CYANOTECH CORP
Form 10-K/A
June 21, 2018

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

FORM 10-K/A

AMENDMENT No. 1

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

For the Fiscal Year Ended March 31, 2018

Commission File Number 0-14602

CYANOTECH CORPORATION

(Exact name of registrant as specified in its charter)

Nevada	**91-1206026**
(State or other jurisdiction of incorporation or organization)	(I. R. S. Employer Identification No.)

73-4460 Queen Kaahumanu Highway, Suite 102, Kailua-Kona, Hawaii	**96740**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: **(808) 326-1353**

Securities registered pursuant to Section 12(b) of the Act:	Name of each exchange on which registered:
None	**NASDAQ Capital Market**

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

Common Stock, $0.02 par value
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§229.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	(Do not check if a smaller reporting company)
	Smaller reporting company
	Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The aggregate market value of the Registrant's Common Stock held by non-affiliates of the Registrant on September 30, 2017 was approximately $18,602,266 based on the closing sale price of the Common Stock on the NASDAQ Capital Market on that date.

Number of shares outstanding of Registrant's Common Stock at June 20, 2018 was 5,772,032.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement for its 2018 Annual Meeting of Stockholders, expected to be filed with the Securities and Exchange Commission on or prior to July 9, 2018 and to be used in connection with the Annual Meeting of Stockholders expected to be held on August 27, 2018, are incorporated by reference in Part III of this Form 10-K.

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EXPLANATORY NOTE

This Amendment No. 1 on Form 10-K/A (this “Amendment”) amends our Annual Report on Form 10-K for the fiscal year ended March 31, 2018, originally filed with the Securities and Exchange Commission on June 15, 2018 (the “Original Filing”). We are filing this Amendment to amend and restate Part II, Item 8 of the Original Filing to correct typographical errors in the REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM. The dates referenced in the Original filing's REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM - Opinion on the financial statements - as December 31, 2018 and 2017 have been amended to show March 31, 2018 and 2017.

In addition, as required by Rule 12b-5 under the Securities Exchange Act of 1934, as amended, new certifications by our principle executive officer and our principle financial officer are filed as exhibits to this amendment.

Except as described above, no other changes have been made to the Original Filing. The Original Filing continues to speak as of the date of the Original Filing, and we have not updated the disclosures contained therein to reflect any events which occurred at a date subsequent to the filing of the Original Filing. Accordingly, this Amendment should be read in conjunction with the Original Filing and the Company’s other filings with the SEC subsequent to the Original Filing.

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Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Stockholders

Cyanotech Corporation

Opinion on the financial statements

We have audited the accompanying consolidated balance sheets of Cyanotech Corporation (a Nevada corporation) and subsidiary (the “Company”) as of March 31, 2018 and 2017, the related consolidated statements of operations, stockholders’ equity and cash flows for each of the three years in the period ended March 31, 2018, and the related notes and schedule listed in the index appearing under Item 15(a)(2) (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of March 31, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended March 31, 2018, in conformity with accounting principles generally accepted in the United States of America.

Basis for opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ GRANT THORNTON LLP

We have served as the Company's auditor since 2009.

Newport Beach, California

June 15, 2018

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CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

March 31,

	2018	2017
	(in thousands, except share data)	
ASSETS		
Current assets:		
Cash	$1,329	$1,407
Accounts receivable, net of allowance for doubtful accounts of $27 in 2018 and $49 in 2017	2,664	2,135
Inventories, net	9,034	7,972
Deferred tax assets	—	157
Prepaid expenses and other current assets	590	565
Total current assets	13,617	12,236
Equipment and leasehold improvements, net	15,734	16,712
Restricted cash	65	—
Other assets	291	213
Total assets	$29,707	$29,161
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Line of credit	$500	$611
Current maturities of long-term debt	655	623
Customer deposits	133	119
Accounts payable	3,527	3,666
Accrued expenses	892	1,013
Total current liabilities	5,707	6,032
Long-term debt, less current maturities	5,790	6,249
Deferred tax liabilities	—	157
Other long term liabilities	103	116
Total liabilities	11,600	12,554
Commitments and contingencies		
Stockholders' equity:		
Preferred stock of $0.01 par value, authorized 10,000,000 shares; no shares issued and outstanding	—	—
Common stock of $0.02 par value, authorized 50,000,000 shares; issued and outstanding 5,772,032 shares at March 31, 2018 and 5,685,381 shares at March 31, 2017	115	114

Additional paid-in capital	32,051	31,577
Accumulated deficit	(14,059)	(15,084)
Total stockholders’ equity	18,107	16,607
Total liabilities and stockholders’ equity	$29,707	$29,161

See accompanying notes to consolidated financial statements

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CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended March 31,

	2018	**2017**	**2016**
	(in thousands, except per share data)		
Net sales	$34,115	$32,042	$31,840
Cost of sales	20,744	19,818	19,974
Gross profit	13,371	12,224	11,866
Operating expenses:			
General and administrative	4,956	6,054	5,796
Sales and marketing	6,438	6,259	6,222
Research and development	563	593	633
Total operating expense	11,957	12,906	12,651
Income (loss) from operations	1,414	(682)	(785)
Other expense:			
Interest expense, net	(499)	(528)	(282)
Total other expense, net	(499)	(528)	(282)
Income (loss) before income taxes	915	(1,210)	(1,067)
Income tax benefit (expense)	110	(5)	(3,328)
Net income (loss)	$1,025	$(1,215)	$(4,395)
Net income (loss) per share:			
Basic	$0.18	$(0.21)	$(0.79)
Diluted	$0.18	$(0.21)	$(0.79)
Shares used in calculation of net income (loss) per share:			
Basic	5,709	5,658	5,581
Diluted	5,781	5,658	5,581

See accompanying notes to consolidated financial statements

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CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years ended March 31, 2018, 2017 and 2016

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
	(in thousands, except per share data)				
Balances at March 31, 2015	5,564,799	$ 111	$ 30,846	$ (9,474)	$ 21,483
Issuances of common stock for Director Stock Grants	13,198	—	78	—	78
Issuance of common stock for exercise of stock options for cash	21,800	1	74	—	75
Compensation expense related to stock options	—	—	587	—	587
Net loss	—	—	—	(4,395)	(4,395)
Balances at March 31, 2016	5,599,797	112	31,585	(13,869)	17,828
Issuances of common stock for Director Stock Grants	19,117	—	78	—	78
Issuance of common stock for exercise of stock options for cash	18,000	1	50	—	51
Issuance of common stock in connection with severance of former executive	77,500	1	(1)	—	—
Shares withheld from former executive for tax payments	(29,033)	(1)	(146)	—	(147)
Settlement agreement with former executive			(140)	—	(140)
Compensation expense related to stock options	—	1	151	—	152
Net loss	—	—	—	(1,215)	(1,215)
Balances at March 31, 2017	5,685,381	114	31,577	(15,084)	16,607
Issuances of common stock for Director Stock Grants	57,501	1	275	—	276
Issuance of common stock for exercise of stock options for cash	29,150	—	75	—	75
Compensation expense related to stock options	—	—	124	—	124
Net income	—	—	—	1,025	1,025
Balances at March 31, 2018	5,772,032	$ 115	$ 32,051	$ (14,059)	$ 18,107

See accompanying notes to consolidated financial statements

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CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended March 31,

	2018	**2017**	**2016**
	(in thousands)		
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (loss)	$1,025	$(1,215)	$(4,395)
Adjustments to reconcile net income (loss) to cash provided by operating activities:			
Loss on sale or disposal of assets	106	63	11
Depreciation and amortization	1,877	1,978	1,520
Amortization of debt issue costs and other assets	72	67	57
Share based compensation expense	400	232	665
Provision for doubtful accounts	—	—	130
Deferred income tax expense	—	—	3,350
Net (increase) decrease in assets:			
Accounts receivable	(529)	848	145
Inventories	(1,062)	(116)	(2,149)
Prepaid expenses and other assets	(139)	27	(39)
Net increase (decrease) in liabilities:			
Customer deposits	13	2	86
Accounts payable	(139)	(334)	1,036
Accrued expenses	(121)	(417)	306
Deferred rent and other liabilities	(13)	85	22
Net cash provided by operating activities	1,490	1,220	745
CASH FLOWS FROM INVESTING ACTIVITIES:			
Investment in equipment and leasehold improvements	(1,005)	(847)	(4,303)
Investment in restricted cash	(65)	—	486
Net cash used in investing activities	(1,070)	(847)	(3,817)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from short term notes payable	—	600	500
Net (payments) draws on line of credit	(111)	611	—
Payment of short term notes payable	—	(600)	(500)
Proceeds from long-term debt, net of costs	166	—	2,407
Payments on capitalized leases	(90)	(77)	(44)
Principal payments on long-term debt	(538)	(504)	(352)
Shares withheld from former executive for tax payments	—	(147)	—

Settlement agreement with former executive	—	(140)	—
Proceeds from issuance of common stock and exercise of stock options	75	51	75
Net cash (used in) provided by financing activities	(498)	(206)	2,086
Net increase (decrease) in cash	(78)	167	(986)
Cash at beginning of year	1,407	1,240	2,226
Cash at end of year	$1,329	$1,407	$1,240

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid during the year for:			
Interest	$413	$431	$362
Income taxes	$—	$—	$47

See accompanying notes to consolidated financial statements

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CYANOTECH CORPORATION AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Description of Business and Summary of Accounting Policies

Description of Business

Cyanotech Corporation (the “Company”) cultivates and produces high-value, high-quality natural products derived from microalgae for the nutritional supplements market. The Company currently cultivates, on a large-scale basis, two microalgal species from which its two major product lines are derived. The Company manufactures all of its products in the United States and sells its products worldwide. As the Company’s operations are solely related to microalgae-based products, management of the Company considers its operations to be in one industry segment. Correspondingly, the Company records revenue and cost of sales information by product category.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The accompanying consolidated financial statements include the accounts of Cyanotech Corporation and its wholly owned subsidiary, Nutrex Hawaii, Inc. (“Nutrex Hawaii” or “Nutrex”). All significant intercompany balances and transactions have been eliminated in consolidation.

Liquidity

As of March 31, 2018, the Company had cash of $1.3 million and working capital of $7.9 million compared to $1.4 million and $6.2 million, respectively, at March 31, 2017. On August 30, 2016, the Credit Agreement, which the Company and First Foundation Bank (the Bank) entered into on June 3, 2016, became effective. The Credit Agreement allows the Company to borrow up to $2.0 million on a revolving basis. At March 31, 2018, the Company had borrowed $0.5 million and had $1.5 million available on the line. On May 29, 2018, the Company borrowed $0.5 million and had $1.0 million available on the line. The line of credit was renewed on August 30, 2017 and will expire on August 30, 2018, the Company intends to renew or replace it with another line of credit on or before the expiration date.

As of March 31, 2018, the Company had $6.4 million of term loans payable to the Bank that require the payment of principal and interest monthly through August 2032. Pursuant to the term loans, the Company is subject to annual financial covenants, customary affirmative and negative covenants and certain subjective acceleration clauses. The Company was in compliance with these financial covenants at March 31, 2018. At March 31, 2017, the Company's current ratio of 1.92:1, fell short of the Bank's annual requirement of 2.10:1. The Bank provided the Company with a letter stating they found the Company to be in compliance with this covenant requirement and all other financial covenants as of March 31, 2017, and did not consider this shortfall to be a default under the Loan Agreements.

Funds generated by operating activities and available cash continue to be the Company's most significant sources of liquidity for working capital requirements, debt service and funding of maintenance levels of capital expenditures. Based upon the Company's fiscal 2019 operating plan and related cash flow projections and the Company's projected consolidated financial position as of March 31, 2019, cash flows expected to be generated by operating activities and available financing are expected to be sufficient to fund the Company's operations for at least the next twelve months, and the Company's current ratio is expected to be in compliance with the annual term loan covenant requirement as of March 31, 2019. However, no assurances can be provided that the Company will achieve its operating plan and cash flow objectives for the next fiscal year or its projected consolidated financial position as of March 31, 2019. Such estimates are subject to change based on future results and such change could cause future results to vary significantly from expected results.

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Estimates and Assumptions

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of any contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the period reported. Management reviews these estimates and assumptions periodically and reflects the effect of revisions in the period that they are determined to be necessary. Actual results could differ significantly from those estimates and assumptions. Significant estimates include forecast of future operating results, cash flows and financial position, inventory valuation and determination of production capacity and abnormal product costs, reserve for inventory, sales allowances, allowance for doubtful accounts and valuation of deferred tax assets.

Financial Instruments

Cash primarily consists of cash on hand and cash in bank deposits.

The Company applies a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 —	Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.
Level 2 —	Inputs to the valuation methodology include:

Quoted prices for similar assets or liabilities in active markets;
Quoted prices for identical or similar assets or liabilities in inactive markets;
Inputs other than quoted prices that are observable for the asset or liability; and
Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 – Inputs to the valuation methodology are unobservable and significant to the fair value.

Cash, Accounts Receivable, Accounts Payable and Accrued Expenses - Due to the short-term nature of these instruments, management believes that the carrying amounts approximate fair value.

Line of Credit and Long-Term Debt - The carrying amount of our line of credit and long-term debt approximates fair value as interest rates applied to the underlying debt are adjusted quarterly to market interest rates, which approximate current interest rates for similar debt instruments of comparable maturities.

Concentration of Credit Risk

The Company maintains its cash accounts with several banks located in Hawaii. The total cash balances are insured by the Federal Deposit Insurance Corporation (“FDIC”) up to $250,000 per bank. The Company had cash balances at March 31, 2018 that exceeded the balance insured by the FDIC by $829,000. Two customers accounted for 32% and 16%, respectively, of our total net sales in the fiscal year ended March 31, 2018. Three customers accounted for 77% of accounts receivable at March 31, 2018. One customer accounted for 24% of total net sales in the fiscal year ended March 31, 2017. Three customers accounted for 60% of accounts receivable at March 31, 2017. Two customers accounted for 19% and 11%, respectively, of total net sales in the fiscal year ended March 31, 2016. Two customers accounted for 44% of accounts receivable at March 31, 2016. Our top ten customers generated 70%, 60% and 58% of our net sales during fiscal 2018, fiscal 2017 and fiscal 2016, respectively.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded at the invoiced amount and do not accrue interest. Credit is extended based on evaluation of the customer's financial condition. Collateral is not required. The allowance for doubtful accounts reflects management's best estimate of probable credit losses inherent in the accounts receivable balance. Management determines the allowance based on historical experience, specifically identified nonpaying accounts and other currently available evidence. Management reviews its allowance for doubtful accounts monthly with a focus on significant individual past due balances over 90 days. All other balances are reviewed on a pooled basis. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance sheet credit exposure related to its customers or otherwise.

Inventories, net

Inventories are stated at the lower of cost or net realizable value. Cost is determined using the first-in, first-out (FIFO) method. Net realizable value is defined as sales price less cost to dispose and a normal profit margin. Inventory costs include materials, labor, overhead and third party costs.

Management provides a reserve against inventory for known or expected inventory obsolescence. The reserve is determined by specific review of inventory items for product age and quality which may affect salability. At March 31, 2018 and 2017, the inventory reserve was $5,000 and $3,000, respectively.

The Company recognizes abnormal production costs, including fixed cost variances from normal production capacity, as an expense in the period incurred. Abnormal amounts of freight, handling costs and wasted material (spoilage) are recognized as current period charges and fixed production overhead costs are allocated to inventory based on the normal capacity of production facilities. Normal capacity is defined as "the production expected to be achieved over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance." The Company expensed abnormal production costs of $538,000, $120,000 and $395,000 to cost of sales for the fiscal years ended March 31, 2018, 2017 and 2016, respectively. Non-inventoriable fixed costs were $271,000, $134,000 and $149,000 for the fiscal years ended March 31, 2018, 2017 and 2016, respectively, and have been included in cost of sales.

Equipment and Leasehold Improvements, net

Equipment and leasehold improvements are stated at cost. Depreciation and amortization are provided using the straight-line method over the estimated useful lives for equipment and furniture and fixtures, and the shorter of the land lease term (see Notes 3 and 6) or estimated useful lives for leasehold improvements as follows:

Equipment (in years)	3	to	10
Furniture and fixtures (in years)	3	to	7
Leasehold improvements (in years)	10	to	25

Capital project costs are accumulated in construction-in-progress until completed, at which time the costs are transferred to the relevant asset and commence depreciation. Repairs and Maintenance costs are expensed in the period incurred. Repairs and maintenance that significantly increase the useful life or value of the asset are capitalized and depreciated over the remaining life of the asset. The Company capitalizes interest cost incurred on funds used to construct property, plant, and equipment. The capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life.

Impairment of Long-Lived Assets

Management reviews long-lived assets, such as equipment, leasehold improvements and purchased intangibles subject to amortization for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized to the extent that the carrying amount exceeds the asset's fair value. Assets to be disposed of and related liabilities would be separately presented in the consolidated balance sheet. Assets to be disposed of would be reported at the lower of the carrying value or fair value less costs to sell and would not be depreciated.

Accounting for Asset Retirement Obligations

Management evaluates quarterly the potential liability for asset retirement obligations under the Company's lease for its principal facility and corporate headquarters. No liability has been recognized as of March 31, 2018 and 2017 (see Note 7).

Revenue Recognition

We recognize revenues when the customer takes ownership and assumes the risk of loss. We have determined that transfer of title and risk of loss generally occurs when product is received by the customer, except in instances where the shipment terms are explicitly FOB Origin, and accordingly we recognize revenue at the point of delivery to the customer. For shipments with terms of FOB Origin where transfer of title and risk of loss occurs at the point of shipping, revenue is recognized upon shipment to the customer. Sales returns and allowances are estimated and recorded as a reduction to sales in the period in which sales are recorded. We record net shipping charges and sales tax in cost of goods sold.

Research and Development

Research and development costs are expensed as incurred and consist primarily of labor, benefits and outside research.

Advertising

Advertising costs are expensed as incurred. Total advertising expense for the years ended March 31, 2018, 2017 and 2016 was $1,548,000, $813,000 and $942,000, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. The asset and liability method requires the recognition of deferred tax assets and liabilities for the expected future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using income tax rates applicable to the period in which the tax difference is expected to reverse.

Judgment is required in determining any valuation allowance recorded against deferred tax assets, specifically net operating loss carryforwards, tax credit carryforwards and deductible temporary differences that may reduce taxable income in future periods. In assessing the need for a valuation allowance, we consider all available evidence including past operating results, estimates of future taxable income and tax planning opportunities. In the event we change our determination as to the amount of deferred tax assets that can be realized, we will adjust our valuation allowance with a corresponding impact to income tax expense in the period in which such determination is made.

In evaluating a tax position for recognition, management evaluates whether it is more-likely-than-not that a position will be sustained upon examination, including resolution of related appeals or litigation processes, based on the technical merits of the position. If the tax position meets the more-likely-than-not recognition threshold, the tax position is measured and recognized in the Company’s financial statements as the largest amount of tax benefit that, in management’s judgment, is greater than 50% likely of being realized upon settlement. As of March 31, 2018 and 2017, there was no significant liability for income tax associated with unrecognized tax benefits.

The Company recognizes accrued interest related to unrecognized tax benefits as well as any related penalties in interest expense in its condensed consolidated statements of operations. As of the date of adoption and during the years ended March 31, 2018, 2017 and 2016, there was no accrual for the payment of interest and penalties related to uncertain tax positions.

Share-Based Compensation

The Company accounts for share-based payment arrangements using fair value. The Company currently has no liability-classified awards. Equity-classified awards, including grants of restricted stock, restricted stock units and employee stock options, are measured at the grant-date fair value of the award and are not subsequently remeasured unless an award is modified. The cost of equity-classified awards is recognized in the statement of operations over the period during which an employee is required to provide the service in exchange for the award, or the vesting period. All of the Company's restricted stock, restricted stock units and stock options are service-based awards, and considered equity-classified awards; as such, they are reflected in Equity and Stock Compensation Expense accounts. All stock-based compensation has been classified as general and administrative expense in the consolidated statement of operations.

The Company utilizes the Black-Scholes option pricing model to determine the fair value of each option award. Expected volatilities are based on the historical volatility of the Company's common stock over a period consistent with that of the expected term of the options. The expected term of the options are estimated based on factors such as vesting periods, contractual expiration dates and historical exercise behavior. The risk-free rates for periods within the contractual life of the options are based on the yields of U.S. Treasury instruments with terms comparable to the estimated option terms.

Per Share Amounts

Basic earnings (loss) per common share is calculated by dividing net income (loss) for the year by the weighted average number of common shares outstanding during the year. Diluted earnings per common share is calculated by dividing net income for the year by the sum of the weighted average number of common shares outstanding during the year plus the number of potentially dilutive common shares ("dilutive securities") that were outstanding during the year. Dilutive securities include restricted stock units and stock options granted pursuant to the Company's stock option plans. Dilutive securities related to the Company's stock option plans are included in the calculation of diluted earnings per common share using the treasury stock method. Potentially dilutive securities are excluded from the computation of earnings per share in periods in which a net loss is reported, as their effect would be antidilutive. A reconciliation of the numerators and denominators of the basic and diluted income (loss) per common share calculations for the years ended March 31, 2018, 2017 and 2016 is presented in Note 11.

New Accounting Pronouncements

In May 2017, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2017-09, *Compensation-Stock Compensation (Topic* 718*) Scope of Modification Accounting.* ASU 2017-09 will clarify and reduce both (i) diversity in practice and (ii) cost and complexity when applying the guidance in Topic 718, to a change to the terms and conditions of a share-based payment award. This guidance will become effective for fiscal years beginning after December 15, 2017 and interim periods within those fiscal years. Early adoption is permitted. The amendments in this ASU should be applied prospectively to an award modified on or after the adoption date. The Company is currently evaluating the impact of this updated standard. The Company does not believe this update will have a significant impact on its consolidated financial statements.

In November 2016, the FASB issued ASU 2016-18, "*Statement of Cash Flows (Topic* 230*): Restricted Cash"* ("ASU No. 2016-18"). This update addresses the fact that diversity exists in the classification and presentation of changes in restricted cash on the statement of cash flows under Topic 230, Statement of Cash Flows. ASU 2016-18 will take effect for public companies for the fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. This guidance is applicable to the Company's fiscal year beginning April 1, 2018. The Company does not anticipate that this guidance will have a material impact on its consolidated financial statements and related disclosures.

In August 2016, FASB issued ASU 2016-15, "*Statement of Cash Flows (Topic* 230*)*: *Classification of Certain Cash Receipts and Cash Payments"* ("ASU No. 2016-15"). This ASU clarifies and provides specific guidance on eight cash flow classification issues that are not currently addressed by current GAAP and thereby reduces the current diversity in practice. ASU No. 2016-15 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early application permitted. This guidance is applicable to the Company's fiscal year beginning April 1, 2018. The Company does not anticipate that this guidance will have a material impact on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, "*Compensation – Stock Compensation (Topic* 718*)*: *Improvements to Employee Share-Based Payment Accounting" ("*ASU No. 2016-09*")*. This ASU makes several modifications to Topic 718 related to the accounting for forfeitures, employer tax withholding on share-based compensation, and the financial statement presentation of excess tax benefits or deficiencies. ASU No. 2016-09 also clarifies the statement of cash flows presentation for certain components of share-based awards. The standard is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods, with early adoption permitted. Amendments requiring recognition of excess tax benefits and tax deficiencies in the income statement must be applied prospectively. Amendments related to the presentation of excess tax benefits on the statement of cash flows may be applied either prospectively or retrospectively based on the Company's election. Amendments related to the statement of cash flows presentation of employee taxes paid when an employer withholds shares must be applied retrospectively. As of April 1, 2017, the Company adopted ASU 2016-09 and elected to present excess tax benefits as an operating activity prospectively and continues to estimate forfeitures rather than recognize them as they occur. The adoption of ASU 2016-09 did not have an impact on its consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, "*Leases (Topic* 842*)" ("*ASU No. 2016-02"). The principle objective of ASU No. 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet. ASU No. 2016-02 continues to retain a distinction between finance and operating leases but requires lessees to recognize a right-of-use asset representing its right to use the underlying asset for the lease term and a corresponding lease liability on the balance sheet for all leases with terms greater than twelve months. ASU No. 2016-02 is effective for fiscal years and interim periods beginning after December 15, 2018. Early adoption of ASU No. 2016-02 is permitted. Entities are required to apply the amendments at the beginning of the earliest period presented using a modified retrospective approach. This guidance is applicable to the Company's fiscal year beginning April 1, 2019. The Company expects this guidance will have a material impact on its consolidated balance sheets due to the recognition of lease rights and obligations as assets and liabilities, respectively. The Company does not expect this guidance to have a material effect on its consolidated results of operations and cash flows.

In November 2015, the FASB issued ASU No. 2015-17, "*Income Taxes (Topic* 740*): Balance Sheet Classification of Deferred Taxes"*. This guidance simplifies the presentation of deferred income taxes and requires that deferred tax assets and liabilities be classified as noncurrent in the classified statement of financial position. ASU 2015-17 will take effect for public companies for the fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. As required, the Company adopted this standard as of April 1, 2017 and accordingly all deferred tax assets and liabilities are classified as non-current. Prior periods were retrospectively adjusted.

In July 2015, the FASB issued ASU No. 2015-11, *"Inventory: Simplifying the Measurement of Inventory"*, that requires inventory not measured using either the last in, first out (LIFO) or the retail inventory method to be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable cost of completion, disposal, and transportation. Prior to the issuance of the standard, inventory was measured at the lower of cost or market (where market was defined as replacement cost, with a ceiling of net realizable value and floor of net realizable value less a normal profit margin). The new standard will be effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and will be applied prospectively. Early adoption is permitted. As required, the Company adopted this standard as of April

1, 2017. The adoption of this standard did not have a material impact on the Company's financial position or results of operations.

In May 2014, the FASB issued their converged standard on revenue recognition, Accounting Standards Update No. 2014-09, "*Revenue from Contracts with Customers (Topic 606)"*, updated in December 2016 with the release of ASU 2016-20. This standard outlines a single comprehensive model for companies to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods and services in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods and services. In addition, the new standard requires that reporting companies disclose the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. In August 2015, the FASB issued ASU No 2015-14 "*Revenue from Contracts with Customers (Topic 606*): *Deferral of the Effective Date,*" which deferred the effective date of ASU 2014-09 to annual reporting periods beginning after December 15, 2017, with earlier application permitted but not before the original effective date.

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The Company adopted ASC 606 using the modified retrospective method on April 1, 2018. The Company utilized a cross-functional team to implement the guidance related to the recognition of revenue from contracts with customers. The implementation approach included an assessment of customer contracts aimed at identifying contractual provisions that could result in a change in the timing or the amount of revenue recognized in comparison with prior guidance, as well as assessing the enhanced disclosure requirements of the new guidance. Revenues are generated through the sale of finished products, and will be recognized at the point in time when control of the merchandise is transferred to the customer and in an amount that considers the impact of estimated returns, discounts and other allowances that are variable in nature. The Company continues to implement changes to its business processes and controls to support the recognition and disclosure requirements under the new guidance. The Company has concluded that the impact of adoption of ASC 606 as of April 1, 2018 is not material to its financial statements.

Note 2 Inventories, net

Inventories consist of the following as of March 31, 2018 and 2017:

	2018	**2017**
	(in thousands)	
Raw materials	$410	$347
Work in process	2,602	2,036
Finished goods(1)	5,878	5,460
Supplies	144	129
Inventories, net	$9,034	$7,972

(1) Net of reserve for obsolescence of $5,000 and $3,000 at March 31, 2018 and 2017, respectively.

Note 3 Equipment and Leasehold Improvements, net

Equipment and leasehold improvements consists of the following as of March 31, 2018 and 2017:

	2018	**2017**
	(in thousands)	
Equipment(1)	$17,935	$17,492

Leasehold improvements	14,248	13,892
Furniture and fixtures	348	380
	32,531	31,764
Less accumulated depreciation and amortization	(17,346)	(15,835)
Construction in-progress	549	783
Equipment and leasehold improvements, net	$15,734	$16,712

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(1) Includes $373,000 of equipment under capital lease at March 31, 2018 and 2017 respectively, with accumulated amortization of $175,000 and $106,000, respectively.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. No such event occurred during the fiscal years ended March 31, 2018, 2017 and 2016. The Company recognized a loss on disposal of equipment, leasehold improvements and intangible assets in the amount of $106,000, $63,000 and $11,000 in fiscal 2018, 2017 and 2016 respectively. Depreciation and amortization expense was $1,877,000, $1,978,000 and $1,520,000 for the years ended March 31, 2018, 2017 and 2016, respectively.

The Company capitalized interest in the amount of $0, $0 and $173,000 for the fiscal years ended March 31, 2018, 2017 and 2016, respectively.

Note 4 Notes Payable

On August 30, 2016, the Revolving Credit Agreement (the "Credit Agreement"), which the Company and First Foundation Bank ("the Bank") entered into on June 3, 2016, became effective after the Company and the Bank received the necessary approvals from the State of Hawaii to secure the lien on the Company's leasehold property in Kona, Hawaii. The Credit Agreement allows the Company to borrow up to $2,000,000 on a revolving basis. Borrowings under the Credit Agreement bear interest at the Wall Street Journal prime rate (4.75% at March 31, 2018) + 2%, floating. The Credit Agreement includes various covenants as defined in the Credit Agreement. The Credit Agreement also contains standard acceleration provisions in the event of a default by the Company. At March 31, 2018, the Company had borrowed $500,000 under the Credit Agreement and had $1,500,000 available on the line. The line of credit will be subject to renewal upon expiration on August 30, 2018.

On May 29, 2018, the Company borrowed $500,000 under the Credit Agreement and had $1,000,000 available on the line.

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The Credit Agreement grants the Bank the following security interests in the Company's property: (a) a lien on the Company's leasehold interest in its Kona facility; (b) an assignment of the Company's interest in leases and rents on its Kona facility; and (c) a security interest in all fixtures, furnishings and equipment related to or used by the Company at the Kona facility. Each security interest is further subject to the terms of the Credit Agreement.

Note 5 Accrued Expenses

Components of accrued expenses as of March 31, 2018 and 2017 are as follows:

	2018	2017
	(in thousands)	
Wages, commissions, bonus and profit sharing	$707	$793
Rent and utilities	69	69
Other accrued expenses	116	151
Total accrued expenses	$892	$1,013

Note 6 Long-Term Debt

Long-term debt consists of the following as of March 31, 2018 and 2017 as follows:

	2018	2017
	(in thousands)	
Long-term debt	$6,678	$7,139
Less current maturities	(655)	(623)
Long-term debt, excluding current maturities	6,023	6,516
Less unamortized debt issuance costs	(233)	(267)
Total long-term debt, net of current maturities and unamortized debt issuance costs	$5,790	$6,249

Term Loans

The Company executed a loan agreement with a lender providing for $2,500,000 in aggregate credit facilities (the "2015 Loan") secured by substantially all the Company's assets, pursuant to a Term Loan Agreement dated July 30, 2015 (the “2015 Loan Agreement”). The 2015 Loan Agreement is evidenced by a promissory note in the amount of $2,500,000, the repayment of which is partially guaranteed under the provisions of a United States Department of Agriculture (“USDA”) Rural Development Guarantee program. The proceeds of the 2015 Loan were used to pay off a $500,000 short term note payable that matured on September 18, 2015, acquire new processing equipment and leasehold improvements at the Company’s Kona, Hawaii facility.

The provisions of the 2015 Loan require the payment of principal and interest until its maturity on September 1, 2022, the obligation fully amortizes over seven (7) years. Interest on the 2015 Loan accrues on the outstanding principal balance at an annual variable rate equal to the published Wall Street Journal prime rate (4.75% at March 31, 2018) plus 2.0% and is adjustable on the first day of each calendar quarter and fixed for that quarter. At no time shall the annual interest rate be less than 6.00%. The 2015 Loan has a prepayment penalty of 5% for any prepayment made prior to the first anniversary of the date of the 2015 Loan Agreement, which penalty is reduced by 1% each year thereafter until the fifth anniversary of such date, after which there is no prepayment penalty. The balance under the 2015 Loan was $1,726,000 and $2,049,000 at March 31, 2018 and 2017, respectively.

The 2015 Loan includes a one-time origination and guaranty fee totaling $113,900 and an annual renewal fee payable in the amount of 0.50% of the USDA guaranteed portion of the outstanding principal balance as of December 31 of each year, beginning December 31, 2015. The USDA has guaranteed 80% of all amounts owing under the 2015 Loan. The Company is subject to financial covenants and customary affirmative and negative covenants. The Company was in compliance with these financial covenants at March 31, 2018.

The Company executed a loan agreement with a lender providing for $5,500,000 in aggregate credit facilities (the “Loan”) secured by substantially all the Company’s assets, including a mortgage on the Company's interest in its lease at the National Energy Laboratory of Hawaii Authority, pursuant to a Term Loan Agreement dated August 14, 2012 (the “Loan Agreement”). The Loan Agreement is evidenced by promissory notes in the amounts of $2,250,000 and $3,250,000, the repayment of which is partially guaranteed under the provisions of a USDA Rural Development Guarantee. The proceeds of the Loan were used to acquire processing equipment and leasehold improvements at its Kona, Hawaii facility.

The provisions of the Loan required the payment of interest only for the first 12 months of the term; thereafter, and until its maturity on August 14, 2032, the obligation fully amortizes over nineteen (19) years. Interest on the Loan accrues on the outstanding principal balance at an annual variable rate equal to the published Wall Street Journal prime rate (4.75% at March 31, 2018) plus 1.0% and is adjustable on the first day of each calendar quarter and fixed for that quarter. At no time shall the annual interest rate be less than 5.50%. The balance under this Loan was $4,648,000 and $4,854,000 at March 31, 2018 and 2017, respectively.

The Loan included a one-time origination and guaranty fees totaling $214,500 and an annual renewal fee payable in the amount of 0.25% of the USDA guaranteed portion of the outstanding principal balance as of December 31 of each year, beginning December 31, 2012. The USDA has guaranteed 80% of all amounts owing under the Loan. The Company is subject to financial covenants and customary affirmative and negative covenants. The Company was in compliance with these financial covenants at March 31, 2018.

On October 6, 2017, the Company entered into an Equipment Finance Agreement (the “Equipment Agreement”) with a lender, which provides up to $175,000 of financing for equipment. The interest rate on this loan is 4.75%. The provisions of the Equipment Agreement require the payment of principal and interest until its maturity on October 31, 2022, the obligation fully amortizes over five (5) years. The balance under this loan was $156,000 at March 31, 2018. $65,000 of the proceeds from this loan are classified as restricted cash until drawn upon to acquire the equipment.

Capital Leases

In August 2016, the Company executed a capital lease agreement with Thermo Fisher Financial providing for $52,000 in equipment, secured by the equipment financed. The capital lease matures in May 2019 and is payable in 36 equal monthly payments. The interest rate under this capital lease is 12.90%. The balance under this lease was $28,000 and $43,000 at March 31, 2018 and 2017, respectively.

In February 2016, the Company executed a capital lease agreement with Bank of the West providing for $51,000 in equipment, secured by the equipment financed. The capital lease matures in March 2021 and is payable in 60 equal monthly payments. The interest rate under this capital lease is 4.18%. The balance under this lease was $32,000 and $42,000 at March 31, 2018 and March 31, 2017, respectively.

In July 2015, the Company executed a capital lease agreement with Huntington Technology Finance providing for $174,000 in equipment, secured by the equipment financed. The capital lease matures in July 2020 and is payable in 60 equal monthly payments. The interest rate under this capital lease is 6.57%. The balance under this lease was $88,000 and $121,000 at March 31, 2018 and March 31, 2017, respectively.

In March 2015, the Company executed a capital lease agreement with Thermo Fisher Financial providing for $86,000 in equipment, secured by the equipment financed. The capital lease matures in March 2018 and is payable in 36 equal monthly payments. The interest rate under this capital lease is 6.5%. The balance under this lease was $0 and $30,000 at March 31, 2018 and 2017, respectively.

Future principal payments under the loan and capital lease agreements as of March 31, 2018 are as follows:

Year ending March 31	**(in thousands)**
2019	$ 655
2020	682
2021	690
2022	707
2023	513
Thereafter	3,431
Total principal payments	$ 6,678

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Note 7 Leases

The Company's principal facility and its corporate headquarters are located at the Natural Energy Laboratory of Hawaii Authority ("NELHA") at Keahole Point in Kailua-Kona, Hawaii. The property is leased from the State of Hawaii under a 40-year commercial lease expiring in 2035. Under the terms of the existing NELHA lease, the Company could be required to remove improvements at the end of the lease term. Under generally accepted accounting principles in the United States, an entity should recognize the fair value of a liability for an asset retirement obligation in the period in which the retirement obligation is incurred, if a reasonable estimate of fair value can be made. If such an estimate cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when the fair value can be reasonably estimated. Based on communications with NELHA, management does not believe the projected cost for such removal to be material to the consolidated financial statements, or likely, given historical practices. However, conditions could change in the future. It is not possible to predict such changes or estimate any impact thereof.

The Company leases facilities, equipment and land under operating leases expiring through 2035. The land lease provides for contingent rentals in excess of minimum rental commitments based on a percentage of the Company's sales. Contingent rental payments for the years ended March 31, 2018, 2017 and 2016 were $49,000, $80,000 and $65,000, respectively.

Future minimum lease payments under non-cancelable operating leases at March 31, 2018 are as follows:

Year ending March 31	**(in thousands)**
2019	$ 626
2020	636
2021	536
2022	535
2023	456
Thereafter	3,815
Total minimum lease payments	$ 6,604

Rent expense, including contingent rent, under operating leases amounted to $578,000, $605,000 and $622,000 for the years ended March 31, 2018, 2017 and 2016, respectively.

Note 8 Other Commitments and Contingencies

From time to time, the Company may become party to lawsuits and claims that arise in the ordinary course of business relating to employment, intellectual property, and other matters. There were no significant legal matters outstanding at March 31, 2018.

As of March 31, 2018, the Company has entered into purchase obligations of $449,000, including agreements to purchase goods or services that are enforceable, are legally binding and specify all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Purchase obligations do not include agreements that are cancelable without penalty.

Note 9 Share-Based Compensation

As of March 31, 2018, the Company had two equity-based compensation plans: the 2016 Equity Incentive Plan (the 2016 Plan) and the 2014 Independent Director Stock Option and Restricted Stock Grant Plan (the “2014 Directors Plan”). The Company has also issued stock options, which remain outstanding as of March 31, 2018, under two equity-based compensation plans which have expired according to their terms: the 2005 Stock Option Plan (the “2005 Plan”) and the 2004 Independent Director Stock Option and Stock Grant Plan (the “2004 Directors Plan”). These plans allowed the Company to award stock options and shares of restricted common stock to eligible employees, certain outside consultants and independent directors. No additional awards will be issued under the 2005 Plan or the 2004 Directors Plan.

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On August 25, 2016, the Company's shareholders approved the 2016 Plan as a successor to the 2005 Plan, authorizing the Board of Directors to provide incentive to the Company's officers, employees and certain independent consultants through equity based compensation in the form of stock options, restricted stock, restricted stock units, stock appreciation rights and other stock based awards (together, "Stock Awards") and performance shares and performance units (together, "Performance Awards"). Awards under the 2016 Plan are limited to the authorized amount of 1,300,000 shares, up to 600,000 of which are available for issuance in connection with Performance Awards and Stock Awards. As of March 31, 2018, there were 1,131,992 shares available for grant under the 2016 Plan.

On August 28, 2014, the Company's shareholders approved the 2014 Directors Plan authorizing the Board of Directors to provide incentive to the Company's independent directors through equity based compensation in the form of stock options and restricted stock. Awards under the 2014 Directors Plan are limited to the authorized amount of 350,000 shares. As of March 31, 2018, there were 231,623 shares available for grant under the 2014 Directors Plan.

The following table presents shares authorized, available for future grant and outstanding under each of the Company's plans:

	As of March 31, 2018		
	Authorized	**Available**	**Outstanding**
2016 Plan	1,300,000	1,131,992	159,675
2014 Directors Plan	350,000	231,623	12,000
2005 Plan	—	—	445,400
2004 Directors Plan	—	—	12,000
Total	1,650,000	1,363,615	629,075

Stock Options

All stock option grants made under the equity-based compensation plans were issued at exercise prices no less than the Company's closing stock price on the date of grant. Options under the 2016 Plan, 2005 Plan and 2014 Directors Plan were determined by the Board of Directors or the Compensation Committee of the Board of Directors in accordance with the provisions of the respective plans. The terms of each option grant include vesting, exercise, and other conditions are set forth in a Stock Option Agreement evidencing each grant. No option can have a life in excess of ten (10) years. The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes option-pricing model. The model requires various assumptions, including a risk-free interest rate, the expected term of the options, the expected stock price volatility over the expected term of the options, and the expected dividend yield. Compensation expense for employee stock options is recognized ratably over the vesting term. Compensation expense recognized for options issued under the Plans was $62,000, $154,000 and $587,000 for the years ended March 31, 2018, 2017 and 2016, respectively.

A summary of option activity under the Company's stock plans for the years ended March 31, 2018, 2017 and 2016 is presented below:

Option Activity	**Shares**	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Term**	**Aggregate Intrinsic Value**
			(in years)	
Outstanding at March 31, 2015	1,433,216	$ 4.08	6.4	$6,221,909
Granted	6,000	5.91		
Exercised	(21,800)	3.26		
Forfeited	(732,416)	3.59		
Outstanding at March 31, 2016	685,000	$ 4.65	5.7	$566,323
Granted	6,000	4.08		
Exercised	(18,000)	2.77		
Forfeited	(170,000)	6.44		
Outstanding at March 31, 2017	503,000	$ 4.10	4.7	$145,946
Granted	120,000	3.53		
Exercised	(29,150)	2.59		
Forfeited	(3,700)	4.50		
Expired	(750)	1.60		
Outstanding at March 31, 2018	589,400	$ 4.06	4.9	$675,300
Exercisable at March 31, 2018	469,400	$ 4.20	3.8	$486,900

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The aggregate intrinsic value in the table above is before applicable income taxes and represents the excess amount over the exercise price optionees would have received if all options had been exercised on the last business day of the period indicated, based on the Company's closing stock price of $5.10, $3.85, $4.98 and $8.42 at March 31, 2018, 2017, 2016 and 2015 respectively. The total intrinsic value of stock options exercised during fiscal years 2018, 2017 and 2016 were $67,000, $23,000 and $58,000, respectively.

A summary of the Company's non-vested options for the year ended March 31, 2018 is presented below:

Nonvested Options	**Shares**	**Weighted Average Grant-Date Fair Value**
Nonvested at March 31, 2017	19,500	$ 2.93
Granted	120,000	1.81
Vested	(19,500)	2.93
Nonvested at March 31, 2018	120,000	$ 1.81

The weighted average grant-date fair value of stock options granted during fiscal years 2018, 2017 and 2016 was $67,000, $5,000 and $7,000, respectively. The total grant-date fair values of stock options that vested during fiscal years 2018, 2017 and 2016 were $57,000, $332,000 and $651,000, respectively.

The following table summarizes the weighted average characteristics of outstanding stock options as of March 31, 2018:

	Outstanding Options			**Exercisable Options**	
Range of Exercise Prices	**Number of Shares**	**Remaining Life (Years)**	**Weighted Average Exercise Price**	**Number of Shares**	**Weighted Average Exercise Price**
$1.60-$3.70	172,200	5.3	$ 3.05	97,200	$ 2.81
$3.71-$4.42	239,700	4.7	$ 3.83	194,700	$ 3.83
$4.43-$5.40	95,000	5.2	$ 5.00	95,500	$ 5.00
$5.41-$7.08	82,500	4.6	$ 5.77	82,500	$ 5.77
Total stock options	589,400	4.9	$ 4.06	469,400	$ 4.20

The range of fair value assumptions related to options granted during the years ended March 31, 2018, 2017 and 2016 were as follows:

	2018	2017	2016
Exercise Price	$3.83	$4.08	$5.91
Volatility	51.91 %	51.13 %	50.00 %
Risk Free Rate	2.50 %	0.60 %	0.22 %
Vesting Period (in years)	3.0	0.5	0.5
Forfeiture Rate	0.00 %	0.00 %	0.00 %
Expected Life (in years)	6.00	1.00	1.00
Dividend Rate	0 %	0 %	0 %

As of March 31, 2018, total unrecognized stock-based compensation expense related to all unvested stock options was $181,000, which is expected to be expensed over a weighted average period of 2.3 years.

Restricted Stock

Grants of fully vested restricted stock issued to Non-Employee Directors was 57,501, 19,117 and 13,198 shares for the three years ended March 31, 2018, 2017 and 2016, respectively. Compensation expense recognized for fully vested restricted stock grants issued under the 2014 Directors Plan was $276,000, $78,000 and $78,000 for the three years ended March 31, 2018, 2017 and 2016, respectively.

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Restricted Stock Units ("RSUs")

RSUs are service-based awards granted to eligible employees under our 2016 Plan. Compensation expense recognized for RSUs issued under the 2016 Plan was $62,000, $0 and $0 for the years ended March 31, 2018, 2017 and 2016, respectively.

The following table summarizes information related to awarded RSUs:

Nonvested Restricted Stock Units	Shares	Weighted Average Grant Price
Nonvested restricted stock units at March 31, 2017	25,000	$ 3.85
Granted	28,074	$ 3.92
Vested	(8,333)	$ 3.85
Exercised	—	$ —
Forfeited	(5,066)	$ 3.92
Nonvested restricted stock units at March 31, 2018	39,675	$ 3.89

As of March 31, 2018, total unrecognized stock-based compensation expense related to unvested restricted stock units was $122,730.

On April 5, 2018, 1,474 RSUs were awarded to employees of the Company. This award is valued at $5.25 per share, the closing market price of Cyanotech common stock on the grant date, and vests over a period of two years.

Note 10 Common and Preferred Stock

The Company has authorized a total of sixty million shares of which fifty million shares are authorized common stock and ten million shares are authorized preferred stock. None of the preferred stock was issued or outstanding at March 31, 2018 and 2017. Under the terms of the Company's Amended and Restated Articles of Incorporation, the Board of Directors is authorized to determine or alter the rights, preferences, privileges and restrictions of the Company's authorized but unissued shares of preferred stock.

Note 11 Earnings (Loss) Per Share

Basic earnings (loss) per share is computed on the basis of the weighted average number of common shares outstanding. Diluted earnings per share is computed on the basis of the weighted average number of common shares outstanding plus the potentially dilutive effect of outstanding stock options using the treasury stock method.

Reconciliations between the numerator and the denominator of the basic and diluted income (loss) per share computations for the years ended March 31, 2018, 2017 and 2016 are as follows:

	Net Income (loss) (Numerator)	**Shares (Denominator)**	**Per Share Amount**
	(in thousands, except per share amounts)		
Year ended March 31, 2018:			
Basic income per share	$1,025	5,709	$ 0.18
Effective dilutive securities—Common stock options	—	72	—
Diluted income per share	$1,025	5,781	$ 0.18
Year ended March 31, 2017:			
Basic and diluted loss per share	$(1,215)	5,658	$ (0.21)
Year ended March 31, 2016:			
Basic and diluted loss per share	$(4,395)	5,581	$ (0.79)

Basic and diluted per share amounts are the same in periods of a net loss, because common share equivalents are anti-dilutive when a net loss is recorded. Diluted earnings per share does not include the impact of common stock options totaling 120,000, 6,000 and 58,000 for the fiscal years ending March 31, 2018, 2017 and 2016, respectively, as the effect of their inclusion would be anti-dilutive. Restricted stock units become dilutive within the period granted and remain dilutive until the units vest and are issued as common stock. Diluted earnings per share does not include the impact of restricted stock units totaling 39,675 and 25,000 for the fiscal years ending March 31, 2018 and 2017, as the effect of their inclusion would be anti-dilutive.

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Note 12 Profit Sharing Plan and 401k Plan

The Company sponsors a profit sharing plan for all employees not covered under a separate management incentive plan. Under the profit sharing plan, a percentage determined by the Board of Directors of pre-tax profits on a quarterly basis may be allocated to non-management employees at management's discretion. The profit sharing bonus may be distributed all in cash on an after-tax basis or distributed half in cash (on an after-tax basis) and the remainder deposited in an employee's 401(k) account on a pre-tax basis. Employees may also make voluntary pre-tax contributions to their 401(k) accounts. Compensation expense under this plan was approximately $91,000, $4,000 and $0 for the fiscal years ended March 31, 2018, 2017 and 2016, respectively. Additionally, the Company makes a retirement contribution to all employees individual 401(k) accounts equal to two percent of each employee's base pay for each bi-weekly pay period on a pre-tax basis. Retirement expense under this plan was approximately $117,000, $139,000 and $147,000 for fiscal years ended March 31, 2018, 2017 and 2016, respectively.

Note 13 Product Line and Geographic Information

Net sales by product line for the years 2018, 2017 and 2016 are as follows:

	2018	**2017**	**2016**
	(in thousands)		
Net sales:			
Natural astaxanthin products			
BioAstin®	$21,650	$19,357	$19,829
Spirulina products			
Spirulina Pacifica®	12,465	12,685	12,011
	$34,115	$32,042	$31,840

Net sales by geographic region for the years 2018, 2017 and 2016 are as follows:

	2018		**2017**		**2016**	
	(dollars in thousands)					
Net sales(1):						
United States	$26,348	77 %	$22,978	72 %	$22,711	71 %
Asia / Pacific	3,238	9 %	4,017	13 %	4,130	13 %
Europe	2,540	8 %	3,652	11 %	2,990	9 %
Other	1,989	6 %	1,395	4 %	2,009	7 %

$34,115	100%	$32,042	100%	$31,840	100%

(1) Net sales are attributed to countries based on location of customer.

Note 14 Income Taxes

Income tax benefit (expense) for the years ended March 31, 2018, 2017 and 2016 consisted of:

	2018	2017	2016
	(in thousands)		
Current:			
Federal	$112	$ (2)	$(1)
State	(2)	(3)	23
Total current benefit (expense)	110	(5)	22
Deferred:			
Federal	—	—	(3,027)
State	—	—	(323)
Total deferred expense	—	—	(3,350)
Income tax benefit (expense)	$110	$ (5)	$(3,328)

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On December 22, 2017 H.R. 1, originally known as the Tax Cuts and Jobs Act, (the "Tax Act") was enacted. Among the significant changes to the U.S. Internal Revenue Code, the Tax Act lowers the U.S. federal corporate income tax rate ("Federal Tax Rate") from 34% to 21% effective January 1, 2018. The Company computed its income tax expense for the March 31, 2018 fiscal year using a blended Federal Tax Rate of 30.79%. The 21% Federal Tax Rate will apply to fiscal years ending March 31, 2019 and each year thereafter.

On December 22, 2017, Staff Accounting Bulletin No. 118 ("SAB 118") was issued to address the application of US GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Tax Act. Upon enactment of the Tax Act, as a result of the rate reduction, the Company re-measured its net deferred tax assets and liabilities using the Federal Tax Rate that will apply when those amounts are expected to reverse, resulting in a write-down of $1.2 million. Because there is a full valuation allowance against these assets, the valuation allowance was reduced accordingly and there was no effect on the provision (benefit) for income taxes. The Company has completed the accounting for the income tax effects of the Tax Act as of March 31, 2018 and has determined that the amount identified as provisional in the quarter ended December 31, 2018 was a materially correct amount. As a result, no measurement period adjustments have been recorded.

The following table reconciles the amount of income taxes computed at the federal blended rate of 30.79% for the year ended March 31, 2018 and 34% for the years ended March 31, 2017 and 2016, to the amount reflected in the Company's consolidated statements of operations for the years ended March 31, 2018, 2017 and 2016:

	2018	**2017**	**2016**
	(in thousands)		
Tax provision at federal statutory income tax rate	$(282)	$411	$363
Stock based compensation	(11)	(281)	(128)
Decrease (increase) in valuation allowance	1,565	(158)	(3,564)
State income taxes benefit (expense), net of federal income tax effect	(36)	49	25
State rate adjustment	3	(1)	1
AMT Credit	112	—	—
Tax Cuts and Jobs Act	(1,244)	—	—
Other, net	3	(25)	(25)
Income tax benefit (expense)	$110	$(5)	$(3,328)

The tax effects of temporary differences related to various assets, liabilities and carry forwards that give rise to deferred tax assets and deferred tax liabilities as of March 31, 2018 and 2017 are as follows:

	2018	**2017**
	(in thousands)	
Deferred tax assets:		

Net operating loss carry forwards	$2,903	$4,325
Inventory	295	405
Compensation accrual	153	187
Tax credit carry forwards	36	147
Other	22	40
Gross deferred tax assets	3,409	5,104
Less valuation allowance	(2,158)	(3,722)
Net deferred tax assets	1,251	1,382
Deferred tax liability- Depreciation and amortization	(1,251)	(1,382)
Net deferred tax assets	$—	$—

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In assessing the valuation allowance for deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Ultimately, the realization of deferred tax assets will depend on the existence future taxable income during the periods. In making this assessment, management considers past operating results, the scheduled reversal of deferred tax liabilities, estimates of future taxable income and tax planning strategies.

In fiscal 2016, the Company recorded a $3,564,000 valuation allowance against deferred tax assets. The Company concluded that a valuation allowance was appropriate in light of the significant negative evidence, which was objective and verifiable, primarily the cumulative losses in recent years. While the Company's long-term financial outlook remains positive, the Company concluded that its ability to rely on its long-term outlook as to future taxable income was limited due to the relative weight of the negative evidence from its recent cumulative losses. The Company's conclusion regarding the need for a valuation allowance against its deferred tax assets could change in the future based on improvements in operating performance, which may result in the full or partial reversal of the valuation allowance.

At March 31, 2018, the Company has net operating loss carry forwards and tax credit carry forwards available to offset future federal income tax as follows (in thousands):

Expires March 31,	**Net Operating Losses**	**Research and Experimentation Tax Credits**
2020	$ —	$ 8
2021	—	2
2022	2,839	—
2023	1,863	1
2026	159	—
2027	2,665	1
2028	1,612	16
2031	389	—
2032	44	—
2033	76	—
2034	392	—
2035	18	—
2037	1,681	—
Indefinite carryforward	266	—
	$ 12,004	$ 28

Under the Tax Act, the corporate Alternative Minimum Tax (AMT) was repealed. Taxpayers with AMT credit carryovers can use the credits to offset regular tax liability for any taxable year. In addition, the AMT credit is refundable in any taxable year beginning after 2017 and before 2022 in an amount equal to 50% (100% in the case of taxable years beginning in 2021) of the excess of the minimum tax credit for the taxable year over the amount of the credit allowable for the year against regular tax liability. Thus, a taxpayers' entire AMT credit carryforward amounts are fully refundable by 2022. The Company has an AMT credit carryforward of $120,000 as of March 31, 2018. The Company has reduced the AMT credit carryforward by applying the current 6.6% sequestration rate. As a result, $8,000 is still available to reduce future federal regular income taxes over an indefinite period. The Company will request the following refunds of $112,000 for the tax years ended March 31, 2018 through March 31, 2022:

Tax Year Ended:	**AMT Credit Refund Request**	
March 31, 2018	$	56,000
March 31, 2019		28,000
March 31, 2020		14,000
March 31, 2021		7,000
March 31, 2022		7,000
	$	112,000

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At March 31, 2018, the Company has state tax net operating loss carry forwards available to offset future California state taxable income of $746,000. These carry forwards expire March 31, 2030 through 2037. At March 31, 2018, the Company has state tax net operating loss carry forwards available to offset future Hawaii state taxable income of $6,532,000. These carry forwards expire March 31, 2030 through 2037.

The following represents the open tax years and jurisdictions that the Company used in its evaluation of tax positions:

Open tax years ending March 31,	**Jurisdiction**
2015-2018	U.S. Federal
2015-2018	State of Hawaii
2014-2018	State of California

Note 15 Selected Quarterly Financial Data (Unaudited)

	First Quarter(1)	**Second Quarter(1)**	**Third Quarter(1)**	**Fourth Quarter (1)**	**Year**
	(in thousands, except per share data)				
2018					
Net sales	$8,809	$ 8,055	$ 9,150	$8,101	$34,115
Gross profit	3,603	3,620	4,240	1,908	13,371
Net income (loss)	501	475	1,107	(1,058)	1,025
Net income (loss) per share					
Basic and diluted	0.09	0.08	0.19	(0.18)	0.18
2017					
Net sales	$7,322	$ 9,862	$ 7,605	$7,253	$32,042
Gross profit	2,821	3,885	2,857	2,661	12,224
Net income (loss)	(691)	99	(349)	(274)	(1,215)
Net income (loss) per share					
Basic and diluted	(0.12)	0.02	(0.06)	(0.05)	(0.21)

(1) The first, second, third and fourth quarters of 2018 include abnormal production costs of $9,000, $75,000, $4,000 and $720,000, respectively. The first, second, third and fourth quarters of 2017 include abnormal production costs of $28,000, $73,000, $148,000 and $5,000, respectively.

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PART IV

Item 15. Exhibits and Financial Statement Schedule

(a) Financial Statements and Schedule

(1) The following Financial Statements of Cyanotech Corporation and subsidiary and the Report of Independent Registered Public Accounting Firm are included in Item 8 of this report:

(2) The following financial statement schedule is included in this report on the pages indicated below:

Financial statement schedules not listed above have been omitted since they are either not required, not applicable or the information is included in the consolidated financial statements or notes thereto.

(b) Exhibit Listing

Exhibit	
23.1*	Consent of Independent Registered Public Accounting Firm signed June 15, 2018—Grant Thornton LLP
31.1*	Certifications of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 signed as of June 21, 2018.
31.2*	Certifications of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 signed as of June 21, 2018.
32.1*	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 signed as of June 21, 2018.
101	The following financial information from our Annual Report on Form 10-K for fiscal year ended March 31, 2018, filed with the SEC on June 15, 2018, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets at March 31, 2018 and 2017, (ii) the Consolidated Statements of Operations for the years ended March 31, 2018, 2017 and 2016, (iii) the Consolidated Statements of Stockholders' Equity for the years ended March 31, 2018, 2017 and 2016, (iv) the Consolidated Statements of Cash Flows for the years ended March 31, 2018 and 2017, and (v) Notes to Consolidated Financial Statements.
*	Included herewith. Other exhibits were filed as shown above.

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Schedule II

Cyanotech Corporation and Subsidiary

Valuation and Qualifying Accounts

Years Ended March 31, 2018, 2017 and 2016

(in thousands)

Description	Balance at Beginning of Year	Additions Charged to Costs and Expense	Charged to Other Accounts	Deductions	Balance at End of Year
Allowance for Doubtful Accounts:					
2018	$ 49	$ —	$ —	$ 22	$ 27
2017	136	—	—	87	49
2016	6	130	—	—	136

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on the 21st day of June, 2018.

CYANOTECH CORPORATION

By: /s/ Mawae R. Morton
Mawae R. Morton
Chief Executive Officer; Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signatures	**Title**	**Date**
/s/ Mawae R. Morton Mawae R. Morton	Chief Executive Officer; Director	June 21, 2018
/s/ Jole Deal Jole Deal	Chief Financial Officer, Vice President—Finance and Administration, Secretary and Treasurer (Principal Financial and Accounting Officer)	June 21, 2018
/s/ Michael A. Davis Michael A. Davis	Chairman of the Board	June 21, 2018
/s/ Gerald R. Cysewski, PH.D.	Chief Scientific Officer and Vice	June 21, 2018

Gerald R. Cysewski	Chairman of the Board	
/s/ Nancy E. Katz Nancy Katz	Director	June 21, 2018
/s/ Walter B. Menzel Walter B. Menzel	Director	June 21, 2018
/s/ David M. Mulder David M. Mulder	Director	June 21, 2018
/s/ David L. Vied David L. Vied	Director	June 21, 2018

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