

Scio Diamond Technology Corp
Form 10-Q
November 23, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2016

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT OF 1934

For the transition period from to

Commission file number: 000-54529

SCIO DIAMOND TECHNOLOGY CORPORATION

(Exact name of registrant as specified in its charter)

Nevada

45-3849662

Edgar Filing: Scio Diamond Technology Corp - Form 10-Q

(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.) organization)

411 University Ridge Suite D

Greenville, SC 29601

(Address of principal executive offices, including zip code)

(864) 751-4880

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

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). x Yes o No

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

Smaller Reporting Company x

(Do not check if smaller reporting company)

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

The number of shares of common stock, \$0.001 par value, outstanding as of November 17, 2016 was 65,098,291.

SCIO DIAMOND TECHNOLOGY CORPORATION

TABLE OF CONTENTS

	PAGE
<u>PART I FINANCIAL INFORMATION</u>	
ITEM 1. <u>FINANCIAL STATEMENTS</u>	4
ITEM 2. <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	19
ITEM 3. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	25
ITEM 4. <u>CONTROLS AND PROCEDURES</u>	25
<u>PART II OTHER INFORMATION</u>	
ITEM 1. <u>LEGAL PROCEEDINGS</u>	26
ITEM 1A. <u>RISK FACTORS</u>	26
ITEM 2. <u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	26
ITEM 3. <u>DEFAULTS UPON SENIOR SECURITIES</u>	26
ITEM 4. <u>MINE SAFETY DISCLOSURES</u>	26
ITEM 5. <u>OTHER INFORMATION</u>	26
ITEM 6. <u>EXHIBITS</u>	27

Special Note Regarding Forward-Looking Statements

Information included in this Quarterly Report on Form 10-Q contains forward-looking statements that reflect the views of the management of the Company with respect to certain future events. Forward-looking statements made by penny stock issuers such as the Company are excluded from the safe harbor in Section 21E of the Securities Exchange Act of 1934 (the “Exchange Act”). Words such as “expects,” “should,” “may,” “will,” “believes,” “anticipates,” “intends,” “plans,” “estimates” and similar expressions or variations of such words, and negatives thereof, are intended to identify forward-looking statements, but are not the exclusive means of identifying forward-looking statements in this report. These forward-looking statements are based on assumptions that may be incorrect, and there can be no assurance that matters anticipated in our forward-looking statements will come to pass.

Forward-looking statements are subject to certain risks and uncertainties which could cause actual results to differ materially from those anticipated. Such risk and uncertainties include, without limitation, those described under Risk Factors set forth in Part I, Item 1A of our Form 10-K for the fiscal year ended March 31, 2016 filed on July 14, 2016.

You are cautioned not to place undue reliance on forward-looking statements. You are also urged to review and consider carefully the various disclosures made in the Company’s other filings with the Securities and Exchange Commission (“SEC”), including amendments to those filings, if any. Except as may be required by applicable laws, the Company undertakes no obligation to update publicly any forward-looking statements for any reason, even if new information becomes available or other events occur in the future.

PART I - FINANCIAL INFORMATION**ITEM 1. UNAUDITED CONDENSED FINANCIAL STATEMENTS****SCIO DIAMOND TECHNOLOGY CORPORATION****CONDENSED BALANCE SHEETS****As of September 30, 2016 and March 31, 2016**

	September 30, 2016 (Unaudited)	March 31, 2016
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 9,947	\$ 192,880
Accounts receivable	204,539	175,448
Deferred contract costs	142,471	142,471
Inventory, net	88,889	189,527
Prepaid expenses	30,181	52,150
Prepaid rent	7,712	19,238
Total current assets	483,739	771,714
Property, plant and equipment		
Facility	886,630	886,630
Manufacturing equipment	3,308,299	3,294,425
Other equipment	73,543	73,543
Construction in progress	11,107	24,981
Total property, plant and equipment	4,279,579	4,279,579
Less accumulated depreciation	(2,401,699)	(2,085,508)
Net property, plant and equipment	1,877,880	2,194,071
Intangible assets, net		
Investment in joint venture – RCDC	6,742,701	7,225,446
	19,530	48,271
TOTAL ASSETS	\$ 9,123,850	\$ 10,239,502
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 635,017	\$ 438,466

Edgar Filing: Scio Diamond Technology Corp - Form 10-Q

Customer deposits	4,784	46,096
Deferred revenue	174,280	174,280
Accrued expenses	571,160	353,921
Convertible notes	105,600	—
Current portion of notes payable	98,999	98,999
Current portion of capital lease obligation	122,495	122,495
Total current liabilities	1,712,335	1,234,257
Notes payable, non-current	2,201,001	2,201,001
Capital lease obligation, non-current	71,994	71,994
Other liabilities	73,807	88,569
TOTAL LIABILITIES	4,059,137	3,595,821
Common stock \$0.001 par value, 75,000,000 shares authorized; 65,098,291 and 63,919,291 shares issued and outstanding at September 30, 2016 and March 31, 2016, respectively	65,098	63,919
Additional paid-in capital	29,471,323	28,942,060
Accumulated deficit	(24,471,708)	(22,362,298)
Total shareholders' equity	5,064,713	6,643,681
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 9,123,850	\$ 10,239,502

The accompanying notes are an integral part of these unaudited condensed financial statements.

SCIO DIAMOND TECHNOLOGY CORPORATION

CONDENSED STATEMENTS OF OPERATIONS

For the Three and Six Months ended September 30, 2016 and 2015

(Unaudited)

	Three Months Ended September 30, 2016	Three Months Ended September 30, 2015	Six Months Ended September 30, 2016	Six Months Ended September 30, 2015
Revenue				
Revenue, net	\$ 242,066	\$ 236,292	\$ 427,127	\$ 408,467
Cost of goods sold				
Cost of goods sold	557,026	461,279	1,104,175	876,646
Gross margin (deficit)	(314,960)	(224,987)	(677,048)	(468,179)
General and administrative expenses				
Salaries and benefits	267,764	255,389	580,353	457,691
Professional fees	79,478	44,122	220,566	96,065
Rent and facilities expense	34,133	40,961	75,917	79,974
Marketing costs	10,339	28,463	13,410	56,646
Corporate general and administrative	50,075	146,631	125,670	232,178
Depreciation and amortization	245,460	198,477	490,920	396,882
Reversal of severance liability	—	(137,561)	—	(137,561)
Loss from operations	(1,002,209)	(801,469)	(2,183,884)	(1,650,054)
Other income/(expense)				
Proceeds from insurance	235,395	—	235,395	—
Income (loss) from RCDC joint venture	(8,372)	18,363	(28,741)	34,702
Interest expense	(70,064)	(26,482)	(132,180)	(71,331)
Net loss	\$ (845,250)	\$ (809,588)	\$ (2,109,410)	\$ (1,686,683)
Loss per share				
Basic:				
Weighted average number of shares outstanding	63,213,291	58,385,140	62,831,990	57,464,860
Loss per share	\$ (0.01)	\$ (0.01)	\$ (0.03)	\$ (0.03)
Fully diluted:				

Edgar Filing: Scio Diamond Technology Corp - Form 10-Q

Weighted average number of shares outstanding	63,213,291	58,385,140	62,831,990	57,464,860	
Loss per share	\$ (0.01) \$ (0.01) \$ (0.03) \$ (0.03)

The accompanying notes are an integral part of these unaudited condensed financial statements.

SCIO DIAMOND TECHNOLOGY CORPORATION
CONDENSED STATEMENTS OF CASH FLOW
For the Six Months Ended September 30, 2016 and 2015

(Unaudited)

	Six Months Ended September 30, 2016	Six Months Ended September 30, 2015
Cash flows from operating activities:		
Net loss	\$ (2,109,410)) \$ (1,686,683)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	802,836	685,349
Employee stock-based compensation	302,666	187,967
Loss/(Income) from joint venture - RCDC	28,741	(34,702)
Changes in assets and liabilities:		
Decrease/(increase) in accounts receivable and deferred revenue	(29,091)) 23,810
Decrease in prepaid expenses and rent	29,595	22,710
Decrease/(increase) in inventory and deferred contract costs	100,638	(37,704)
Increase/(decrease) in accounts payable	196,551	(148,888)
Decrease in customer deposits	(41,312)) (24,692)
Increase/(decrease) in accrued expenses	217,239	(186,473)
Decrease in other liabilities	(14,762)) (12,301)
Net cash used in operating activities	(516,309)) (1,211,607)
Cash flows from investing activities:		
Purchase of property, plant and equipment	—	(189,043)
Net cash used in investing activities	—	(189,043)
Cash flows from financing activities:		
Proceeds from the sale of common stock – net of fees	227,776	1,565,000
Proceeds from the exercise of stock options	—	11,238
Proceeds from sale of convertible notes	105,600	—
Net cash provided by financing activities	333,376	1,576,238
Change in cash and cash equivalents	(182,933)) 175,588
Cash and cash equivalents, beginning of period	192,880	767,214
Cash and cash equivalents, end of period	\$ 9,947	\$ 942,802

The accompanying notes are an integral part of these unaudited condensed financial statements.

(continued)

6

SCIO DIAMOND TECHNOLOGY CORPORATION
CONDENSED STATEMENTS OF CASH FLOW
For the Six Months Ended September 30, 2016 and 2015 (Unaudited)
(Continued)

	Six Months Ended September 30, 2016	Six Months Ended September 30, 2015
Supplemental cash flow disclosures:		
Cash paid for:		
Interest	\$ —	\$ 72,097
Income taxes	\$ —	\$ —
Non-cash investing and financing activities:		
Purchase of property, plant and equipment in accounts payable	\$ —	\$ 92,000
Reclass of debt to capital lease due to completion of sale leaseback transaction	\$ —	\$ 200,000

The accompanying notes are an integral part of these unaudited condensed financial statements.

SCIO DIAMOND TECHNOLOGY CORPORATION
CONDENSED STATEMENTS OF SHAREHOLDERS' EQUITY
For the period April 1, 2016 through September 30, 2016

(Unaudited)

	Common Stock Shares	Common Stock Amount	Additional Paid in Capital	Accumulated Deficit	Total
Balance, April 1, 2016	63,919,291	\$63,919	\$28,942,060	\$(22,362,298)	\$6,643,681
Common stock issued for cash @ \$0.22 per share, net of brokerage fees of \$31,604	1,179,000	1,179	226,597	—	227,776
Stock-based incentive compensation	—	—	302,666	—	302,666
Net loss for the six months ended September 30, 2016	—	—	—	(2,109,410)	(2,109,410)
Balance, September 30, 2016	65,098,291	\$65,098	\$29,471,323	\$(24,471,708)	\$5,064,713

The accompanying notes are an integral part of these unaudited condensed financial statements.

NOTE 1 — ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Business

Scio Diamond Technology Corporation (referred to herein as the “Company”, “we”, “us” or “our”) was incorporated under the laws of the State of Nevada as Krossbow Holding Corp. on September 17, 2009. The Company’s focus is on man-made diamond technology development and commercialization.

Going Concern

The Company has generated little revenue to date and consequently its operations are subject to all risks inherent in the establishment and commercial launch of a new business enterprise. The Company continues to develop its diamond technology while operating its factory to maximize revenue. The Company experienced a process water leak in our facility in mid-December 2015 causing damage to our diamond growers and a temporary interruption in production. The shutdown had a significant negative impact on revenue and delayed attainment of the Company’s near-term business objectives. The Company’s insurance carrier provided it with \$350,000 during the fiscal year ended March 31, 2016, to cover the cost of the business interruption. Due to the on-going negative impact of the shutdown on our business, our insurance carrier has provided an additional \$235,395 in extended business indemnity payments through September 30, 2016.

These factors raise substantial doubt about the Company’s ability to continue as a going concern. Management has responded to these circumstances by implementing the following strategies and actions:

- Continuing efforts with insurance carrier to cover the costs of the business interruption and any future adverse financial effects of the shutdown;

- Continuing efforts to solicit investment in the Company in the form of private placements of common shares to accredited investors not to exceed the shares authorized;

- Continuing efforts to solicit investment in the Company in the form of secured and unsecured debt;
- Continue to optimize production of recently expanded existing manufacturing capabilities to increase product revenues;

- Continuing to focus efforts on new business development opportunities to generate revenues and expand and diversify the customer base;

- Continuing development of