NOCOPI TECHNOLOGIES INC/MD/
Form 10-Q
November 14, 2011

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United States
Securities and Exchange Commission
Washington, D.C. 20549
Form 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2011.

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: 000-20333

NOCOPI TECHNOLOGIES, INC.

(Exact name of registrant as specified in its charter)

MARYLAND	87-0406496
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
9C Portland Road, West Conshohocken, PA	19428
(Address of principal executive offices)	(Zip Code)

(610) 834-9600

(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 þ 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 þ 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 o (Do not check if a smaller reporting company)	Smaller reporting company þ

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date. 58,187,378 shares of common stock, par value $0.01, as of November 10, 2011

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Nocopi Technologies, Inc.
*Statements of Operations**
(unaudited)

	Three Months ended September 30		Nine Months ended September 30	
	2011	2010	2011	2010
Revenues				
Licenses, royalties and fees	$ 85,800	$ 78,000	$ 285,600	$ 189,700
Product and other sales	86,900	103,800	299,600	237,000
	172,700	181,800	585,200	426,700
Cost of revenues				
Licenses, royalties and fees	16,100	15,100	47,600	54,900
Product and other sales	51,100	70,200	168,500	174,500
	67,200	85,300	216,100	229,400
Gross profit	105,500	96,500	369,100	197,300
Operating expenses				
Research and development	28,400	27,500	85,800	104,600
Sales and marketing	38,900	38,500	131,300	107,600
General and administrative	81,200	79,600	263,100	254,600
	148,500	145,600	480,200	466,800
Net loss from operations	(43,000)	(49,100)	(111,100)	(269,500)
Other income (expenses)				
License transfer fee, net	54,000		54,000	
Reversal of accounts payable and accrued expenses	57,400		57,400	
Interest expense, bank charges and financing cost	(2,300)	(2,500)	(7,600)	(8,300)
	109,100	(2,500)	103,800	(8,300)
Net income (loss)	$ 66,100	$ (51,600)	$ (7,300)	$ (277,800)
	$ .00	$ (.00)	$ (.00)	$ (.00)

Basic and diluted net income (loss) per common share				
Basic and diluted weighted average common shares outstanding	58,187,378	56,289,541	58,049,157	55,567,682

* **See accompanying notes to these financial statements.**

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Nocopi Technologies, Inc.
*Balance Sheets**

	September 30 2011 (unaudited)	December 31 2010 (audited)
Assets		
Current assets		
Cash	$ 1,400	$ 10,600
Accounts receivable less $5,000 allowance for doubtful accounts	168,500	171,100
Inventory	24,600	34,800
Prepaid and other	11,900	37,200
Total current assets	206,400	253,700
Fixed assets		
Leasehold improvements	72,500	72,500
Furniture, fixtures and equipment	184,500	184,500
	257,000	257,000
Less: accumulated depreciation and amortization	251,900	247,400
	5,100	9,600
Total assets	$ 211,500	$ 263,300
Liabilities and Stockholders Deficiency		
Current liabilities		
Line of credit	$ 75,000	$ 93,800
Demand loans	52,500	50,500
Accounts payable	235,400	263,400
Accrued expenses	116,200	142,500
Deferred revenue	54,500	46,500
Total current liabilities	533,600	596,700
Stockholders deficiency		
Common stock, $0.01 par value		
Authorized 75,000,000 shares		
Issued and outstanding 2011 58,187,378 shares; 2010 57,852,041 shares	581,900	578,500
Paid-in capital	12,380,600	12,365,400
Accumulated deficit	(13,284,600)	(13,277,300)
Total stockholders deficiency	(322,100)	(333,400)
Total liabilities and stockholders deficiency	$ 211,500	$ 263,300

* **See accompanying notes to these financial statements.**

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Nocopi Technologies, Inc.
*Statements of Cash Flows**
(unaudited)

	Nine Months ended September 30	
	2011	**2010**
Operating Activities		
Net loss	$ (7,300)	$ (277,800)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	4,500	6,300
Reversal of accounts payable and accrued expenses	(57,400)	
Compensation expense stock option grants		3,000
Financing cost warrant grants	600	2,200
	(59,600)	(266,300)
Decrease in assets		
Accounts receivable	2,600	63,700
Inventory	10,200	32,600
Prepaid and other	25,300	18,300
Increase (decrease) in liabilities		
Accounts payable and accrued expenses	3,100	(10,800)
Deferred revenue	8,000	31,400
	49,200	135,200
Net cash used in operating activities	(10,400)	(131,100)
Investing Activities		
Additions to fixed assets		(2,300)
Net cash used in investing activities		(2,300)
Financing Activities		
Proceeds from demand loans	17,000	50,500
Repayment of demand loan	(15,000)	
Repayment of borrowings under line of credit	(18,800)	
Issuance of common stock	18,000	64,600
Net cash provided by financing activities	1,200	115,100
Decrease in cash	(9,200)	(18,300)
Cash at beginning of year	10,600	37,200
Cash at end of period	$ 1,400	$ 18,900

Supplemental disclosure of cash flow information				
Cash paid for interest	$	2,500	$	2,900
Supplemental disclosure of non cash investing activities				
Disposal of fully depreciated equipment				
Furniture, fixtures and equipment	$		$	2,700
Accumulated depreciation and amortization	$		$	2,700

*** See accompanying notes to these financial statements.**

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NOCOPI TECHNOLOGIES, INC.
NOTES TO FINANCIAL STATEMENTS
(UNAUDITED)

Note 1. Financial Statements

The accompanying unaudited condensed financial statements have been prepared by Nocopi Technologies, Inc. (the Company). These statements include all adjustments (consisting only of normal recurring adjustments) which management believes necessary for a fair presentation of the statements and have been prepared on a consistent basis using the accounting policies described in the summary of Accounting Policies included in the Company s 2010 Annual Report on Form 10-K. Certain financial information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the accompanying disclosures are adequate to make the information presented not misleading. The Notes to Financial Statements included in the 2010 Annual Report on Form 10-K should be read in conjunction with the accompanying interim financial statements. The interim operating results for the three months and nine months ended September 30, 2011 may not be necessarily indicative of the operating results expected for the full year.

The Company follows Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 220 in reporting comprehensive income. Comprehensive income is a more inclusive financial reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income. Since the Company has no items of other comprehensive income, comprehensive income (loss) is equal to net income (loss).

Note 2. Going Concern

Since its inception, the Company has incurred significant losses and, as of September 30, 2011, had accumulated losses of $13,284,600. For the nine months ended September 30, 2011, the Company had a net loss from operations of $111,100. At September 30, 2011, the Company had negative working capital of $327,200 and a stockholders deficiency of $322,100. For the year ended December 31, 2010, the Company s net loss from operations was $234,400. Due in part to the recession that has and is continuing to negatively impact the country s economy, the Company, which is substantially dependent on its licensees to generate licensing revenues, may incur further operating losses and experience negative cash flow in the future. Achieving profitability and positive cash flow depends on the Company s ability to generate and sustain significant increases in revenues and gross profits from its traditional business and new product lines. There can be no assurances that the Company will be able to generate sufficient revenues and gross profits to return to and sustain profitability and positive cash flow in the future.

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During the second quarter of 2011, the Company raised $18,000 in a private placement exempt from registration under section 4(2) of the Securities Act of 1933, as amended, whereby 335,337 shares of the Company s common stock were sold to two non-affiliated individual investors. In late September 2011, the Company received an unsecured loan of $2,000 from an individual and repaid the loan in October 2011. Additionally, in late January 2011, the Company received an unsecured loan of $15,000 from William P. Curtis, Jr., a Director, and repaid the loan in early February 2011. During 2010, the Company received unsecured loans totaling $50,500 from four individuals, of which $7,500 was lent by Herman M. Gerwitz, a Director. During 2010, the Company raised $101,600 in a private placement exempt from registration under section 4(2) of the Securities Act of 1933, as amended, whereby 2,668,333 shares of the Company s common stock were sold to five non-affiliated individual investors and 211,412 were sold to two Directors of the Company. Receipt of funds from these investors and from the demand loan holders has permitted the Company to continue in operation to the current date. Management of the Company believes that it will need additional capital in the future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases from traditional and new product lines can be realized. There can be no assurances that the Company will be successful in obtaining sufficient additional capital, or if it does, that the additional capital will enable the Company to impact its revenues so as to have a material positive effect on the Company s operations and cash flow. The Company believes that without additional capital, whether in the form of debt, equity or both, it may be forced to cease operations at an undetermined date in the future.

Note 3. Stock Based Compensation

The Company follows FASB ASC 718, *Compensation Stock Compensation*, and uses the Black-Scholes option pricing model to calculate the grant-date fair value of an award.

In February 2009, the Board of Directors of the Company, under the Company s 1999 Stock Option Plan, granted options to acquire 200,000 shares of its common stock to five employees of the Company, options to acquire 75,000 shares of its common stock to two consultants and options to acquire 50,000 shares of its common stock to an officer of the Company at $0.12 per share. The options vested in February 2010 and expire five years from the date of grant. In accordance with the fair value method as described in the accounting requirements of FASB ASC 718, expense of approximately $22,900 was recognized over the vesting period of the options through February 2010 to account for the cost of services received by the Company in exchange for the grant of stock options. There was no compensation expense recognized during the three months and nine months ended September 30, 2011. There was no compensation expense recognized during the three months ended September 30, 2010. During the nine months ended September 30, 2010, compensation expense of approximately $3,000 was recognized. There was no unrecognized portion of expense at September 30, 2011. The Company s stock option plans terminated prior to 2010, and no further stock options can be granted under the plans; however, stock options granted before the termination dates may be exercised through their expiration dates.

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The following table summarizes all stock option activity of the Company since December 31, 2010:

	Number of Shares	Exercise Price	Weighted Average Exercise Price	
Outstanding options - December 31, 2010	945,000	$.12 to $.45	$	.29
Options expired	300,000	$.22	$	.22
Outstanding options - September 30, 2011	645,000	$.12 and $.45	$	.32
Weighted average remaining contractual life (years)	1.89			
Exercisable options - September 30, 2011	645,000	$.12 and $.45	$	.32

Note 4. Line of Credit

The Company has a line of credit with a bank that, at its inception in 2008, allowed the Company to borrow up to $100,000 to provide a future source of working capital. The line of credit, which matures in September 2014, is secured by all the assets of the Company and bears interest at the bank s prime rate plus 0.5%. At September 30, 2011, the interest rate applicable to the Company s line of credit was 3.75%. Until the third quarter of 2010, the Company had been required to pay interest only on borrowings under the line of credit. In the third quarter of 2010, the Company was notified by the bank that the fully drawn line of credit, which had an outstanding balance of $100,000 at that time, was not being renewed. The bank offered to the Company and the Company accepted repayment terms that require the Company to repay the outstanding loan balance in forty-eight equal monthly installments of $2,083 plus interest at the bank s prime rate plus 0.5%, beginning in October 2010. The incurrence of certain unsecured loans in 2010 and 2011 constitutes a violation of certain covenants under the Company s line of credit which gives the lender certain rights, including the right to require the Company to repay immediately the entire outstanding loan balance, which was $75,000 at September 30, 2011, rather than on a monthly basis over the following thirty-six months. Should the bank require immediate prepayment, the Company s financial condition could be materially adversely affected. Management of the Company intends to cure this violation.

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Note 5. Demand Loans

In September 2011, the Company received an unsecured loan of $2,000 from an individual and repaid the loan, with interest at 8%, in October 2011.

In January 2011, the Company received an unsecured loan of $15,000 from William P. Curtis, Jr., a Director, and repaid the loan, with interest at 8%, in February 2011. The loan was used to finance the Company s working capital requirements. Additionally, the Company granted warrants to purchase 15,000 shares of common stock of the Company at $0.06 per share to Mr. Curtis. The warrants expire in five years. A financing cost of approximately $600, representing the fair value of the warrants, was charged to income in the first quarter of 2011. The fair value of the warrants was determined using the Black-Scholes pricing model with the following assumptions: expected life-5 years; interest rate-2%; expected volatility based on the Company s historical volatility-83%; and dividend yield-0.

In March 2010, the Company received unsecured loans totaling $40,500 from three individuals of which $7,500 was lent by Herman M. Gerwitz, a Director. The loans bear interest at 8% and are payable on demand. The loans were used to finance the Company s working capital requirements. Additionally, the Company granted warrants to purchase 40,500 shares of common stock of the Company at $0.0703 per share to these three individuals. The warrants expire in five years. A financing cost of approximately $1,800, representing the fair value of the warrants, was charged to income in the first quarter of 2010. The fair value of the warrants was determined using the Black-Scholes pricing model with the following assumptions: expected life-5 years; interest rate-2.65%; volatility-77%; and dividend yield-0.

In May 2010, the Company received an unsecured loan of $10,000 from an individual. The loan bears interest at 8% and is payable on demand. The loan was used to finance the Company s working capital requirements. Additionally, the Company granted warrants to purchase 10,000 shares of common stock of the Company at $0.06 per share to this individual. The warrants expire in five years. A financing cost of approximately $400, representing the fair value of the warrants, was charged to income in the second quarter of 2010. The fair value of the warrants was determined using the Black-Scholes pricing model with the following assumptions: expected life-5 years; interest rate 2.11%; volatility-78%; and dividend yield-0.

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The following table summarizes all warrant activity of the Company since December 31, 2010:

	Number of Shares	Exercise Price	Weighted Average Exercise Price
Outstanding warrants - December 31, 2010	97,500	$.06 to $.27	$ .14
Warrants granted	15,000	$.06	$ .06
Warrants expired	47,000	$.21 to $.27	$ .23
Outstanding warrants - September 30, 2011	65,500	$.06 and $.07	$ .07
Weighted average remaining contractual life (years)	3.68		
Exercisable warrants - September 30, 2011	65,500	$.06 and $.07	$ .07

Note 6. Stockholders Deficiency

During the first nine months of 2011, the Company sold a total of 335,337 shares of its common stock to two non-affiliated individual investors for a total of $18,000 pursuant to a private placement. During the first nine months of 2010, the Company sold 1,460,000 shares of its common stock to three non-affiliated individuals, 148,912 shares of its common stock to Philip B. White, a Director and 62,500 shares of its common stock to Herman M. Gerwitz, a Director, for a total of $64,600 pursuant to the private placement.

Note 7. Other Income (Expenses)

Other income (expenses) includes, for the three months and nine months ended September 30, 2011, (i) a license transfer fee of $60,000, net of commission expense of $6,000, received in connection with the sale by a licensee in the entertainment and toy products market of an operating division that included, with the Company s consent, assignment of the technology license with the Company to another business in the entertainment and toy products market during the third quarter of 2011; (ii) the reversal of approximately $19,400 of accounts payable and related accrued expenses related to invoices received during the first nine months of 2001 from a professional services business that provided legal services to the Company that the Company, with legal counsel, has determined to be no longer statutorily payable as the statute of limitations to bring a claim has expired; and (iii) the reversal of a total of $38,000 of accrued expenses related to (x) potential reimbursement of expenses to members of a group who in 1999 succeeded in electing four members to the Company s Board of Directors and (y) the purchase of equipment in 2007 for which an invoice was never submitted by the supplier that the Company, with legal counsel, has determined to be no longer statutorily payable as the applicable statutes of limitations to bring such claims have expired. Additionally, other income (expenses) includes interest on funds borrowed under the Company s line of credit with a bank and on unsecured loans from five individuals. Also included in other income (expenses) are financing costs related to warrants issued in the first nine months of 2011 and 2010 in conjunction with unsecured loans received during those periods.

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Note 8. Income Taxes

There is no provision for income taxes for the three months ended September 30, 2011 due to the availability of net operating loss carryforwards. There is no income tax benefit for the losses for the nine months ended September 30, 2011 and for the three months and nine months ended September 30, 2010 because the Company has determined that the realization of the net deferred tax asset is not assured. The Company has created a valuation allowance for the entire amount of such benefits.

There was no change in unrecognized tax benefits during the period ended September 30, 2011 and there was no accrual for uncertain tax positions as of September 30, 2011.

Tax years from 2008 through 2010 remain subject to examination by U.S. federal and state jurisdictions.

Note 9. Earnings (Loss) per Share

In accordance with FASB ASC 260, *Earnings per Share*, basic earnings (loss) per common share is computed using net earnings (loss) divided by the weighted average number of common shares outstanding for the periods presented. The computation of diluted earnings per common share involves the assumption that outstanding common shares are increased by shares issuable upon exercise of those stock options and warrants for which the market price exceeds the exercise price. The number of shares issuable upon the exercise of such stock options and warrants is decreased by shares that could have been purchased by the Company with related proceeds. Because the exercise prices for the stock options and warrants exceeded the average market price during the three months ended September 30, 2011, common stock equivalents, consisting of stock options and warrants, were anti-dilutive. Because the Company reported a net loss for the nine months ended September 30, 2011 and for the three months and nine months ended September 30, 2010, common stock equivalents, consisting of stock options and warrants, were anti-dilutive.

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Note 10. Major Customer and Geographic Information

The Company s revenues, expressed as a percentage of total revenues, from non-affiliated customers that equaled 10% or more of the Company s total revenues were:

	Three Months ended September 30		Nine Months ended September 30	
	2011	2010	2011	2010
Customer A	19%	10%	22%	14%
Customer B	22%	14%	22%	17%
Customer C	25%	29%	19%	30%

The Company s non-affiliate customers whose individual balances amounted to more than 10% of the Company s net accounts receivable, expressed as a percentage of net accounts receivable, were:

	September 30 2011	December 31 2010
Customer A	19%	
Customer B	58%	75%
Customer C	20%	16%

The Company performs ongoing credit evaluations of its customers and generally does not require collateral. The Company also maintains allowances for potential credit losses. The loss of a major customer could have a material adverse effect on the Company s business operations and financial condition.

The Company s revenues by geographic region are as follows:

	Three Months ended September 30		Nine Months ended September 30	
	2011	2010	2011	2010
North America	$ 127,100	$ 139,600	$ 407,000	$ 340,500
Asia	45,600	17,900	150,800	61,900
South America		24,300	27,400	24,300
	$ 172,700	$ 181,800	$ 585,200	$ 426,700

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

Forward-Looking Information

This Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 (the Exchange Act), regarding, among other things, anticipated improvements in operations, the Company s plans, earnings, cash flow and expense estimates, strategies and prospects, both business and financial. All statements other than statements of current or historical fact contained in this report are forward-looking statements. The words believe, expect, anticipate, should, plan, &#