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SCIENTIFIC INDUSTRIES INC
Form 10QSB
November 14, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

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

For quarterly period ended SEPTEMBER 30, 2006

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

For the transition period from _____ to _____

Commission File Number: 0-6658

SCIENTIFIC INDUSTRIES, INC.

(Exact name of small business issuer as specified in its charter)

Delaware 04-2217279
(State of incorporation) (I.R.S. Employer Identification No.)

70 ORVILLE DRIVE, BOHEMIA, NEW YORK 11716
(Address of principal executive offices)

(631)567-4700
(Issuer's telephone number)

NOT APPLICABLE

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

Check whether the issuer (1) filed all reports required to be filed by
Section 13 or 15(d) of the Exchange Act during the past 12 months (or for
such shorter period that the registrant was required to file such reports),
and (2) has been subject to such filing requirements for the past 90 days.

Yes [] No []

State the number of shares outstanding of each of the issuer's classes of
common equity, as of October 27, 2006: 1,000,352 shares outstanding of the
Company's Common Stock, par value, \$.05.

Transitional Small Business Disclosure Format (check one):

Yes [] No []

PART I-FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

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SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEET

ASSETS

September 30, 2006

Current Assets:	
Cash and cash equivalents	\$ 271,600
Investment securities	1,180,200
Trade accounts receivable, less allowance for doubtful accounts of \$10,600	466,300
Inventories	960,000
Prepaid expenses and other current assets	38,700
Deferred taxes	27,800
Total current assets	2,944,600
Property and equipment at cost, less accumulated depreciation of \$504,900	112,300
Intangible assets, less accumulated amortization of \$77,200	41,400
Other	38,600
Total assets	\$3,136,900 =====

LIABILITIES AND SHAREHOLDERS' EQUITY

Current Liabilities:	
Accounts payable	\$ 87,200
Accrued expenses and taxes	273,500
Dividends payable	70,000
Total current liabilities	430,700
Deferred taxes	5,500
Shareholders' equity:	
Common stock, \$.05 par value; authorized 7,000,000 shares; 1,020,154 issued and outstanding	51,000
Additional paid-in capital	1,010,500
Accumulated other comprehensive loss, unrealized holding loss on investment securities	(5,300)
Retained earnings	1,696,900
	2,753,100
Less common stock held in treasury, at cost, 19,802 shares	52,400
Total shareholders' equity	2,700,700
Total liabilities and shareholders' equity	\$3,136,900 =====

See notes to unaudited condensed consolidated financial statements

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For the Three Month Periods Ended
September 30, 2006 September 30, 2005

Net sales	\$ 802,900	\$ 890,000
Cost of goods sold	388,500	433,300
Gross profit	<u>414,400</u>	<u>456,700</u>
Operating Expenses:		
General and administrative	164,500	174,000
Selling	70,300	63,500
Research and development	79,300	91,800
	<u>314,100</u>	<u>329,300</u>
Income from operations	<u>100,300</u>	<u>127,400</u>
Interest and other income, net	14,300	7,500
Income before income taxes	114,600	134,900
Income taxes, all current	37,000	38,000
Net income	<u>\$ 77,600</u>	<u>\$ 96,900</u>
Basic earnings per common share	\$.08	\$.10
Diluted earnings per common share	\$.07	\$.09
Cash dividends declared per common share	\$.07	\$.09

See notes to unaudited condensed consolidated financial statements

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Three Month Periods Ended
September 30, 2006 September 30, 2005

Operating activities:		
Net income	\$ 77,600	\$ 96,900
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		

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Loss on sale of investments	-	2,500
Depreciation and amortization	13,000	16,400
Change in assets and liabilities:		
Accounts receivable	(152,400)	(101,900)
Inventories	(29,700)	(52,300)
Prepaid expenses and other current assets	65,200	8,000
Other assets	100	(1,100)
Accounts payable	19,100	11,100
Accrued expenses and taxes	61,200	1,700
Deferred compensation	-	1,100
	<hr/>	<hr/>
Total adjustments	(23,500)	(114,500)
	<hr/>	<hr/>
Net cash provided by (used in) operating activities	54,100	(17,600)
	<hr/>	<hr/>
Investing activities:		
Purchase of investment securities, available for sale	(6,000)	(154,300)
Redemptions of investment securities, available for sale	-	123,900
Redemptions of investment securities, held to maturity	-	15,000
Capital expenditures	-	(3,400)
Purchase of intangible assets	(4,200)	(17,800)
	<hr/>	<hr/>
Net cash used in investing activities	(10,200)	(36,600)
	<hr/>	<hr/>
Net (decrease) increase in cash and cash equivalents	43,900	(54,200)
Cash and cash equivalents, beginning of year	227,700	183,900
	<hr/>	<hr/>
Cash and cash equivalents, end of period	\$ 271,600	\$ 129,700
	=====	=====
Supplemental disclosures:		
Cash paid during the period for:		
Income Taxes	\$ 36,000	\$ 58,300

See notes to unaudited condensed consolidated financial statements

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

General: The accompanying unaudited interim condensed consolidated financial statements are prepared pursuant to the Securities and Exchange Commission's rules and regulations for reporting on Form 10-QSB. Accordingly, certain information and footnotes required by accounting principles generally accepted in the United States for complete financial statements are not included

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herein. The Company believes all adjustments necessary for a fair presentation of these interim statements have been included and are of a normal and recurring nature. These interim statements should be read in conjunction with the Company's financial statements and notes thereto, included in its Annual Report on Form 10-KSB for the fiscal year ended June 30, 2006. The results for the three months ended September 30, 2006, are not necessarily an indication of the results that may be expected for the full fiscal year ending June 30, 2007.

1. Significant accounting policies:

Principles of consolidation:

The accompanying condensed consolidated financial statements include the accounts of the Company and Scientific Packaging Industries, Inc., a New York corporation which is an inactive wholly-owned subsidiary of the Company. All intercompany items and transactions have been eliminated in consolidation.

2. Line of Business and Concentrations:

The Company is engaged in manufacturing and marketing of equipment for research in university, hospital and industrial laboratories. The Company believes that it has only one reportable segment. Approximately 73% and 67% of net sales for the three month periods ended September 30, 2006 and 2005, respectively, were derived from the Company's main product, the Vortex-Genie 2(R) mixer, excluding accessories.

The Company's export sales (principally Europe and Asia) were approximately \$339,900 and \$349,500 (42% and 39% of net sales) for the three month periods ended September 30, 2006 and 2005, respectively.

Two of the Company's customers accounted in the aggregate for 34% of net sales for the three month period ended September 30, 2006. Three of the Company's customers accounted in the aggregate for 52% of net sales for the three month period ended September 30, 2005.

During the fourth quarter of fiscal 2006, the Company's principal customer and distributor advised the Company that it would no longer market and buy the Company's products. Sales to this customer accounted for approximately 28% of net sales for the three months ended September 30, 2005. There were no sales to this customer in the three months ended September 30, 2006.

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

3. Inventories:

Inventories for interim financial statement purposes are based

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on perpetual inventory records. Components of inventory are as follows:

	September 30, 2006
Raw Materials	\$ 866,300
Work in process	32,400
Finished Goods	61,300
	\$ 960,000
	=====

4. Earnings per common share:

Basic earnings per common share is computed by dividing net income by the weighted-average number of shares outstanding. Diluted earnings per common share includes the dilutive effect of stock options and a warrant, which was exercised during the three months ended September 30, 2005.

Earnings per common share was computed as follows:

	For the Three Month Periods Ended	
	September 30, 2006	September 30, 2005
Net income	\$ 77,600	\$ 96,900
	=====	=====
Weighted average common shares outstanding	1,000,352	980,310
Effect of dilutive securities	58,968	80,515
	-----	-----
Weighted average dilutive common shares outstanding	1,059,320	1,060,825
	=====	=====
Basic earnings per common share	\$.08	\$.10
	=====	=====
Diluted earnings per common share	\$.07	\$.09
	=====	=====

All options outstanding for the three months ended September 30, 2006 and the options and warrant outstanding during the three months ended September 30, 2005 were included in the foregoing computations on a weighted average basis.

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

5. Comprehensive Income:

There was no significant difference between net income and comprehensive income for the three month periods ended September 30, 2006 and 2005.

6. Stock-Based Compensation Plans

The Company maintains an Incentive Stock Option Plan which

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through the fiscal year ended June 30, 2006 it accounted for under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related Interpretations. Under this method, no stock-based compensation costs were reflected in net income, as all options granted under those plans had an exercise price equal to the fair market value of the underlying common stock on the date of grant. The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation in the prior period:

For the Three Month Period Ended
September 30, 2005

Net income:		
As reported	\$	96,900
Pro Forma		96,400
Earnings per common and common equivalent share:		
Basic - as reported	\$.10
Basic - pro forma	\$.10
Diluted - as reported	\$.09
Diluted - pro forma	\$.09

Any stock-based compensation transaction subsequent to June 30, 2006 is to be accounted for using Statement of Financial Accounting Standards No. 123(R)). This statement, issued on December 16, 2004, by the Financial Accounting Standards Board, requires compensation costs related to stock-based payment transactions to be recognized commencing with our fiscal year ending June 30, 2007. With limited exceptions, the amount of compensation cost is measured based on the grant-date fair value of the equity or liability instruments issued. In addition, liability awards will be measured each reporting period. Compensation cost are recognized over the period that an employee provides service in exchange for the award. Statement 123(R)) replaces FASB Statement No. 123, Accounting for Stock-Based Compensation, and supercedes APB Opinion No. 25, accounting for Stock Issued to Employees. The Company did not incur any stock-based compensation costs for the three months ended September 30, 2006.

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS

Certain statements contained in this report are not based on historical facts, but are forward-looking statements that are based upon various assumptions about future conditions. Actual events in the future could differ materially from those described in the forward-looking information. Numerous unknown factors and future events could cause such differences, including but not limited to, product demand, market acceptance, success of marketing strategy, success of expansion efforts, impact of competition, adverse economic conditions, and other factors affecting the Company's business that are beyond the Company's

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control, which are discussed elsewhere in this report. Consequently, no forward-looking statement can be guaranteed. The Company undertakes no obligation to publicly update forward-looking statements, whether as a result of new information, future events or otherwise. This Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with our financial statements and the related notes included elsewhere in this report.

Liquidity and Capital Resources

Net cash provided by operating activities increased by \$71,700 to \$54,100 for the three month period of the current fiscal year as compared to (\$17,600) used in operating activities in the comparative period of the prior fiscal year. The principal factors accounting for the difference were lower prepaid expenses and other assets and higher accrued expenses and taxes at September 30, 2006 compared to year end, partially offset by higher accounts receivable. Cash used in investing activities was (\$10,200) for the three months ended September 30, 2006 as compared to (\$36,600) used in the three months ended September 30, 2005 reflecting lower net purchases of investment securities and lower capital expenditures during the current year three month period. As a result of the foregoing, cash and cash equivalents increased by \$43,900 to \$271,600 as of September 30, 2006 from a balance of \$227,700 as of June 30, 2006 as compared to a balance of \$129,700 as of September 30, 2005, reflecting a \$54,200 decrease from \$183,900 as of June 30, 2005.

On September 29, 2006, the Board of Directors of the Company declared a cash dividend of \$.07 per share of Common Stock payable on January 12, 2007 to holders of record as of the close of business on October 30, 2006.

The Company's working capital of \$2,513,900 as of September 30, 2006 was similar to the working capital of \$2,489,100 at June 30, 2006. The Company has available for its working capital needs, a secured bank line of credit of \$200,000 with North Fork Bank with interest at prime, all of which was available as of September 30, 2006. The Company has never borrowed under this line of credit. Management believes that the Company will be able to meet its cash flow needs during the next 12 months from its available financial resources which include its cash and investment securities.

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY

If a proposed acquisition, the subject of an outstanding agreement in principle, is consummated, the acquisition consideration will be 125,000 shares of the Company's Common Stock and payment by the Company in cash of \$400,000 plus four future annual contingent payments based on net sales of the acquired entity.

Financial Overview

The income before income taxes for the quarter September 30, 2006, (the "September 30, 2006 Quarter") was \$114,600, a 15% decrease from \$134,900 for the three months ended September 30, 2005 (the "September 30, 2005 Quarter") principally the result of a \$87,100 reduction in net sales (\$802,900 compared to \$890,000).

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During the fourth quarter of fiscal 2006, the Company was informed by its then principal customer and distributor for more than 30 years of its decision to discontinue marketing the Company's products, which the Company believes was the result of a change in its marketing and selling focus to its private label products. As a result, there were no sales to this customer during the September 30, 2006 Quarter as compared to approximately \$253,000 of sales to this customer during the September 30, 2005 Quarter. To diminish the impact, the Company has pursued other selling outlets including appointing new distributors, increasing sales to distributors through cooperative promotional efforts and other agreements, increased advertising activity, and expanded direct selling efforts.

Results of Operations

The Three Months Ended September 30, 2006 Compared with the Three Months Ended September 30, 2005

The Company's net sales for the three months ended September 30, 2006 (the "September 30, 2006 Quarter") decreased \$87,100 (9.8%) to \$802,900 from \$890,000 for the three months ended September 30, 2005 (the "September 30, 2005 Quarter"), principally the result of a \$253,000 decrease in sales to our previous major customer, partially offset by increased sales to other distributors and higher direct sales. The gross profit percentage for the September 30, 2006 Quarter was 51.6% compared to 51.3% for the September 30, 2005 Quarter, mainly the result of higher direct sales and lower dealer discounts.

General and administrative expenses for the September 30, 2006 Quarter were \$164,500, a decrease of \$9,500 (5.5%) from \$174,000 for the September 30, 2005 Quarter due to lower legal expenses.

Selling expenses of \$70,300 for the September 30, 2006 Quarter were \$6,800 (10.7%) higher than \$63,500 for the September 30, 2005 Quarter primarily due to higher advertising expenses.

Lower contract engineering costs was the principal reason for the \$12,500 (13.6%) decrease in research and development expenses for the September 30, 2006 Quarter to \$79,300 from \$91,800 for the September 30, 2005 Quarter.

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY

Interest and other income increased \$6,800 to \$14,300 for the September 30, 2006 Quarter compared with \$7,500 for the September 30, 2005 Quarter mainly due to higher interest rates and balances of investment securities.

As a result of the foregoing, income before income taxes was \$114,600 for the September 30, 2006 Quarter, reflecting a \$20,300 (15.0%) decrease from \$134,900 for the September 30, 2005 Quarter.

Income taxes amounted to \$37,000 (32.3% effective rate) for the September 30, 2006 Quarter as compared to \$38,000 (28.2% effective rate) for the comparable period last year. The higher tax rate was principally due to no research and development credits available during the September 30, 2006 Quarter. Net income,

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accordingly, for the September 30, 2006 Quarter was \$77,600, a 19.9% decrease from \$96,900 for the September 30, 2005 Quarter.

ITEM 3. CONTROLS AND PROCEDURES

As of the end of the period covered by this report, based on an evaluation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange

Act of 1934), the Chief Executive and Chief Financial Officer of the Company concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in its Exchange Act reports is recorded, processed, summarized and reported within the applicable time periods specified by the SEC's rules and forms.

There was no change in the Company's internal controls over financial reporting that occurred during the most recent fiscal quarter that materially affected or is reasonably likely to materially affect the Company's internal controls over financial reporting.

SCIENTIFIC INDUSTRIES, INC. AND SUBSIDIARY

PART II - OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibit Number:	Description
31.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K:

Registrant filed a report on Form 8-K on August 7, 2006 reporting under Item 8.01, Other Events.

SIGNATURE

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, hereunto duly authorized.

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Scientific Industries, Inc.

Registrant

Date November 14, 2006

/s/Helena R. Santos

Helena R. Santos
President, Chief Executive Officer
and Treasurer
Chief Financial and Principal
Accounting Officer