PRECISION OPTICS CORPORATION, INC.
Form 10-Q
May 16, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2016

or

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

For the transition period from __________ to __________

Commission File Number: 001-10647

PRECISION OPTICS CORPORATION, INC.

(Exact name of registrant as specified in its charter)

Massachusetts	**04-2795294**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

22 East Broadway, Gardner, Massachusetts 01440-3338

(Address of principal executive offices) (Zip Code)

(978) 630-1800

(Registrant's telephone number, including area code)

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 x No o

Indicate by check mark 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

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

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

The number of shares outstanding of the issuer's common stock, par value $0.01 per share, at May 15, 2016 was 7,539,582 shares.

PRECISION OPTICS CORPORATION, INC.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

PRECISION OPTICS CORPORATION, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	March 31, 2016	June 30, 2015
ASSETS		
CURRENT ASSETS		
Cash and Cash Equivalents	$172,269	$241,051
Accounts Receivable, net	607,976	588,042
Inventories, net	1,053,302	1,073,256
Prepaid Expenses	100,194	65,182
Total Current Assets	1,933,741	1,967,531
PROPERTY AND EQUIPMENT		
Machinery and Equipment	2,479,471	2,431,127
Leasehold Improvements	553,596	553,596
Furniture and Fixtures	148,303	148,303
Vehicles	19,674	19,674
	3,201,044	3,152,700
Less: Accumulated Depreciation and Amortization	(3,115,345)	(3,096,993)
Net Property and Equipment	85,699	55,707
Patents, net	22,874	18,644
TOTAL ASSETS	$2,042,314	$2,041,882
LIABILITIES AND STOCKHOLDERS’ EQUITY		
CURRENT LIABILITIES		
Current Portion of Capital Lease Obligation	$7,728	$–
Accounts Payable	1,025,422	912,150
Customer Advances	23,010	118,800
Accrued Employee Compensation	176,130	222,222
Accrued Professional Services	54,471	60,735
Accrued Warranty Expense	25,000	25,000
Other Accrued Liabilities	7,200	36,087

Total Current Liabilities	1,318,961	1,374,994
Capital Lease Obligation, net of current portion	33,968	–
STOCKHOLDERS' EQUITY		
Common Stock, $0.01 par value - Authorized - 50,000,000 shares; Issued and Outstanding – 7,539,582 shares at March 31, 2016 and 6,389,806 shares at June 30, 2015	75,396	63,898
Additional Paid-in Capital	44,128,796	43,232,500
Accumulated Deficit	(43,514,807)	(42,629,510)
Total Stockholders' Equity	689,385	666,888
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$2,042,314	$2,041,882

The accompanying notes are an integral part of these consolidated interim financial statements.

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PRECISION OPTICS CORPORATION, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE THREE AND NINE MONTHS ENDED

MARCH 31, 2016 AND 2015

(UNAUDITED)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2016	2015	2016	2015
Revenues	$1,140,825	$1,141,892	$2,954,024	$2,949,154
Cost of Goods Sold	867,292	828,963	2,331,131	2,361,575
Gross Profit	273,533	312,929	622,893	587,579
Research and Development Expenses, net	118,285	140,177	377,199	355,782
Selling, General and Administrative Expenses	407,406	410,549	1,179,520	1,104,466
Gain on Sale of Assets	(8,480)	(691)	(26,948)	(17,901)
Total Operating Expenses	517,211	550,035	1,529,771	1,442,347
Operating Loss	$(243,678)	$(237,106)	$(906,878)	$(854,768)
Interest Expense	(469)	–	(469)	–
Other Income	22,050	39,222	22,050	39,222
Net Loss	(222,097)	(197,884)	(885,297)	(815,546)
Loss Per Share:				
Basic	$(0.03)	$(0.03)	$(0.13)	$(0.13)
Diluted	$(0.03)	$(0.03)	$(0.13)	$(0.13)
Weighted Average Common Shares Outstanding:				
Basic	7,484,197	6,334,757	7,033,090	6,241,438
Diluted	7,484,197	6,334,757	7,033,090	6,241,438

The accompanying notes are an integral part of these consolidated interim financial statements.

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PRECISION OPTICS CORPORATION, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE NINE MONTHS ENDED

MARCH 31, 2016 AND 2015

(UNAUDITED)

	Nine Months Ended March 31, 2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Loss	$(885,297)	$(815,546)
Adjustments to Reconcile Net Loss to Net Cash Used In Operating Activities -		
Depreciation and Amortization	18,352	14,962
Gain on Sale of Assets	(26,948)	(17,901)
Stock-based Compensation Expense	194,133	42,750
Non-cash Consulting Expense	55,050	38,625
Non-cash Gain on Settlement of Liabilities by Issuing Common Stock	(22,050)	(39,222)
Changes in Operating Assets and Liabilities -		
Accounts Receivable, net	(19,934)	(11,424)
Inventories	19,954	(259,864)
Prepaid Expenses	(35,012)	21,096
Accounts Payable	113,272	165,514
Customer Advances	(95,790)	74,400
Accrued Expenses	(65,943)	61,770
Net Cash Used In Operating Activities	(750,213)	(724,840)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additional Patent Costs	(4,230)	(10,972)
Purchases of Property and Equipment	(4,554)	(59,973)
Proceeds from Sale of Assets	26,948	17,901
Net Cash Provided by (Used in) Investing Activities	18,164	(53,044)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of Capital Lease Obligation	(2,094)	–
Gross Proceeds from Private Placement of Common Stock	700,000	980,291
Private Placement Expenses Incurred	(34,639)	(121,512)
Net Cash Provided by Financing Activities	663,267	858,779
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(68,782)	80,895
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	241,051	202,380
CASH AND CASH EQUIVALENTS, END OF PERIOD	$172,269	$283,275

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash Paid for Income Taxes	$912	$912
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Issuance of Common Stock to Consultants	$48,300	$93,793
Acquisition of Manufacturing Equipment Under Capital Lease	$43,790	$–

The accompanying notes are an integral part of these consolidated interim financial statements.

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PRECISION OPTICS CORPORATION, INC.

NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Operations

The accompanying consolidated financial statements include the accounts of Precision Optics Corporation, Inc. and its wholly-owned subsidiaries (the “Company”). All significant intercompany accounts and transactions have been eliminated in consolidation.

These consolidated financial statements have been prepared by the Company, without audit, and reflect normal recurring adjustments which, in the opinion of management, are necessary for a fair statement of the results of the third quarter and nine months of the Company’s fiscal year 2016. These consolidated financial statements do not include all disclosures associated with annual consolidated financial statements and, accordingly, should be read in conjunction with footnotes contained in the Company’s consolidated financial statements for the year ended June 30, 2015 together with the Report of Independent Registered Public Accounting Firm filed under cover of the Company’s 2015 Annual Report on Form 10-K, filed with the Securities and Exchange Commission on October 13, 2015.

Use of Estimates

The preparation of these consolidated financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Income (Loss) Per Share

Basic income (loss) per share is computed by dividing net income or net loss by the weighted average number of shares of common stock outstanding during the period. Diluted income (loss) per share is computed by dividing net income or net loss by the weighted average number of shares of common stock outstanding during the period, plus the number of potentially dilutive securities outstanding during the period such as stock options and warrants. For the three and nine months ended March 31, 2016 and 2015, the effect of such securities was antidilutive and not included in the diluted calculation because of the net loss generated in these periods.

The following is the calculation of loss per share for the three and nine months ended March 31, 2016 and 2015:

	Three Months Ended March 31		Nine Months Ended March 31	
	2016	2015	2016	2015
Net Income Loss – Basic and Diluted	$(222,097)	$(197,884)	$(885,297)	$(815,546)
Basic Weighted Average Shares Outstanding	7,484,197	6,334,757	7,033,090	6,241,438
Potentially Dilutive Securities	–	–	–	–
Diluted Weighted Average Shares Outstanding	7,484,197	6,334,757	7,033,090	6,241,438
Loss Per Share				
Basic	$(0.03)	$(0.03)	$(0.13)	$(0.13)
Diluted	$(0.03)	$(0.03)	$(0.13)	$(0.13)

The number of shares issuable upon the exercise of outstanding stock options and warrants that were excluded from the computation as their effect was antidilutive was approximately 4,168,000 and 3,794,000 for the three months ended March 31, 2016 and 2015, respectively, and approximately 4,168,000 and 3,794,000 for the nine months ended March 31, 2016 and 2015, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

In assessing the likelihood of utilization of existing deferred tax assets, management has considered historical results of operations and the current operating environment. Based on this evaluation, a full valuation reserve has been provided for the deferred tax assets.

2. INVENTORIES

Inventories are stated at the lower of cost (first-in, first-out) or market and consisted of the following:

	March 31, 2016	June 30, 2015
Raw Materials	$466,062	$485,266
Work-In-Progress	351,702	388,503
Finished Goods	235,538	199,487
Total Inventories	$1,053,302	$1,073,256

3. CAPITAL LEASE OBLIGATION

During the quarter ended March 31, 2016, the Company entered into a five-year capital lease obligation for the acquisition of manufacturing equipment totaling $51,252. At March 31, 2016, future minimum lease payments under the capital lease obligation are as follows:

Fiscal Year	**Amount**
2016	$2,563
2017	10,250
2018	10,250
2019	10,250

2020	10,250
2021	5,126
Total Minimum Payments	$48,689
Amount Representing Interest	6,993
Present Value of Minimum Lease Payments	41,696
Less – current portion	7,728
	$33,968

4. STOCK-BASED COMPENSATION

Stock-based compensation costs recognized during the quarters ended March 31, 2016 and 2015 amounted to $51,705 and $2,625 respectively, and the costs were included in the accompanying consolidated statements of operations in: selling, general and administrative expenses (2016 - $33,721; 2015 - $0), research and development expenses (2016 - $9,316; 2015 - $2,625) and cost of goods sold (2016 - $8,668; 2015 - $0). Stock-based compensation costs recognized during the nine month periods ended March 31, 2016 and 2015 amounted to $194,133 and $42,750, respectively, and were included in the accompanying consolidated statements of operations in: selling, general and administrative expenses (2016 - $94,099; 2015 - $27,000), research and development expenses (2016 - $48,023, 2015 - $15,750) and cost of goods sold (2016 - $52,011, 2015 - $0). No compensation has been capitalized because such amounts would have been immaterial.

The following tables summarize stock option activity for the nine months ended March 31, 2016:

	Options Outstanding		
	Number of Shares	**Weighted Average Exercise Price**	**Weighted Average Contractual Life**
Outstanding at June 30, 2015	1,079,079	$ 1.43	8.46 years
Grants	60,000	0.48	
Cancellations	(3,800)	$ 3.00	
Outstanding at March 31, 2016	1,135,279	$ 1.37	7.83 years

Information related to the stock options outstanding as of March 31, 2016 is as follows:

Range of Exercise Prices	Number of Shares	Weighted-Average Remaining Contractual Life (years)	Weighted-Average Exercise Price	Exercisable Number of Shares	Exercisable Weighted-Average Exercise Price
$0.48	60,000	10.00	$ 0.48	20,000	$ 0.48
$0.73	316,000	9.14	$ 0.73	165,000	$ 0.73
$0.73	330,000	9.14	$ 0.73	132,915	$ 0.73
$0.90	35,000	8.28	$ 0.90	23,334	$ 0.90
$0.90	30,000	8.28	$ 0.90	30,000	$ 0.90
$1.20	207,800	5.92	$ 1.20	207,800	$ 1.20
$0.90	9,000	7.76	$ 0.90	9,000	$ 0.90
$0.85	9,000	6.76	$ 0.85	9,000	$ 0.85
$0.55	44,000	5.92	$ 0.55	44,000	$ 0.55
$0.27	40,000	5.29	$ 0.27	40,000	$ 0.27
$1.35	1,200	3.65	$ 1.35	1,200	$ 1.35
$1.25	1,200	2.65	$ 1.25	1,200	$ 1.25
$6.25	1,600	0.66	$ 6.25	1,600	$ 6.25
$7.75	1,200	1.66	$ 7.75	1,200	$ 7.75
$13.75	49,279	0.11	$ 13.75	49,279	$ 13.75
$0.27–$13.75	1,135,279	7.83	$ 1.37	735,528	$ 1.73

The aggregate intrinsic value of the Company’s “in-the-money” outstanding and exercisable options as of March 31, 2016 was $8,400.

5. <u>SALE OF STOCK</u>

On October 19, 2015, the Company entered into agreements with accredited investors for the sale and purchase of 1,044,776 shares of the Company’s common stock, $0.01 par value at a purchase price of $0.67 per share. The Company received $700,000 in gross proceeds from the offering. The Company has used the net proceeds from this placement for general working capital purposes.

In conjunction with the placement, the Company also entered into a registration rights agreement with the investors, whereby the Company is obligated to file a registration statement with the Securities Exchange Commission on or before 90 calendar days after October 19, 2015 to register the resale by the investors of the 1,044,776 shares of the Company’s common stock purchased in the placement. The registration statement was filed on January 19, 2016 and became effective on February 1, 2016.

In conjunction with the offering, certain anti-dilution provisions of the warrants issued in conjunction with the Company’s June 25, 2008 and September 28, 2012 financing transactions were triggered. As a result, the number of existing June 25, 2008 warrants increased from 493,398 to 517,222 and the related exercise price of the warrants decreased from $1.03 to $0.98 per share. Also, as a result of the offering, the number of existing September 28, 2012 warrants increased from 2,189,724 to 2,293,013 and 217,322 to 222,559, respectively, and the related exercise price decreased from $1.11 to $1.06 and from $0.85 to $0.83, respectively.

6. SALE OF ASSETS

During the nine months ended March 31, 2016, the Company sold equipment that was previously written off for proceeds totaling $26,948, and recorded a gain of $26,948, which is included within operating expenses in the accompanying consolidated statements of operations.

7. OTHER INCOME

Other income in the amount of $22,050 and $39,222 for the quarter and nine months ended March 31, 2016 and 2015, respectively, represents non-cash gains on the settlement of liabilities for services rendered to the Company, by issuing 105,000 shares and 82,222 shares of common stock in February 2016 and January 2015, respectively. The non-cash gain is the difference between the recorded amount of the liabilities and the value of the stock when issued.

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

The following discussion of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and notes to those statements included elsewhere in this Quarterly Report on Form 10-Q for the quarter and nine months ended March 31, 2016 and with our audited consolidated financial statements for the year ended June 30, 2015 included in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission on October 13, 2015.

This Quarterly Report on Form 10-Q contains forward-looking statements. When used in this report, the words "expects," "anticipates," "suggests," "believes," "intends," "estimates," "plans," "projects," "continue," "ongoing," "potential," "expect," "predict," "believe," "intend," "may," "will," "should," "could," "would" and similar expressions are intended to identify forward-looking statements. You should not place undue reliance on these forward-looking statements. Our actual results could differ materially from those anticipated in the forward-looking statements for many reasons, including the risks described in this report, the risks described in our Annual Report on Form 10-K for the year ended June 30, 2015 and other reports we file with the Securities and Exchange Commission. Although we believe the expectations reflected in the forward-looking statements are reasonable, they relate only to events as of the date on which the statements are made. We do not intend to update any of the forward-looking statements after the date of this report to conform these statements to actual results or to changes in our expectations, except as required by law.

Overview

We have been a developer and manufacturer of advanced optical instruments since 1982. Today, the vast majority of our business is the design and manufacture of high-quality medical devices and approximately 10% of our business is the design and manufacture of military and industrial products. Our medical instrumentation line includes traditional endoscopes and endocouplers as well as other custom imaging and illumination products for use in minimally invasive surgical procedures. Much of our recent development efforts have been targeted at the development of next generation endoscopes. For the last ten years, we have funded internal research and development programs to develop next generation capabilities for designing and manufacturing 3D endoscopes and very small Microprecision™ lenses, anticipating future requirements as the surgical community continues to demand smaller and more enhanced imaging systems for minimally invasive surgery.

Our unique proprietary technology in the areas of micro optical lenses and prisms, micro medical fiber and CMOS based cameras, and custom design of medical grade instruments, combined with recent developments in the areas of 3D displays, has allowed us to begin commercialization of related product and service offerings to a widening group of customers addressing various medical device, defense and aerospace applications. We believe that new products based on these technologies provide enhanced optical and imaging qualities for many uses including existing surgical procedures and development of new procedures enabled by the small size and image quality of our camera modules.

We are registered to the ISO 9001:2008 and ISO 13485:2003 Quality Standards and comply with the FDA Good Manufacturing Practices and the European Union Medical Device Directive for CE marking of our medical products. Our internet website is www.poci.com. Information on our website is not intended to be integrated into this report.

The markets in which we do business are highly competitive and include both foreign and domestic competitors. Many of our competitors are larger and have substantially greater resources than we do. We routinely outsource specialized production efforts as required to obtain the most cost effective production. Over the years, we have achieved extensive experience collaborating with other optical specialists worldwide.

Our products and services have been principally sold to original equipment manufacturers, or OEM, customers. We believe our product offerings are competitive based on performance and other technical features. Based on certain cost advantages we maintain, we are able to offer products at a competitive price, including certain products that may be offered as single-use products to end customers. Further, our performance relating to factors such as scheduling and reliability, is essential to our customers.

We believe that our future success depends to a large degree on our ability to increase sales to current customers, to customers to whom we are currently engaged, and to new customers with whom we are in early stage evaluation. Further, we may seek to develop new technologies, processes, products and services to enhance the performance characteristics, methods of manufacture and cost of existing products. Accordingly, we expect to continue to seek and obtain product-related design and development contracts with customers and to selectively invest our own funds on research and development, particularly in the areas of Microprecision™ optics, micro medical cameras and 3D endoscopes.

For the nine months ended March 31, 2016, approximately 50% of our sales were made to five customers. Of these, two are large, international, medical device companies who have been our customers for many years. Both of these customers continue to purchase products that we developed over five years ago, and both now purchase new products that were developed and launched into production by us more recently. The other three top customers purchase products that we developed in recent years, and which rely heavily on our unique, proprietary Microprecision™ lens technology and optical visualization system expertise.

Current sales and marketing activities are intended to broaden awareness of the benefits of our products, which we believe are ready for general application to medical device projects requiring surgery-grade visualization from sub-millimeter sized devices and handheld 3D endoscopy. We believe greater demand for the small size and high image quality of our Microprecision™ line products will be driven by new medical procedures that have not previously been possible, by improved performance of existing endoscopes and other medical devices used in current minimally invasive medical procedures, and by broad migration toward the use of single-use medical devices.

General

This management's discussion and analysis of financial condition and results of operations is based upon our unaudited consolidated financial statements, which have been prepared without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

There have been no significant changes in our critical accounting policies as disclosed in the Notes to our Financial Statements contained in our Annual Report on Form 10-K for the year ended June 30, 2015 filed with the Securities and Exchange Commission on October 13, 2015.

Results of Operations

Our total revenues for the quarter ended March 31, 2016, the third quarter of our fiscal year 2016, were $1,140,825, as compared to $1,141,892 for the same period in the prior year, a decrease of $1,067, or 0.09%. The decrease in revenues for the quarter ended March 31, 2016 was primarily due to lower unit volume sales of certain traditional products, partially offset by higher unit volume sales of certain new product offerings, including optical components, single-use fiberscopes and CMOS micro cameras, and higher engineering services revenue. We believe the increase in engineering services revenue is a positive indication of future product sales. Our total revenues for the nine months ended March 31, 2016 were $2,954,024, as compared to $2,949,154 for the same period in the prior year, an increase of $4,870, or 0.2 %. The increase in revenues for the nine month period was primarily due to higher unit volume sales of optical components, single-use fiberscopes and CMOS micro cameras, and higher engineering services revenue, partially offset by lower unit volume sales of certain traditional products.

Revenues from our largest customers, as a percentage of our total revenues, for the nine months ended March 31, 2016 and 2015, were as follows:

	Nine Months Ended March 31,	
	2016	2015
Customer A	16%	11%
Customer B	14	23
Customer C	6	10
Customer D	–	12
All Others	64	44
	100%	100%

No other customer accounted for more than 10% of our revenues during those quarters.

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Gross profit for the quarter ended March 31, 2016 was $273,533, as compared to $312,929 for the same period in the prior year, which reflects a decrease of $39,396. Gross profit for the quarter ended March 31, 2016 as a percentage of our revenues was 24.0%, a decrease from the gross profit percentage of 27.4% for the same period in the prior year. Gross profit for the nine months ended March 31, 2016 was $622,893, as compared to $587,579 for the same period in the prior year, which reflects an increase of $35,314. Gross profit for the nine months ended March 31, 2016 as a percentage of our revenues was 21.1%, an increase from the gross profit percentage of 19.9% for the same period in the prior year. The decrease in our gross profit percentage in the most recent quarter compared to the prior year was due primarily to manufacturing inefficiencies on a few projects. The increase in our gross profit percentage in the most recent nine months was due primarily to the reduced cost of manufacturing inefficiencies such as scrap, partially offset by higher stock-based compensation expenses in the current fiscal year. Further, our quarterly gross profit and gross profit percentage depend on a number of factors, including overall sales volume, the mix of products sold, and the costs of initial production in connection with new products. If we are able to successfully increase our sales volumes, we expect our gross margins to increase.

Research and development expenses were $118,285 for the quarter ended March 31, 2016, compared to $140,177 for the same period in the prior year, a decrease of $21,892, or 15.6%. The decrease in the quarter ended March 31, 2016 compared to same period in the prior year was primarily due to the increase in our engineering services revenue. As a result of increases in such revenue, a greater portion of our fixed engineering cost is included in cost of goods sold. Quarterly research and development expenses depend on our assessment of new product opportunities and available resources. Research and development expenses were net of reimbursement of related costs of $0 and $0 during the quarters ended March 31, 2016 and 2015, respectively. Research and development expenses were $377,199 for the nine months ended March 31, 2016, compared to $355,782 for the same period in the prior year, an increase of $21,417, or 6.0%. The increase in the nine month period ended March 31, 2016 compared to the same period in the prior year was primarily due to higher stock-based compensation expenses, and by lower reimbursements received from customers for such activities, partially offset by the increase in engineering services revenue as explained above. Research and development expenses were net of reimbursement of related costs of $0 and $23,404 during the nine months ended March 31, 2016 and 2015, respectively.

Selling, general and administrative expenses were $407,406 for the quarter ended March 31, 2016, compared to $410,549 for the same period in the prior year, a decrease of $3,143, or 0.8%. The decrease in the quarter ended March 31, 2016 compared to the same period in the prior year was primarily due to the curtailment of operations of our Hong Kong subsidiary, partially offset by higher stock-based compensation expenses and consulting expenses. Selling, general and administrative expenses were $1,179,520 for the nine months ended March 31, 2016, compared to $1,104,466 for the same period in the prior year, an increase of $75,054, or 6.8%. The increase in the nine month period ended March 31, 2016 compared to the same period in the prior year was primarily due to higher stock-based compensation expenses and consulting expenses, partially offset by the curtailment of operations of our Hong Kong subsidiary.

No income tax provision was recorded in the first, second or third quarters of fiscal year 2016 or 2015 because of the losses generated in those periods.

Liquidity and Capital Resources

We have traditionally funded working capital needs through product sales, management of working capital components of our business, and by cash received from public and private offerings of our common stock, warrants to purchase shares of our common stock or convertible notes. We have incurred quarter to quarter operating losses during our efforts to develop current products including Microprecision™ optical elements, micro medical camera assemblies and 3D endoscopes. Our management expects that such operating losses will continue until sales increase to breakeven and profitable levels. Our management also believes that the opportunities represented by these products have the potential to generate sales increases to achieve breakeven and profitable results.

Until we achieve and sustain breakeven and profitable results, we will be required to pursue several options to manage cash flow and raise capital, including issuing debt or equity or entering into a strategic alliance. The sale of additional equity or convertible debt securities would result in additional dilution to our current stockholders, and debt financing, if available, may involve restrictive covenants that could restrict our operations or finances. Financing may not be available in amounts or on terms acceptable to us, if at all. If we are unable to secure additional capital, we may be required to curtail our research and development initiatives and take additional measures to reduce costs in order to conserve our cash in amounts sufficient to sustain operations and meet our obligations. If we cannot raise funds on acceptable terms or achieve positive cash flow, we may not be able to continue to develop new products, grow market share, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements, any of which could negatively impact our business, operating results and financial condition, or impact our ability to continue to conduct operations.

During the quarter ended March 31, 2016, we incurred a net loss of $222,097 and used cash in operating activities of $225,282. As of March 31, 2016, cash and cash equivalents were $172,269, accounts receivable were $607,976, and current liabilities were $1,318,961. As of June 30, 2015, cash and cash equivalents were $241,051, accounts receivable were $588,042, and current liabilities were $1,374,994.

On October 19, 2015, we closed agreements with institutional and accredited investors for the sale and purchase of 1,044,776 shares of our common stock at a purchase price of $0.67 per share. We received $700,000 in gross proceeds from the offering. We are using the net proceeds from this placement for general working capital purposes.

Capital equipment expenditures during the nine months ended March 31, 2016 and 2015 were $4,554 and $59,973, respectively. Future capital equipment expenditures will be dependent upon future sales and success of on-going research and development efforts.

Contractual cash commitments for the fiscal years subsequent to March 31, 2016 are summarized as follows:

	2016	2017	Thereafter	Total
Operating Leases	$5,730	$18,402	$ 8,400	$32,532
Capital Leases	2,563	10,250	35,876	48,689
Totals	$8,293	$28,652	$ 44,276	$81,221

We have contractual cash commitments related to open purchase orders as of March 31, 2016 of approximately $243,000.

Off-Balance Sheet Arrangements

We currently have no off-balance sheet arrangements that have or are reasonably likely to have a current or future material effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

As a smaller reporting company, as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.

Item 4. Controls and Procedures.

Management's Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and our Chief Financial Officer evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures, including internal control over financial reporting, were not effective, as of March 31, 2016, to ensure the information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934, as amended (i) is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Our disclosure controls and procedures are intended to be designed to provide reasonable assurance that such information is accumulated and communicated to our management. Based on this evaluation, our management concluded that our internal control over financial reporting was not effective as of March 31, 2016.

The following is a description of two material weaknesses in our internal control over financial reporting:

Segregation of Duties: As previously disclosed in our Annual Reports on Form 10-K for the fiscal years ended June 30, 2008-2015, our management identified a control deficiency during the 2008 fiscal year because we lacked sufficient staff to segregate accounting duties. We believe the control deficiency resulted primarily because we have the equivalent of one and one-half persons performing all accounting-related on-site duties. As a result, we did not maintain adequate segregation of duties within our critical financial reporting applications, the related modules and financial reporting processes. This control deficiency could result in a misstatement of balance sheet and income statement accounts in our interim or annual consolidated financial statements that would not be detected. Accordingly, management has determined that this control deficiency constitutes a material weakness. During the period beginning with fiscal year 2008 through June 30, 2015, no audit adjustments resulting from this condition were required.

To address and remediate the material weakness in internal control over financial reporting described above, beginning with the quarter ended September 30, 2008, we instituted a procedure whereby our Chief Executive Officer, our Chief Financial Officer and other members of our Board of Directors perform a higher level review of the quarterly and annual reports on Form 10-Q and Form 10-K prior to filing.

We believe that the step outlined above strengthens our internal control over financial reporting and mitigates the material weakness described above. As part of our assessment of internal control over financial reporting for the fiscal year ended June 30, 2015, our management has evaluated this additional control and has determined that it is operating effectively.

Inventory Valuation: As previously disclosed in our Annual Reports on Form 10-K for the fiscal years ended June 30, 2009-2015, we reported a material weakness with respect to the valuation of our inventories. Specifically, the amounts used to value our inventory at June 30, 2009 with respect to overhead rates and purchased items were often inconsistent with the supporting documentation, due to year-to-year changes in overhead rates and costs of purchased items that were not properly reflected in inventory valuation. Accordingly, management had determined that this control deficiency constituted a material weakness as of June 30, 2009. One audit adjustment of approximately $58,000 to our audited financial statements as of June 30, 2011 was necessary as a result of this condition.

Changes in Internal Control over Financial Reporting

There was no change in our internal control over financial reporting that occurred during the first quarter of our fiscal year covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

To address and remediate the material weakness in internal control over financial reporting described above, beginning in the quarter ended September 30, 2009 and continuing through the quarter ended March 31, 2016, we implemented processes to improve our inventory controls and documentation surrounding inventory valuation for overhead rates, and performed procedures to ensure that the pricing of inventory items was consistent with the supporting documentation. We believe that the step outlined above strengthens our internal control over financial reporting and mitigates the material weakness described above.

We intend to continue to remediate material weaknesses and enhance our internal controls but cannot guarantee that our efforts will result in remediation of our material weaknesses or that new issues will not be exposed in this process.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

Our Company, on occasion, may be involved in legal matters arising in the ordinary course of our business. While management believes that such matters are currently insignificant, matters arising in the ordinary course of business for which we are or could become involved in litigation may have a material adverse effect on our business, financial condition or results of operations. We are not aware of any pending or threatened litigation against us or our officers and directors in their capacity as such that could have a material impact on our operations or finances.

Item 1A. Risk Factors.

There have been no material changes from the risk factors previously disclosed in our annual report on Form 10-K for the fiscal year ended June 30, 2015, as filed with the Securities and Exchange Commission on October 13, 2015.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

On February 18, 2016, we issued 105,000 shares of common stock valued at $0.46 per share for services rendered to us.

We relied on the Section 4(a)(2) exemption from securities registration under the federal securities laws for transactions not involving any public offering. No advertising or general solicitation was employed in offering the securities. The securities were issued to accredited investors and a limited number of non-accredited investors. The securities were offered for investment purposes only and not for the purpose of resale or distribution, and the transfers thereof were appropriately restricted by us.

Item 3. Defaults Upon Senior Securities.

We did not default upon senior securities during the quarter ended March 31, 2016.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

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Item 6. Exhibits.

Exhibit	Description
2.1	Asset Purchase Agreement between the Company and Optometrics Corporation, dated January 18, 2008 (included as Exhibit 2.1 to the Form 8-K filed January 25, 2008 and incorporated herein by reference).
3.1	Articles of Organization of Precision Optics Corporation, Inc., as amended (included as Exhibit 3.1 to the Form SB-2 filed March 16, 2007 and incorporated herein by reference).
3.2	Bylaws of Precision Optics Corporation, Inc. (included as Exhibit 3.2 to the Form S-1 filed December 18, 2008 and incorporated herein by reference).
3.3	Articles of Amendment to the Articles of Organization of Precision Optics Corporation, Inc., dated November 25, 2008 and effective December 11, 2008 (included as Exhibit 3.1 to the Form 8-K filed December 11, 2008 and incorporated herein by reference).
3.4	Amended and Restated Bylaws of Precision Optics Corporation, Inc. (included as Exhibit 3.1 to the Company's Current Report on Form 8-K filed July 11, 2014 and incorporated herein by reference).
4.1	Registration Rights Agreement by and among the Company and each investor named therein, dated February 1, 2007 (included as Exhibit 4.1 to the Form 8-K filed February 2, 2007 and incorporated herein by reference).
4.2	Form of Warrant to Purchase Shares of Common Stock (included as Exhibit 4.2 to the Form 8-K filed February 2, 2007 and incorporated herein by reference).
4.3	Registration Rights Agreement by and among the Company and each investor named therein, dated June 25, 2008 (included as Exhibit 4.1 to the Form 8-K filed June 27, 2008 and incorporated herein by reference).
4.4	Form of Warrant to Purchase Shares of Common Stock, dated June 25, 2008 (included as Exhibit 4.2 to the Form 8-K filed June 27, 2008 and incorporated herein by reference).
4.5	Form of 10% Senior Secured Convertible Note, dated June 25, 2008 (included as Exhibit 4.3 to the Form 8-K filed June 27, 2008 and incorporated herein by reference).
4.6	Form of Warrant to Purchase Shares of Common Stock, dated September 28, 2012 (included as Exhibit 4.1 to the Form 8-K filed October 2, 2012 and incorporated herein by reference).
4.7	Registration Rights Agreement by and among the Company and each investor named therein, dated September 28, 2012 (included as Exhibit 4.2 to the Form 8-K filed October 2, 2012 and incorporated herein by reference).
4.8	Warrant to Purchase Shares of Common Stock issued to Loewen, Ondaatje, McCutcheon USA LTD, dated September 28, 2012 (included as Exhibit 4.3 to the Form 8-K filed October 2, 2012 and incorporated herein by reference).

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4.9	Form of Warrant to Purchase Shares of Common Stock (Special Situations Settlement), dated February 12, 2013 (included as Exhibit 4.1 to the Form 8-K filed February 13, 2013 and incorporated herein by reference).
4.10	Registration Rights Agreement by and among the Company, Special Situations Fund III QP, L.P. and Special Situations Private Equity Fund, L.P., dated February 12, 2013 (included as Exhibit 4.2 to the Form 8-K filed February 13, 2013 and incorporated herein by reference).
4.11	Form of Warrant to Purchase Shares of Common Stock (Pitlor and Schumsky Settlement), dated February 12, 2013 (included as Exhibit 4.3 to the Form 8-K filed February 13, 2013 and incorporated herein by reference).
10.1	Precision Optics Corporation, Inc. 1997 Incentive Plan, as amended and restated (included as Exhibit 10.1 to the Form 10-QSB filed November 13, 2003 and incorporated herein by reference).
10.2	Precision Optics Corporation, Inc. 2006 Equity Incentive Plan (included as Exhibit 99.1 to the Form 8-K filed December 4, 2006 and incorporated herein by reference).
10.3	Purchase Agreement by and among the Company and each investor named therein, dated February 1, 2007 (included as Exhibit 10.1 to the Form 8-K filed February 2, 2007 and incorporated herein by reference).
10.4	Form of Incentive Stock Option Certificate (included as Exhibit 10.1 to the Form 10-QSB filed February 14, 2007 and incorporated herein by reference).
10.5	Form of Nonstatutory Stock Option Certificate (included as Exhibit 10.2 to the Form 10-QSB filed February 14, 2007 and incorporated herein by reference).
10.6	Purchase Agreement by and among the Company and each investor named therein, dated June 25, 2008 (included as Exhibit 10.1 to the Form 8-K filed June 27, 2008 and incorporated herein by reference).
10.7	Pledge and Security Agreement by and among the Company and each investor named therein, dated June 25, 2008 (included as Exhibit 10.2 to the Form 8-K filed June 27, 2008 and incorporated herein by reference).
10.8	Consulting Agreement between the Company and Jack P. Dreimiller, dated August 15, 2008 (included as Exhibit 10.1 to the Form 8-K filed August 18, 2008 and incorporated herein by reference).
10.9	Side Letter Agreement between the Company and the investors signatory to the Purchase Agreement, dated November 25, 2008 (included as Exhibit 10.1 to the Form 8-K filed December 11, 2008 and incorporated herein by reference).
10.10	Side Letter Agreement between the Company and the holders signatory to the 10% Senior Secured Convertible Note, dated December 11, 2008 (included as Exhibit 10.15 to the Form S-1 filed December 18, 2008 and incorporated herein by reference).

10.11	Side Letter Agreement between the Company and the holders signatory to the 10% Senior Secured Convertible Note, dated April 2, 2009 (included as Exhibit 10.16 to the Form S-1/A filed April 6, 2009 and incorporated herein by reference).
10.12	Compensation Agreement with Richard E. Forkey, dated December 3, 2010 (included as Exhibit 10.11 to the Form 8-K filed December 6, 2010 and incorporated herein by reference).
10.13	Compensation Agreement with Joseph N. Forkey, dated December 3, 2010 (included as Exhibit 10.12 to the Form 8-K filed December 6, 2010 and incorporated herein by reference).
10.14	Compensation Agreement with Joel R. Pitlor, dated December 3, 2010 (included as Exhibit 10.13 to the Form 8-K filed December 6, 2010 and incorporated herein by reference).
10.15	Asset Purchase Agreement between the Company and Intuitive Surgical Operations, Inc., dated July 27, 2011 (included as Exhibit 10.1 to the Form 8-K filed August 3, 2011 and incorporated herein by reference).
10.16	Amendment to Pledge and Security Agreement by and among the Company and each investor named therein, dated July 27, 2011 (included as Exhibit 10.2 to the Form 8-K filed August 3, 2011 and incorporated herein by reference).
10.17	Demand Note in the amount of $10,000, dated July 13, 2011, issued by the Company to Dr. Joseph N. Forkey (included as Exhibit 10.22 to the Form 10-K filed September 28, 2011, and incorporated herein by reference.)
10.18	Precision Optics Corporation, Inc. 2011 Equity Incentive Plan, dated October 13, 2011 (included as Exhibit 10.2 to Form S-8 filed October 14, 2011, and incorporated herein by reference.)
10.19	Precision Optics Corporation, Inc. 2011 Deferred Compensation Plan, dated October 13, 2011 (included as Exhibit 10.3 to Form S-8 filed October 14, 2011, and incorporated herein by reference.)
10.20	Side Letter Agreement to the Compensation Agreement with Richard E. Forkey, dated October 14, 2011 (included as Exhibit 10.4 to the Form 8-K filed October 19, 2011 and incorporated herein by reference).
10.21	Side Letter Agreement to the Compensation Agreement with Joseph N. Forkey, dated October 14, 2011 (included as Exhibit 10.5 to the Form 8-K filed October 19, 2011 and incorporated herein by reference).
10.22	Side Letter Agreement to the Compensation Agreement with Joel N. Pitlor, dated October 14, 2011 (included as Exhibit 10.6 to the Form 8-K filed October 19, 2011 and incorporated herein by reference).

10.23	Endorsement to 10% Senior Secured Convertible Note by the Company, dated October 31, 2011, and accepted by Special Situations Private Equity Fund, L.P. (included as Exhibit 10.2 to the Form 8-K filed November 3, 2011 and incorporated herein by reference).
10.24	Endorsement to 10% Senior Secured Convertible Note by the Company, dated October 31, 2011, and accepted by Special Situations Fund III QP, L.P. (included as Exhibit 10.3 to the Form 8-K filed November 3, 2011 and incorporated herein by reference).
10.25	Endorsement to 10% Senior Secured Convertible Note by the Company, dated July 31, 2012, and accepted by Arnold Schumsky (included as Exhibit 10.27 to the Form 10-K filed October 15, 2012, and incorporated herein by reference.)
10.26	Endorsement to 10% Senior Secured Convertible Note by the Company, dated August 31, 2012, and accepted by Arnold Schumsky (included as Exhibit 10.28 to the Form 10-K filed October 15, 2012, and incorporated herein by reference.)
10.27	Notice of Repayment of 10% Senior Secured Convertible Note in Full by the Company, dated September 28, 2012, and accepted by Arnold Schumsky (included as Exhibit 10.29 to the Form 10-K filed October 15, 2012, and incorporated herein by reference.)
10.28	Purchase Agreement by and among the Company and each investor named therein, dated September 28, 2012 (included as Exhibit 10.1 to the Form 8-K filed October 2, 2012 and incorporated herein by reference).
10.29	Settlement Agreement by and among the Company, Special Situations Fund III QP, L.P. and Special Situations Private Equity Fund, L.P., dated February 12, 2013 (included as Exhibit 10.1 to the Form 8-K filed February 13, 2013 and incorporated herein by reference).
10.30	Settlement Agreement by and between the Company and Joel Pitlor, dated February 12, 2013 (included as Exhibit 10.2 to the Form 8-K filed February 13, 2013 and incorporated herein by reference).
10.31	Settlement Agreement by and between the Company and Arnold Schumsky, dated February 12, 2013 (included as Exhibit 10.3 to the Form 8-K filed February 13, 2013 and incorporated herein by reference).
10.32	Form of Purchase Agreement by and among the Company and investor (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed July 7, 2014 and incorporated herein by reference).
10.33	Form of Registration Rights Agreement by and among the Company and investor (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed July 7, 2014 and incorporated herein by reference).
10.34	Precision Optics Corporation, Inc. Amended 2011 Equity Incentive Plan, dated October 14, 2011, as amended on April 16, 2015 (included as Exhibit 10.1 to the Company's Registration Statement on Form S-8 filed April 20, 2015, and incorporated herein by reference).
10.35	Form of Purchase Agreement by and among the Company and investor (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed October 23, 2015 and incorporated herein by reference).

10.36	Form of Registration Rights Agreement by and among the Company and investors (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on October 23, 2015 and incorporated herein by reference).
14.1	Precision Optics Corporation, Inc. Corporate Code of Ethics and Conduct (included as Exhibit 14.1 to the Form 10-K filed September 28, 2008 and incorporated herein by reference).
31.1*	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Officers pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema.
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase.
101.LAB*	XBRL Taxonomy Extension Label Linkbase.
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase.

*Filed herewith.

SIGNATURES

Pursuant to the requirements 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.

	PRECISION OPTICS CORPORATION, INC.	
Date: May 16, 2016	By:	/s/ Joseph N. Forkey Joseph N. Forkey Chief Executive Officer (Principal Executive Officer)
Date: May 16, 2016	By:	/s/ Jack P. Dreimiller Jack P. Dreimiller Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)

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