside parties;
- (h) insufficient revenues to cover operating costs.

There is no assurance that the Company will be profitable, the Company may not be able to successfully develop, manage or market its products and services, the Company may not be able to attract or retain qualified executives and technology personnel, the Company's products and services may become obsolete, government regulation may hinder the Company's business, additional dilution in outstanding stock ownership may be incurred due to the issuance of more shares, warrants and stock options, or the exercise of warrants and stock options, and other risks inherent in the Company's businesses.

The Company undertakes no obligation to publicly revise these forward-looking statements to reflect events or circumstances that arise after the date hereof. Readers should carefully review the factors described in other documents the Company files from time to time with the Securities and Exchange Commission, including the Quarterly Reports on Form 10-Q and Annual Reports on Form 10-K filed by the Company and any Current Reports on Form 8-K filed by the Company.



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XsunX develops and markets proprietary Thin Film Photovoltaic (TFPV) solar cell designs and core solar cell manufacturing systems, enabling licensees to manufacture TFPV solar devices on various substrates. We function as a strategic solar technology partner, supplying the advanced thin film solar cell manufacturing know-how and capabilities that will enable original equipment manufacturers ("OEM") customers to address the expanding market for thin film solar products.

The product of the Company's development efforts is intended to deliver two aspects of deliverable technologies in the form of an integrated solution providing, a) commercially scalable manufactured processes and equipment designed for the specific manufacture of the Company's thin film solar technologies, and, b) proprietary thin film solar cell designs that address new application opportunities in the growing field of Building Integrated Photovoltaics.

XsunX is positioning itself as a provider of TFPV device designs and core manufacturing products to an expanding global group of existing and new entrant solar product manufacturers. The company is working to establish an environment in which XsunX products and technologies are viewed as advanced core support infrastructure to manufacturers increasing their opportunities for success in servicing their regional solar markets.

In March XsunX launched efforts to expand the scope of business development efforts to include the planned establishment of a solar energy module manufacturing facility to be located in the United States. The Company intends to employ the use of certain of its technologies, and those under license, for use in the manufacture and sale of finished solar energy products. The Company is planning the manufacturing line around a 5 megawatt modular design allowing operations to scale from 5 to 20 to 50 megawatts of production capacity in 2008, 2009, and 2010 respectively.

Management believes the summary data presented herein is a fair presentation of the Company's results of operations for the periods presented. Due to the Company's change in primary business focus in October 2003 and new business opportunities these historical results may not necessarily be indicative of results to be expected for any future period. As such, future results of the Company may differ significantly from previous periods.

### RESULTS OF OPERATIONS FOR THE THREE-MONTH PERIOD ENDED MARCH 31, 2007 COMPARED TO THE SAME PERIOD IN 2006

The Company generated minimal revenues of \$6,880 from a licensing agreement in the period ended March 31, 2007 as compared to zero revenue in the same period in 2006.

The Company incurred operating expenses totaling \$500,935 for the three months ending March 31, 2007 compared to \$392,195 for the same period in 2006. Primary sources for the increase to operating expense of \$108,740 include: Salaries increased by \$175,435 to 216,105 from \$40,670 in the same period in 2006 as a result of the continued growth of the company workforce., Insurance expense increase \$31,049 to \$31,049 as compared to \$0 in the same period in 2006, Travel expenses increased \$31,214 to \$38,376 from \$7,162 as compared to the same period in 2006. These were offset by a decrease in Research and Development expenses of \$129,173 to \$109,236 as compared to \$238,409 for the same period in 2006. The \$1,356,484 operating expenses includes non-cash charges of \$16,714 for depreciation.

The net loss for the three months ending March 31, 2007 was (\$442,904) as compared to a net loss of (\$551,471) for the same period 2006. The decreased net loss of \$108,567 includes (i) The operating expense changes

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discussed above, (ii) a decrease in interest expense of \$160,136 related to the conversion of a debenture in the prior period to common stock, and (iii) an increase in interest income of \$50,291 resulting from the investment of cash balances in interest bearing accounts and the Sencera note.

The Company incurred net losses of (\$442,904) and (\$551,471) in the three-month period ended March 31, 2007 and 2006 respectively. The associated net loss per share was \$(0.01) for the three month period ended March 31, 2007

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and \$(0.01) for the same period in 2006. The Company anticipates the trend of losses to continue in future quarters until the Company can recognize sales of significance of which there is no assurance.

### RESULTS OF OPERATIONS FOR THE SIX-MONTH PERIOD ENDED MARCH 31, 2007 COMPARED TO THE SAME PERIOD IN 2006

The Company generated minimal revenues of \$6,880 from a licensing agreement in the period ended March 31, 2007 as compared to \$8,000 in the same period in 2006.

The Company incurred operating expenses totaling \$1,122,530 for the six months ending March 31, 2007 compared to \$1,648,550 for the same period in 2006. Primary sources for the decrease to operating expense of \$526,020 include: A decrease of \$950,886 in Warrant Option Expenses and a decrease in Research and Development expenses of \$82,681 to \$320,331 for the six months ending March 31, 2007 as compared to \$403,012 for the same period in 2006. These decreases to operating expenses were partially offset by an increase to Salaries of \$272,981 to \$357,880 from \$84,899 in the same period in 2006 as a result of the continued growth of the company workforce, Insurance expense increase \$34,585 to \$34,585 as compared to \$0 in the same period in 2006, Travel expenses increased \$63,559 to \$75,581 from \$12,022 as compared to the same period in 2006, Advertising increased \$43,031 to \$43,470 as compared to 439 in the same period in 2006, Legal and Accounting fees increased by \$40,968 to \$109,577 as compared to \$68,609 in the same period in 2006 and Consulting increased \$42,542 to \$42,542 as compared to zero in 2006. The \$1,122,530 operating expenses includes non-cash charges of \$34,667 for depreciation.

The net loss for the six months ending March 31, 2007 was (\$1,031,245) as compared to a net loss of (\$1,799,826) for the same period 2006. The decreased net loss of \$768,581 includes (i) The operating expense changes discussed above, (ii) a decrease in interest expense of \$160,136 related to the conversion of a debenture in the prior period to common stock, and (iii) an increase in interest income of \$83,545 resulting from the investment of cash balances in interest bearing accounts and the Sencera note.

The Company incurred net losses of (\$1,031,245) and (\$1,799,826) in the six-month period ended March 31, 2007 and 2006 respectively. The associated net loss per share was \$(0.01) for the three month period ended March 31, 2007 and \$(0.01) for the same period in 2006. The Company anticipates the trend of losses to continue in future quarters until the Company can recognize sales of significance of which there is no assurance.

### LIQUIDITY AND CAPITAL RESOURCES

The Company had cash at March 31, 2007 of \$2,401,422 and prepaid expenses in the amount of \$311,896 as compared to cash of \$4,305,105 and prepaid expenses in the amount of \$349,117 as of September 30, 2006. The Company had a net working capital of \$2,210,609 as compared to a working capital of \$4,065,523 at September 30, 2006. Cash flow used in operating activities during the

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six-month period ended, March 31, 2007, was (\$1,042,194) as compared to a use of cash of (\$792,161) for the same period 2006. The increase of cash used in operations of \$250,033 included (i) the decrease in net loss resulting primarily from decreased interest expense of \$160,136 relating to the conversion of a debenture in prior periods to common stock, (ii) increased cash flow on interest income of \$50,291 of which \$19,288 was a non-cash accrual of interest relating to the Sencera note, and (iii) the operation changes discussed above. The current period ending March 31, 2007 also included a non-cash depreciation expense of \$43,761 compared to \$27,647 in the same period in 2006. Additionally, a non-cash reduction to expense of \$12,000 was realized in the period associated with the return of common shares for services that were not performed.

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For the six-months ended March 31, 2007, the Company's capital needs have been met from the use of working capital provided by the proceeds of (i) the issuance of Common Stock for Debenture conversion and; (ii) the issuance of Common Stock for warrant conversion which both occurred in the fiscal year ended September 30, 2006.

We had, at March 31, 2007, cash and cash equivalents of \$2,713,318 and net working capital of \$2,210,609.

### DEVELOPMENT STAGE COMPANY

The Company is in the development stage and as of the period ending March 31, 2007, did not have any significant revenues. We have begun marketing efforts and anticipate the sale of licenses in the 2007 period however the cash flow requirements associated with the transition to revenue recognition may exceed cash generated from operations in the current and future periods. We may seek to obtain additional financing from equity and/or debt placements. As such, the Company's ability to secure additional financing on a timely basis is critical to its ability to stay in business and to pursue planned operational activities.

While we have been able to raise capital in a series of equity and debt offerings in the past there can be no assurances that we will be able to obtain such additional financing, on terms acceptable to us and at the times required, or at all.

Irrespective of whether the Company's cash assets prove to be inadequate to meet the Company's operational needs, the Company might seek to compensate providers of services by issuances of stock in lieu of cash.

### Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We do not have any market risk sensitive instruments. Since all operations are in U.S. dollar denominated accounts, we do not have foreign currency risk. Our operating costs are reported in U.S. dollars.

The Company does not invest in term financial products or instruments or derivatives involving risk other than money market accounts, which fluctuate with interest rates at market.

### Item 4. CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chairman have evaluated the effectiveness 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, as

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amended) as of the end of the period covered by this quarterly report and, based on this evaluation, have concluded that the disclosure controls and procedures are effective.

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There have been no changes in the Company's internal control over financial reporting that occurred during the Company's first fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

### PART II - OTHER INFORMATION

#### Item 1. LEGAL PROCEEDINGS

The Company is currently not aware of nor has any knowledge of any legal proceedings or claims that we believe will have, individually or in the aggregate, a material adverse affect on our business, financial condition or operating results.

#### Item 1A. RISK FACTORS

An investment in our shares involves a high degree of risk. Before making an investment decision, you should carefully consider all of the risks described on this Form 10-Q and Annual Reports on Form 10-K and Form 10KSB previously filed by the Company and any Current Reports on Form 8-K filed by the Company. If any of the risks discussed in these reports actually occur, our business, financial condition and results of operations could be materially and adversely affected. If this were to happen, the price of our shares could decline significantly and you may lose all or a part of your investment. The risk factors described below are not the only ones that may affect us. Our forward-looking statements in this prospectus are subject to the following risks and uncertainties. Our actual results could differ materially from those anticipated by our forward-looking statements as a result of the risk factors below. See "Cautionary and Forward-Looking Statements."

#### RISKS RELATED TO OUR BUSINESS

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WE HAVE NOT GENERATED ANY SIGNIFICANT REVENUES AND MAY NEVER ACHIEVE PROFITABILITY

We are a development stage company and, to date, have not generated any significant revenues. From inception through March 31, 2007, we had an accumulated deficit of \$10,202,983. For the quarter ended March 31, 2007 and 2006, we incurred net losses of \$447,949 and \$551,471 respectively. We cannot assure you that we can achieve or sustain profitability in the future. Our operations are subject to the risks and competition inherent in the establishment of a business enterprise. There can be no assurance that future operations will be profitable. Revenues and profits, if any, will depend upon various factors, including whether our product development can be completed, and if it will achieve market acceptance. We may not achieve our business objectives and the failure to achieve such goals would have an adverse impact on us.

WE MAY NEED TO RAISE ADDITIONAL CAPITAL WHICH MAY NOT BE AVAILABLE ON ACCEPTABLE TERMS OR AT ALL

In the future, we may be required to raise additional funds, particularly if we are unable to generate positive cash flow as a result of our operations. There can be no assurance that financing will be available in amounts or on terms

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acceptable to us, if at all. The inability to obtain additional capital may reduce our ability to continue to conduct business operations. If we are unable to obtain additional financing, we will likely be required to curtail our research and development plans. Any additional equity financing may involve substantial dilution to our then existing shareholders.

WE MAY NOT BE ABLE TO SUCCESSFULLY COMMERCIALIZE OUR TECHNOLOGIES WHICH WOULD RESULT IN CONTINUED LOSSES AND MAY REQUIRE US TO CURTAIL OR CEASE OPERATIONS

As is the case with any new technology, we expect the development process to continue. We cannot assure that our engineering resources will be able to modify

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the product fast enough to meet market requirements. We can also not assure that our product will gain market acceptance and that we will be able to successfully commercialize the technologies. The failure to successfully commercialize the technologies would result in continued losses and may require us to curtail or cease operations

OUR REVENUES ARE DEPENDENT UPON ACCEPTANCE OF OUR PRODUCTS BY LICENSEES; THE FAILURE OF WHICH WOULD CAUSE TO CURTAIL OR CEASE OPERATIONS

We believe that virtually all of our revenues will come from the licensing of our proprietary technologies to major manufacturers. We intend to offer non-exclusive licensing rights. As a result, we will continue to incur substantial operating losses until such time as we are able to generate revenues from licensing and service fees for our products through our distribution partners. There can be no assurance that businesses and customers will adopt our technology and products, or those businesses and prospective customers will agree to pay the licensing and service fees for our products. In the event that we are not able to significantly increase the number of customers that license our products, or if we are unable to charge the necessary license fees, our financial condition and results of operations will be materially and adversely affected.

IF WE LOSE KEY EMPLOYEES AND CONSULTANTS OR ARE UNABLE TO ATTRACT OR RETAIN QUALIFIED PERSONNEL, OUR BUSINESS COULD SUFFER.

Our success is highly dependent on our ability to attract and retain qualified scientific and management personnel. We are highly dependent on our management, including Mr. Tom Djokovich who has been critical to the development of our technologies and business. The loss of the services of Mr. Djokovich could have a material adverse effect on our operations. We do not have an employment agreement with Mr. Djokovich. Accordingly, there can be no assurance that he will remain associated with us. His efforts will be critical to us as we continue to develop our technology and as we transition from a development stage company to a company with commercialized products and services. If we were to lose Mr. Djokovich, or any other key employees or consultants, we may experience difficulties in competing effectively, developing our technology and implementing our business strategies.

THE LOSS OF STRATEGIC RELATIONSHIPS USED IN THE DEVELOPMENT OF OUR PRODUCTS AND TECHNOLOGY COULD IMPEDE OUR ABILITY TO COMPLETE OUR PRODUCT AND RESULT IN A MATERIAL ADVERSE EFFECT CAUSING THE BUSINESS TO SUFFER.

We have established a plan of operations under which a portion of our operations rely on strategic relationships with third parties, to provide general facilities, personnel, and expertise in research, development, systems design, assembly and support. A loss of any of our third party relationships for any reason could cause us to experience difficulties in implementing our business

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strategy. There can be no assurance that we could establish other relationships of adequate expertise in a timely manner or at all.

WE CANNOT GUARANTEE YOU THAT OUR PATENTS ARE BROAD ENOUGH TO PROVIDE ANY MEANINGFUL PROTECTION NOR CAN WE ASSURE YOU THAT ONE OF OUR COMPETITORS MAY NOT DEVELOP MORE EFFECTIVE TECHNOLOGIES, DESIGNS OR METHODS WITHOUT INFRINGING OUR INTELLECTUAL PROPERTY RIGHTS OR THAT ONE OF OUR COMPETITORS MIGHT NOT DESIGN AROUND OUR PROPRIETARY TECHNOLOGIES.

We have been granted, and exclusively own, three patents from the United States Patent and Trademark Office. We have also been granted a license to a patent and technology portfolio relating to photovoltaic technology design, manufacturing processes, and the development of technology. These patents and licenses may not protect us against our competitors, and patent litigation is very expensive. We may not have sufficient cash available to pursue any patent litigation to its conclusion because currently we do not generate revenues.

We cannot rely solely on our current patents to be successful. The standards that the U.S. Patent and Trademark Office and foreign patent office's use to grant patents, and the standards that U.S. and foreign courts use to interpret patents, are not the same and are not always applied predictably or uniformly

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and can change, particularly as new technologies develop. As such, the degree of patent protection obtained in the U.S. May differ substantially from that obtained in various foreign countries. In some instances, patents have been issued in the U.S. while substantially less or no protection has been obtained in Europe or other countries.

We cannot be certain of the level of protection, if any, that will be provided by our patents. If we attempt to enforce them and they are challenged in court where our competitors may raise defenses such as invalidity, unenforceability or possession of a valid license. In addition, the type and extent of any patent claims that may be issued to us in the future are uncertain. Our patents may not contain claims that will permit us to stop competitors from using similar technology.

THE FOLLOWING RISKS RELATE PRINCIPALLY TO OUR COMMON STOCK AND ITS MARKET VALUE:

THERE IS A LIMITED MARKET FOR OUR COMMON STOCK WHICH MAY MAKE IT MORE DIFFICULT FOR YOU TO DISPOSE OF YOUR STOCK

Our common stock is quoted on the OTC Bulletin Board under the symbol "XSNX." There is a limited trading market for our common stock. Accordingly, there can be no assurance as to the liquidity of any markets that may develop for our common stock, the ability of holders of our common stock to sell our common stock, or the prices at which holders may be able to sell our common stock.

OUR STOCK PRICE MAY BE VOLATILE

The market price of our common stock is likely to be highly volatile and could fluctuate widely in price in response to various factors, many of which are beyond our control, including:

- o technological innovations or new products and services by us or our competitors;
- o additions or departures of key personnel;
- o sales of our common stock;
- o our ability to integrate operations, technology, products and services;

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- o our ability to execute our business plan;
- o operating results below expectations;
- o loss of any strategic relationship;
- o industry developments;
- o economic and other external factors; and
- o period-to-period fluctuations in our financial results.

Because we have a limited operating history with limited revenues to date, you may consider any one of these factors to be material. Our stock price may fluctuate widely as a result of any of the above listed factors.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These market fluctuations may also materially and adversely affect the market price of our common stock.

WE HAVE NOT PAID DIVIDENDS IN THE PAST AND DO NOT EXPECT TO PAY DIVIDENDS IN THE FUTURE. ANY RETURN ON INVESTMENT MAY BE LIMITED TO THE VALUE OF OUR COMMON STOCK

We have never paid cash dividends on our common stock and do not anticipate paying cash dividends in the foreseeable future. The payment of dividends on our common stock will depend on earnings, financial condition and other business and economic factors affecting it at such time as the board of directors may consider relevant. If we do not pay dividends, our common stock may be less valuable because a return on your investment will only occur if its stock price appreciates.

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Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS - None.

Item 3. DEFAULTS UPON SENIOR SECURITIES - None.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS - None.

Item 5. OTHER INFORMATION - None

Item 6. EXHIBITS - 31 Sarbanes-Oxley Certification  
32 Sarbanes-Oxley Certification

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: May 15, 2007

XSUNX, INC.

By: /s/ Tom M. Djokovich

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Tom M. Djokovich, Chief Executive  
Officer, President