

Scio Diamond Technology Corp  
Form 10-K  
June 29, 2015

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

**FORM 10-K**

**(Mark One)**

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

**For the fiscal year ended March 31, 2015**

**Or**

- 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: 000-54529**

**SCIO DIAMOND TECHNOLOGY CORPORATION**

(Exact name of registrant as specified in its charter)

**Nevada**

(state or other jurisdiction of incorporation or organization)

**45-3849662**

(I.R.S. Employer I.D. No.)

**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)

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

**None**

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

**Common Stock, par value \$0.001**

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

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

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

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

Indicate by 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 (§ 332.405 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  No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

The aggregate market value of voting common stock held by non-affiliates of the registrant as of September 30, 2014, the last business day of the registrant's most recently completed second fiscal quarter, computed by reference to the closing sale price of the registrant's common stock on that date, was approximately \$20,002,182.

The number of shares of common stock outstanding as of June 23, 2015 \$0.001 par value, was 57,516,499.

**INDEX**

<u>PART I</u>	4
<u>ITEM 1. BUSINESS</u>	4
<u>ITEM 1A. RISK FACTORS</u>	10
<u>ITEM 1B. UNRESOLVED STAFF COMMENTS</u>	20
<u>ITEM 2. PROPERTIES</u>	21
<u>ITEM 3. LEGAL PROCEEDINGS</u>	21
<u>ITEM 4. MINE SAFETY DISCLOSURES</u>	21
<u>PART II</u>	22
<u>ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	22
<u>ITEM 6. SELECTED FINANCIAL DATA</u>	23
<u>ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	23
<u>ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	29
<u>ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	30
<u>ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS AND FINANCIAL DISCLOSURE</u>	47
<u>ITEM 9A. CONTROLS AND PROCEDURES</u>	47
<u>ITEM 9B. OTHER INFORMATION</u>	48
<u>PART III</u>	49
<u>ITEM 10. DIRECTORS, EXECUTIVE OFFICERS, AND CORPORATE GOVERNANCE</u>	49
<u>ITEM 11. EXECUTIVE COMPENSATION</u>	49
<u>ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	49
<u>ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE</u>	49

<u>ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES</u>	50
<u>PART IV</u>	51
<u>ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES</u>	51

## **CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

This Report, including information included or incorporated by reference in this document, contains statements which constitute forward-looking statements. 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. Forward-looking statements may relate to our financial condition, results of operation, plans, objectives, or future performance. These statements are based on many assumptions and estimates and are not guarantees of future performance. Our actual results may differ materially from those anticipated in any forward-looking statements, as they will depend on many factors about which we are unsure, including many factors which are beyond our control. The words “may,” “would,” “could,” “should,” “will,” “expect,” “anticipate,” “predict,” “project,” “potential,” “believe,” “continue,” “assume,” “intend,” “plan,” and “estimate” and similar expressions, are meant to identify such forward-looking statements.

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 below under Item 1A - Risk Factors and the following: (1) the Company has limited cash resources and if it is not able to obtain further financing required for continuing operations, marketing, product development, and research its business operations will fail, (2) the Company has not generated substantial revenues or cash flow from operations, and as a result, faces a high risk of business failure, (3) the Company’s lack of diversification and dependence on material customers increases the risks associated with the Company’s business and an investment in the Company, and the Company’s financial condition may deteriorate rapidly if it fails to succeed in developing the Company’s business and expanding our customer base, (4) the Company may not effectively execute the Company’s business plan or manage the Company’s potential future business development, (5) ) the Company may expend a substantial amount of time and resources in connection with the Securities and Exchange Commission’s (“SEC”) recent subpoena, potential inquiries or legal actions in connection with its filings with the SEC or otherwise, which may impair the Company’s ability to raise capital and to operate its business, (6) the Company’s business could be impaired if it fails to comply with applicable regulations, (7) the Company has had significant turnover in management and may not be able to retain key management personnel to manage the Company or laboratory scientists to carry out the Company’s business operations, which could have a material adverse effect on the Company’s business, (8) the market for lab-grown diamond may not develop as anticipated, and (9) competition may adversely affect our business. You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date hereof. The Company undertakes no obligation to publish revised forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrences of unanticipated events. You are also urged to review and consider carefully the various disclosures made hereafter by the Company from time to time with its SEC filings.

## **PART I**

### **ITEM 1. BUSINESS**

#### *Corporate History*

We were incorporated on September 17, 2009 in the State of Nevada under the name Krossbow Holdings Corporation (“Krossbow”). Krossbow did not implement its original business plan and decided to acquire existing technology to seek to efficiently and effectively produce man-made diamond. In connection with this change in business purpose, Krossbow changed its name to Scio Diamond Technology Corporation to reflect its new business direction.

On August 5, 2011, Edward S. Adams and Michael R. Monahan acquired control of the Company through the purchase of shares of the Company’s issued and outstanding common stock from Jason Kropp, Krossbow’s sole director and executive officer at that time. Messrs. Monahan and Adams served on the Company’s Board of Directors until their resignations from the Board on June 30, 2013, and June 23, 2014, respectively. Additionally, on August 5, 2011, the Company executed an Asset Purchase Agreement with another privately-held Nevada corporation that also had the name “Scio Diamond Technology Corporation” (“Private Scio”). Under the terms of the Asset Purchase Agreement, the Company purchased the name “Scio Diamond Technology Corporation” and acquired other rights from Private Scio for 13,000,000 newly issued shares of common stock of the Company.

On August 31, 2011, the Company acquired certain assets of Apollo Diamond, Inc. (“ADI”) (the “ADI Asset Purchase”), consisting primarily of diamond growing machines and intellectual property related thereto, for which the Company paid ADI an aggregate of \$2,000,000. In connection with the ADI Asset Purchase, the Company also agreed to provide certain current and former stockholders of ADI qualifying as accredited investors the opportunity to acquire up to approximately 16 million shares of common stock of the Company for \$0.01 per share (the “ADI Offering”).

On June 5, 2012, the Company acquired substantially all of the assets of Apollo Diamond Gemstone Corporation (“ADGC”) (the “ADGC Asset Purchase”), consisting primarily of lab-grown diamond gemstone-related know-how, inventory, and various intellectual property, in exchange for \$100,000 in cash and the opportunity for certain current and former stockholders of ADGC qualifying as accredited investors to acquire up to approximately 1 million shares of common stock of the Company for \$0.01 per share (the “ADGC Offering”) with the intent that ADI Offering be conducted substantially concurrently with the ADGC Offering (collectively, the “ADI/ADGC Offering”).

In December, 2011, the Company began a build-out of its Greenville, South Carolina production facility. Construction was largely completed in March 2012 and equipment was moved from ADI’s former facility in Massachusetts to South Carolina over the first calendar quarter of 2012. The Company began initial production with ten diamond growing machines in July 2012.

Since July 2012, the Company has been operational with ten diamond growing machines in our Greenville facility. Through March of 2013, the Company’s production was focused on industrial cutting tool products supplied to a single customer. Subsequent to March 2013, the Company has expanded its product focus to include diamond gemstone material as well as industrial materials.

On September 16, 2013, the Company entered into a series of agreements with SAAMABA, LLC and S21 Research Holdings (the “Grace Rich Agreements”) to form a joint venture (“Grace Rich LTD”) with operations in the People’s Republic of China (“PRC”) to deploy over 100 Company designed diamond growing machines. Under the Grace Rich Agreements, the Company has agreed to license its proprietary technology for the manufacture of diamond gemstones of agreed upon specifications. In exchange for the license, the Company received licensing and development revenue and a 30% ownership position in the joint venture. In addition to the licensed technology, the Grace Rich Agreements include obligations for the Company to provide and be compensated for technology consulting services to the joint

venture to support the start-up of operations. The Company does not control the joint venture and is not required to make any on-going funding contributions to the joint venture and our ownership stake cannot be reduced from 30%.

On December 16, 2014, the Company entered into an agreement for the Sale and Lease of Growers (the “Grower Sale-Lease Agreement”) with Heritage Gemstone Investors, LLC (“HGI”). Pursuant to the Grower Sale-Lease Agreement, the Company agreed to a sale-leaseback arrangement for certain diamond growers produced by the Company during the term of the Grower Sale-Leaseback Agreement by which the Company will sell diamond growers to HGI and then lease the growers back from HGI. The direct profit margin generated from the growers will be split between the Company and HGI in accordance with the Grower Sale-Lease Agreement. The Grower Sale-Lease Agreement requires the Company to operate and service the growers, and requires HGI to up-fit certain existing growers and to make capital improvements to the new growers under certain circumstances. The Company will also have the right to repurchase the leased growers upon the occurrence of certain events.

On December 18, 2014 entered into an arrangement with Renaissance Diamonds, Inc. (“Renaissance”) creating Renaissance Created Diamond Company, LLC (“RCDC”). The Company and Renaissance are each 50% members of RCDC. The arrangement was entered into in order to facilitate the development of procedures and recipes for, and to market and sell, lab-grown fancy-colored diamonds. RCDC will purchase rough diamond material from the Company and process and finish the material into finished gemstones for sale to various retailers and other participants in the market for gemstones. Profits generated by RCDC’s operations will be distributed between the Company and Renaissance according to the terms of the LLC Agreement.

## ***Our Business***

### *General*

The Company is first and foremost a materials company that has developed proprietary technology through which high quality single crystal diamond materials are produced through a chemical vapor deposition (“CVD”) process (the “Diamond Technology”). The Company’s primary mission is the development of profitable and sustainable commercial production of its diamond materials, which are suitable for known, emerging and anticipated industrial, technology and consumer applications. The Company intends to pursue progressive development of its core diamond materials technologies and related intellectual property that the Company hopes will evolve into product opportunities across various applications. We believe these opportunities may be monetized through a combination of end product sales, joint ventures and licensing arrangements with third parties, and through continued development of intellectual property. Anticipated application opportunities for the Company’s diamond materials include the following: precision cutting devices, diamond gemstone jewelry, power switches, semiconductor processors, optoelectronics, geosciences, water purification, and MRI and other medical science technology.

Prior to October 1, 2011, the Company was a development stage company. Developmental activities ceased and the Company commenced producing diamond materials in July 2012. Less than three years into production, the Company is already in the initial phases of commercializing the Diamond Technology and its goal is to become a preferred manufacturer of single crystal diamond and a leading global supplier of diamond materials for multiple applications. The Company hopes to further shape the evolution of various markets for its product and to leverage the technical foundation of the Diamond Technology by expanding into strategic partnerships with select industry leaders with distribution channels already in place to capture high value application opportunities.

As of March 31, 2015, nearly all of the Company’s production capacity is being sold for use in the gemstone market. As of March 31, 2015 we had generated \$3,026,282 in cumulative net revenue. Through March 31, 2015, over 50% of our product has been sold overseas and 100% of these sales have been to external customers and to our joint venture partners as discussed in Item 8, Notes 10 and 11.

### ***The Diamond Technology***

We acquired our Diamond Technology primarily from ADI. ADI was originally founded in 1990 with the goal of developing and perfecting two advanced semiconductor materials, gallium nitride (now used in light emitting diodes) and diamond. From 2000 onward, ADI focused solely on diamond and developing a process by which large, single-crystal diamond could be grown in a controlled laboratory environment.

The core Diamond Technology that was acquired by the Company is based on a CVD diamond growth system. Diamond wafers produced through the Diamond Technology CVD process have been shown to be exceptionally pure (nitrogen content < 10 ppb), and possess low levels of structural defects. Advances in this technology have dramatically improved the quality, and lowered the cost of high-quality diamond, resulting in new applications of diamond in electronics, optics, high power devices and quantum computing.



The Diamond Technology provides a materials production platform and is supported by intellectual property, including trade secrets, 36 issued patents (27 in the United States and 9 in foreign jurisdictions).

Our Diamond Technology utilizes CVD growth technology to produce diamond crystals. This technology utilizes a highly scalable manufacturing process for producing large size, high-quality diamond crystals at a low cost. Unlike the high-pressure, high-temperature (“HPHT”) process, the Diamond Technology process allows for concurrent production of multiple diamond crystals.

The Company’s diamond crystals are grown on small slices of diamond called “seeds” that the Company either grows internally or acquires from third parties. Over time, the Company has been able to transition to larger seeds than previously used. This transition allows the Company to see a substantial increase in the size of the material it is producing and allows for the Company to better match its production to specific customer needs.

In addition to utilizing larger “seeds,” our process can also be scaled through larger capacity diamond growing machines. The Company has successfully developed 4-inch growing technology that allows for up to a 100% increase in production capacity from the current 3-inch growing technology. The Company is implementing this new technology across its production platform and anticipates being substantially complete with the upgrade during the first fiscal quarter of 2016.

Finally, we expect that as we increase our production levels, our production costs per carat will actually decrease due to economies of scale.

### ***Facilities***

The Company’s production facility is located in Greenville, South Carolina. This facility, covering 9,470 square feet of leased space including both our headquarters and our production facility, was substantially completed and ready for production as of June 30, 2012. Ten of the production reactors purchased from ADI were installed in the facility and are currently operating. The Company is in the process of adding two additional reactors to the Greenville facility which we believe is the maximum capacity of this facility.

The Grace Rich LTD joint venture’s production facility is under development in the PRC and is not operational as of March 31, 2015.

### ***Products and Markets***

The current market for laboratory-grown diamond remains largely unknown and uncertain. Sales of laboratory-grown diamond into the gemstone market are thought to be very small currently. The industrial market for these products is more developed, but it is diffused globally and the Company is unable to reliably estimate its size or breadth.

In addition to the precision cutting market and opportunities for the Company in the diamond gemstone market, we will continue to explore other opportunities for our diamond materials through applications where the unique properties of diamond may be desirable and advantageous, including: alternative energy, optoelectronics, communications, biotechnology, water treatment, quantum computing and the diamond device arenas.

Competitive factors that will influence the market for our products include product quality, consistency of supply and price. We believe that we will be able to compete on the basis of these factors. We believe that we will be able to reliably and efficiently produce lab-grown diamond possessing substantially the same qualities and characteristics of their mined diamond counterparts.

### ***Gemstones***

Within the gemstone industry, our single-crystal diamond can be used in jewelry products requiring the highest quality gemstones and can be regularly grown in matched color sets ranging in polished sizes from 5-points (0.05 carats) to over 1.50 carats. Our diamond may be well suited for jewelry featuring matching diamond of various sizes, clarities and colors, diamond engagement rings, and fashion jewelry. The potential consistency and other potential characteristics of lab-grown diamond gemstones grown using the Diamond Technology may provide advantages over their mined counterparts in areas that matter to jewelers, jewelry manufacturers and consumers, with potential characteristics such as:

- Equal quality and brilliance of diamond product;
- Matched sizes, colors and clarities (particularly in goods ranging in sizes from 0.05 - 0.50 carats);
- Consistency of diamond finish due to high quality;
- Opportunity for color palette of diamond gemstones; and

Lack of negative issues related to environmental and social concerns.

We will seek to establish and maintain market acceptance through consumer education and industry cooperation. We intend to require laser marking of lab-grown diamond grown using the Diamond Technology (without compromising aesthetics) in order to brand and instill confidence in the consumer and the market as well as to differentiate our lab-grown diamond from earth-mined diamond. We intend to educate retailers and consumers on the physical properties of the Company's lab-grown diamond as compared to mined diamond and quality of the Company's lab-grown diamond.

*Commercial, Industrial and Technological Applications*

Diamond has exceptional qualities for use in advanced electronics and optics applications, but to date, development progress has been slow because of, among other things, diamond's relative scarcity and high cost. Diamond's unique hardness, clarity and thermal characteristics have made it highly desirable for scientific use for decades. However, material consistency issues and economics have created barriers to mass application adoption of diamond. We believe that our patented technology and production approach give us the ability to improve the quality and lower the cost of producing diamond materials, creating the opportunity for usage in a wider range of applications.

The demand for computing and communications products has increased significantly. As devices become more intelligent and ubiquitous, the need for connectivity at very high speeds, data intensive storage needs and ever-faster computer processors are pushing the limits of conventional silicon-based devices. Diamond enables these technologies to move past their current limitations and may be able to facilitate the development of next-generation devices in key areas such as wireless networking, optical storage, and high speed computing.

The Company anticipates several opportunities to monetize our patented technology and production approach in various technological applications. Pursuit of these opportunities is expected to be directed in part in concert with strategic partners.

Several of diamond's properties provide significant advantages over other materials used in devices/systems, such as high power switches, radiation detectors, and microwave windows suitable for use in plasma fields or other nuclear reactor high-electromagnetic interference ("EMI") environments.

Industrial diamonds already comprise what we estimate is a \$1 billion-plus market per year, but consist of low-quality diamonds that have primarily been utilized in rudimentary cutting and polishing devices. These diamond materials are largely in the form of diamond grit and diamond dust. Through the introduction of higher-quality relatively large diamond materials, substantial growth is anticipated for the industrial diamond market. As previously noted, we have initially experienced this in precision cutting devices.

The diamond and diamond-like materials historically used in the development of these non-gem applications have various limitations that have formerly impeded progress in optoelectronics and other technology applications. As our production volume increases and manufacturing costs continue to decrease due to our capacity expansion, we anticipate that our diamond materials will provide a viable and potentially economically preferred alternative for many of these highly-valued electronic, optical and industrial applications.

In order to more fully explore the opportunities discussed above, we intend to continue current production of our high quality diamond materials and to pursue related commercial opportunities. Currently, we intend to continue to explore opportunities in the precision cutting devices market while concurrently seeking opportunities for our lab-grown diamond gemstones.

### ***The Industry and Competition***

Our lab-grown diamond gemstones and diamond materials for use in industrial applications face competition from established producers and sellers of mined diamond, including companies such as De Beers, and other known and current and potential future manufacturers of lab-grown diamond. Our competitors include large multi-national gemstone diamond companies as well as start-up and development-stage gemstone diamond and technology companies, some of whom we may not be aware. Many of our competitors have significantly greater financial, technical, manufacturing and marketing resources and greater access to distribution channels than the Company. Many of our competitors may be able to devote substantially greater resources to promotion and systems development than we can. Barriers to developing competitive technology in our market may not be sufficient to prevent competitors from entering the industry, and current and new competitors may be able to develop competing diamond at a relatively low cost. We believe that our success will depend heavily upon whether we can achieve significant market acceptance before our potential competitors are able to introduce broadly accepted competitive products.

Companies that produce lab-grown diamond and who may compete with the Company in one or more of its markets include Element Six (South Africa), a privately held subsidiary of De Beers, AOTC Group NV (Netherlands), Pure Grown Diamond/IIa Technologies (USA, Singapore & Malaysia), Washington Diamond/Carnegie Institute, Sumitomo Electric Industries, Ltd. and Cornes Technologies (Japan). Other companies could seek to introduce lab-grown diamond or other competing diamond or to develop competing processes for production of lab-grown

diamond and diamond materials. We believe that competition will increase as demand for diamond materials increases for use in industrial and technology applications and as lab-grown diamonds continue to gain market acceptance.

***Raw Materials***

The principal raw materials used in the manufacture of our products are diamond seeds and certified high purity bottled gases. Certain diamond seeds are purchased from other diamond material producers, but the Company maintains its primary seed inventory through its self-sustaining seed production. Seeds are re-used through multiple production runs.

Our manufacturing process is dependent upon large amounts of electrical power delivered on an uninterrupted basis. The Company has worked with the local electric utility, a Fortune 200 company, to build and operate equipment at its manufacturing site that meets its needs. This equipment is provided to the Company on a long-term operating lease, which includes warranty, maintenance, and the delivery of electrical power at attractive per kilowatt/hour rates.

***Customers***

In July 2012 the Company began to produce diamond material and entered into a purchase order with an international supplier of precision diamond cutting tools pursuant to which the Company has been providing CVD single crystal diamond in specified wafer sizes. At March 31, 2013, the Company had largely fulfilled its initial purchase order with this customer. Since then, the Company has aggressively expanded its customer base with a focus on the gemstone marketplace. During the year ended March 31, 2015, the Company had 31 customers purchasing various materials for industrial and gemstone applications.

If we continue to reliably manufacture diamond products and are successful in expanding our manufacturing capacity, we anticipate that we will experience increased demand for our products both domestically and internationally, given the potential demand for diamond, the variety of potential uses for these products in gemstone, high tech applications, alternative energy technologies, and defense technologies.

***Patents, Trademarks, Licenses, Franchises, Concessions, Royalty Agreements or Labor Contracts***

At March 31, 2015, we held the following number of patents:

Jurisdiction	No. of Patents
United States	27
Foreign	9
Total	36

During the fiscal year ended March 31, 2015, the Company had one new patent granted in the United States. This patent expanded our intellectual property rights related to our Diamond Technology.

All of the Company’s patents have various lives based on the date of issue. Expiration of individual patents is expected to occur between 2019 and 2032.

Our research and development staff will continue efforts to develop proprietary manufacturing processes and equipment designed to enhance our manufacturing facilities and reduce costs.

We also own various trademarks and trade secrets that we developed within the Company or acquired from ADI and ADGC.

***Distribution***

Through March 31, 2015 the Company has had a limited number of customers. The Company has distributed its products directly to these customers without using intermediaries or distributors.

***Joint Ventures***

On September 16, 2013, the Company entered into the Grace Rich Agreements to form a joint venture with operations in the PRC. This joint venture is to initially deploy 100 Scio-designed diamond growing machines. The Company has licensed its proprietary technology for the manufacture of diamond gemstones to the joint venture to produce

material of agreed upon specifications. In exchange for the license, the Company has received licensing and development revenue and a 30% non-dilutable ownership position in the joint venture. In addition to the licensed technology, the Grace Rich Agreements include obligations for the Company to provide and be compensated for technology consulting services to the joint venture to support the start-up of operations. The Company is assisting the joint venture with the initial deployment of the licensed technology and the development of its production facility. The Company does not control the joint venture and is not required to make any on-going funding contributions.

On December 18, 2014, the Company entered into an arrangement with Renaissance Diamonds, Inc. (“Renaissance”) creating Renaissance Created Diamond Company, LLC (“RCDC”). The Company and Renaissance are each 50% members of RCDC. The arrangement was entered into in order to facilitate the development of procedures and recipes for, and to market and sell, lab-grown fancy-colored diamonds. RCDC will purchase rough diamond material from the Company and process and finish the material into finished gemstones for sale to various retailers and other participants in the market for gemstones. Profits generated by RCDC's operations will be distributed between the Company and Renaissance according to the terms of the LLC Agreement.

### ***Government Regulations***

Laboratory technology activities are subject to various federal, state, foreign and local laws and regulations, which govern research, lab development, taxes, labor standards, occupational health, and waste disposal, protection of the environment, mine safety, hazardous substances and several other matters. We believe that we are in compliance in all material respects with applicable technology, health, safety and environmental statutes and the regulations promulgated by the relevant jurisdictions. Currently, there are no costs associated with our compliance with such regulations and laws. Certain federal and state laws and regulations govern the testing, creation and sale of the types of diamond we intend to produce. The United States Federal Trade Commission (“FTC”) and other comparable regulatory authorities in the United States and in foreign countries may extensively and rigorously regulate our lab-grown diamond, product development activities and manufacturing processes. In the United States, the FTC regulates the introduction and labeling of gemstone diamond. We may be required to:

- Obtain clearance before we can market and sell our lab-grown diamond;
- Satisfy content requirements applicable to our labeling, sales and promotional materials;
- Comply with manufacturing and reporting requirements; and
- Undergo rigorous inspections.

The process of obtaining marketing clearance for new gemstone diamond from the FTC may prove costly and time consuming. The FTC has neither approved nor prohibited the use of the term “cultured” to describe the diamond the Company intends to sell as gemstones. However, in December 2006, the Jewelers’ Vigilance Committee submitted a petition (the “Petition”) to the FTC seeking amendment to the Guides for the Jewelry, Precious Metals, and Pewter Industries, 16 C.F.R. Part 23 (“Guides”) to include the term “cultured” as a proscribed term to describe laboratory-created diamond. By opinion, dated July 21, 2008, the FTC denied the Petition, finding it did not demonstrate that the use of the term “cultured” to describe laboratory-created diamond, when qualified by one of the terms provided in the Guides, is deceptive or unfair and declined to amend the Guides as requested by the Petition. The Company has not procured FTC clearance, and the FTC has not precluded the Company from selling diamond produced using the Diamond Technology. FTC has the power to restrict the offer and sale of diamond that could deceive or have the tendency or effect of misleading or deceiving purchasers or prospective purchasers with regard to the type, kind, quality, character, value, origin or other characteristics of a diamond gemstone. Under current guidelines issued by the FTC, the Company is permitted to market its diamond gemstones as “Scio-created,” “lab-created diamond,” “laboratory created diamond,” “laboratory grown diamond” or “cultured” so long as that term is accompanied by any of the foregoing and such designations may inhibit marketing descriptions that are more favorable to creating consumer demand. We may come under close scrutiny by governmental agencies and industry testing organizations and also by competitors in the gemstone industry, any of which may challenge our promotion and marketing of our lab-grown diamond. If our production or marketing is challenged by governmental agencies or competitors, or if regulations are issued that restrict our ability to produce and market our lab-grown diamond as “cultured diamond”, “lab-created diamond”, or otherwise as a mined diamond alternative, our business, operating results and financial condition could be materially adversely affected.

Our lab-grown diamond must also comply with similar laws and regulations of foreign countries in which we market such diamond. In general, the extent and complexity of gemstone diamond regulation is increasing worldwide. This trend may continue, and the cost and time required to obtain marketing clearance in any given country may increase as a result. Should it prove necessary, there can be no assurances that our lab-grown diamond will obtain any necessary foreign clearances on a timely basis, or at all.

Federal, state, local and foreign laws and regulations (especially those regarding approval of gemstone diamond) are always subject to change, and could have a material adverse effect on the testing and sale of our lab-grown diamond and, therefore, our business.



***Research and Development***

Our research and development activities have been limited to date as we have focused first on establishment of our production facility and immediately thereafter on production of diamond materials for commercial purposes. We expect to invest in new technology and intellectual property development to further improve production efficiencies and develop new products in the future.

### ***Environmental Regulations***

Our operations are subject to local, state and federal laws and regulations governing environmental quality and pollution control. To date, our compliance with these regulations has had no material effect on our operations, capital, earnings, or competitive position, and the cost of such compliance has not been material. We are unable to assess or predict at this time what effect additional regulations or legislation could have on our activities.

### ***Employees***

We had eight full-time employees as of March 31, 2015.

### ***Securities Exchange Act of 1934 Reports***

We maintain an Internet website at the following address: <http://www.sciodiamond.com>. The contents of the website are not incorporated either directly or by reference into this Form 10-K or into our other filings with the SEC. The Company makes available on or through our Internet website certain reports and amendments to those reports that are filed or furnished to the SEC pursuant to Section 13(a) or 15(d) of the Exchange Act. These include annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and beneficial ownership reports on Forms 3, 4 and 5. This information is available on our website free of charge as soon as reasonably practicable after we electronically file the information with, or furnish it to, the SEC.

## **ITEM 1A. RISK FACTORS.**

*Our business, financial condition, and results of operations could be harmed by any of the following risks, or other risks that have not been identified or which we currently believe are immaterial or unlikely. Shareholders should carefully consider the risks described below in conjunction with the other information in this Form 10-K and the information incorporated by reference in this Form 10-K, including our financial statements and related notes.*

### **Risks Related to Our Business**

***We have a very limited operating history, and have incurred losses to date. We have generated limited revenues to date, and therefore, it is difficult to evaluate our business and prospects.***

Our Company is in the preliminary stages of operation. While our Company has recently engaged in revenue-producing business activities, it is not yet a profitable enterprise and may incur substantial losses for the foreseeable future. In addition, the Company's revenues are presently derived from a limited number of customers. The Company has not finalized the scope of products it anticipates it will bring to market. As a company in the early stages of operation, our business is subject to all the risks inherent in a new business enterprise. We have no substantial operating history for investors to consider in evaluating our business and prospects. When making an investment decision, investors should consider the risks, expenses and difficulties that we may encounter as a young company in a new market. These risks include, but are not limited to, the following:

- Our need to fund and manage our rapidly developing and changing operations;
- Our need to expand our sales and marketing activities;
- Our need to quickly hire and integrate new personnel, including various levels of senior management who have been hired relatively recently;
- Our ability to develop additional applications and markets for our diamond materials, including the diamond gemstone industry;
- Our ability to produce diamond materials sufficient to meet the specifications and needs of various industrial and technology applications;

Our ability to produce diamond materials and lab-grown diamond sufficient to meet anticipated demand in the gemstone marketplace;

Acceptance of our lab-grown diamond in the gemstone marketplace; and

The need to further refine and improve our technology with respect to man-made diamond development/growing and commercialization including the need to make the diamond growing process commercially viable, acceptable (by our own and third party measures) and economical and our intellectual property and product offerings, and the need to respond to changing technologies and consumer preferences.

Likewise the diamond materials and lab-grown diamond gemstones produced using the Diamond Technology (collectively “Scio Diamond Materials”) are in a relatively early stage of development and are subject to the risks inherent in the development and marketing of Scio Diamond Materials, including unforeseen design, manufacturing or other problems or failure to develop market acceptance. Our business is subject to the risks inherent in the transition of technology from research and development and prototype proof-of-concept to commercial production and market acceptance.

Failure by the Company to complete and integrate commercial development of the Scio Diamond Materials it will market and distribute in sufficient quantities to meet market demand would have a material adverse effect on the Company's business, operating results and financial condition. Accordingly, the Company's prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in their early stage of development, particularly technology-based companies operating with developing and unproven manufacturing processes.

To address these risks, the Company must, among other things, respond to competitive developments, attract and motivate qualified personnel, develop market acceptance for its diamond, establish effective distribution channels, effectively manage any growth that may occur and continue to upgrade and successfully commercialize the Diamond Technology and Scio Diamond Materials incorporating such technology.

The Company purchased its Diamond Technology from ADI and ADGC (together, the "Apollo Companies"). Neither of the Apollo Companies was able to successfully (profitably) develop and commercialize their man-made diamond development/growing process.

***We will require additional funding.***

We currently have limited cash and working capital to support our operations. Our future continuing operations will require additional funding, and we may not be able to obtain such funding on acceptable terms or at all. We likely will require additional capital to be able to fund continued development and improvement of the process for growing Scio Diamond Materials and to fund our expansion of manufacturing capacity to meet projected growth of the market for our diamond. There can be no assurance that such efforts for raising capital will not involve substantial dilution with respect to existing or future stockholders of the Company.

Our future capital requirements will depend on many factors, including the speed at which our production process can be scaled-up for high yield production, market acceptance of and demand for our diamond, and the timing of our expansion into new diamond markets. Our future capital requirements depend upon many factors, including, but not limited to:

- The rate at which we increase our production capacity;
- The rate at which we expand our sales and marketing operations;
- The rate at which we attract consumers, distributors and strategic relationships;
- The extent to which we are able to develop and upgrade the technology and infrastructure; and
- The response of competitors to our Scio Diamond product offerings.

We expect additional financing to be required and there can be no assurance that additional equity or debt financing, if required, will be available on acceptable terms or at all. If we raise additional funds by selling stock, the percentage ownership of our then current stockholders will be reduced, and we may raise these funds with securities that have rights, preferences, or privileges equal or superior to the rights of investors owning our common shares. If we cannot raise adequate funds to satisfy our capital requirements, we may have to limit our operations significantly, or the Company could terminate operations entirely, resulting in a complete loss of investment for our stockholders. Our inability to obtain financing on acceptable terms when needed would have a material adverse effect on the Company's business, operating results and financial condition.

***We have had significant turnover in key management personnel.***

We have had significant turnover in our executive officers. Our success depends in part upon our ability to retain the services of certain executive officers and other key employees and on the skills, experience and performance of senior management and certain other key personnel, most of whom have either never worked together or who have worked

together for only a short period of time. The loss of the services of our executive officers or other key employees would have a material adverse effect on our business, operating results and financial condition. Because we are in the early stages of commercialization, we are also dependent on our ability to recruit, retain and motivate personnel with technical, manufacturing and chemical vapor deposition process skills. There are a limited number of personnel with these qualifications and competition for such personnel may be intense. Our inability to attract, integrate and retain additional qualified key personnel would materially adversely affect our business, operating results and financial condition.

***We may expend a substantial amount of time and resources in connection with SEC, other regulatory or stockholder-related inquiries or legal actions related to our filed financial statements and other disclosures and the transactions related thereto or other matters.***

We have recently received a subpoena issued by the SEC ordering the provision of documents and related information concerning various corporate transactions between the Company and its predecessors and other persons and entities. The Company is fully cooperating with this inquiry. We may expend a substantial amount of time and resources in connection with the SEC subpoena, other regulatory or stockholder-related inquiries or legal actions related to our previously filed financial statements and other disclosures and the transactions related thereto or other matters. Such actions could have a material adverse effect on the Company's liquidity and financial condition and could also affect our ability to file periodic reports on a timely basis and investor confidence in the accuracy and completeness of our financial statements, which in turn could harm our business and have an adverse effect on our stock price and our ability to raise additional funds.

***We expect future losses.***

In order to achieve a commercially viable operation, we have made and expect to make further significant investments in technology, infrastructure, research and development. We expect to expend substantial financial and other resources on expanding our operations, in particular our diamond growth technology infrastructure, diamond fabrication, and sales/marketing activities. As a result, we must generate significant revenues to achieve and maintain profitability. We expect that our sales and marketing expenses, general and administrative expenses, as well as the continued development expenses will continue to increase.

***Our business model is unproven.***

Our initial business model was focused on selling lab-grown diamond for various precision cutting applications. We are concurrently seeking to produce other lab-grown diamond for retail gemstone consumption and other commercial applications. Although other companies have sold some minimal amounts of lab-grown diamond gemstones to date, the full extent of the market for such lab-grown diamond is not fully known. Our business model is relatively new, is unproven and is likely to continue to evolve. Accordingly, our business model may not be successful, and we may need to make substantial changes thereto. Our ability to generate significant revenues will depend, in large part, on our ability to successfully market our product to consumers, distributors and commercial customers. We intend to continue to develop our business model as the market for our products evolves.

***We are wholly dependent on the Diamond Technology.***

Our diamond supply depends entirely on our ability to manufacture diamond using the Diamond Technology acquired via the August 31, 2011 purchase of assets by the Company from ADI and the June 5, 2012 purchase of assets by the Company from ADGC (together, the "Asset Purchase").

Although the ability to produce limited quantities of high quality lab-grown diamond gemstones has been demonstrated, it has yet to be proven that such success can be transferred into a mass production process that will yield high-quality gemstones and material suitable for retail gemstone distribution and commercial/industrial applications. The inability or difficulty to transfer the Diamond Technology into a high-yield production facility would have a material adverse effect on our business, operating results and financial condition. Any disruption in our ability to produce high quality lab-grown diamond would have a significant material effect on our business.

***Our future revenues are unpredictable, and we expect our operating results to fluctuate from period to period.***

## Edgar Filing: Scio Diamond Technology Corp - Form 10-K

Our lack of operating history and the emerging nature of the markets in which we expect to compete make it difficult for us to accurately forecast revenues in any given period. As such, revenues could fall short of our expectations if we experience production delays or difficulties. Likewise, revenues could fall short of expectations should our product not be met with the demand we anticipate from the marketplace. We have limited experience in financial planning for our business on which to base our planned operating expenses.

Our operating results are likely to fluctuate substantially from period to period as a result of a number of factors, many of which are beyond our control. These factors include, but are not limited to, the following:

- Outside market influences beyond our control, including extended periods of decreased demand for Scio diamond;
  - Our ability to enter into successful strategic relationships;
  - Our ability to attract purchasers and/or distributors;
- The amount and timing of operating costs and capital expenditures relating to expansion of production operations;
  - The rate at which individuals and organizations accept our diamond;
  - An announcement or introduction of new or enhanced diamonds or services by our competitors;
  - Our ability to attract and retain qualified personnel; and
  - Pricing policies instituted by our current and possible future competitors.

The Company has generated limited revenue to date and consequently its operations are subject to all risks inherent in the establishment of a new business enterprise. For the period from inception, September 17, 2009, through March 31, 2015, the Company has an accumulated deficit of (\$18,738,915). We are currently generating limited revenues and expect to continue to generate revenue in the future, but there can be no assurances that we will ever generate sufficient revenues to achieve profitability. If we do achieve profitability, there can be no assurances that we can sustain or increase profitability.

***Our ability to develop our core technologies is subject to uncertainties.***

The process by which we plan to manufacture diamond is highly complex. We anticipate that customers will have highly specific quality standards that our diamond will be required to meet. The diamond we intend to sell is in the early stages of development and there can be no assurances that it will meet high customer standards. Product failure or the inability to meet customer requirements would have a material adverse effect on our business, operating results and financial condition. The process by which we plan to produce our diamond requires the integration of several complex components, some of which will be provided by third-party suppliers. The successful integration of the Diamond Technology with third-party products will determine the performance and scalability of our production process. We will be dependent upon our employees and vendors to maintain an adequate testing and technical support infrastructure to ensure the successful adoption and rollout of our diamond to customers. We currently have limited experience in these areas. Failing in any of these areas could materially adversely affect our business.

***We may not be able to establish effective distribution channels.***

We initially intend to sell our diamond in selected markets in the United States and internationally. We expect that we will be required to enter into distribution agreements with, and will be dependent upon, a number of third parties for distribution and sales of our diamond. We are currently selling diamond directly to customers and have not yet entered into distribution agreements with any distributors. There can be no assurance that we will be able to enter into distribution agreements with distributors or that our distribution strategy will prove to be successful. Additionally, there can be no assurance that distributors will devote the efforts needed for successful distribution of our diamond. The inability of the Company to enter into favorable arrangements with distributors or to achieve desired distribution of our diamond would have a material adverse effect on our business, operating results and financial condition.

Our sales of diamond for commercial applications are dependent upon our ability to enter into profitable relationships with businesses best able to reap rewards from the unique characteristics of diamond. There is no assurance that we will be able to initiate and maintain these relationships.

***The Diamond Technology may be vulnerable to failure.***

Our success depends, in part, on the performance, reliability and availability of the Diamond Technology and the diamond we ultimately produce. The Diamond Technology and diamond produced thereby may be vulnerable to failure. The failure of the Diamond Technology or diamond produced thereby could adversely affect our business. The process for manufacturing diamond using the Diamond Technology is vulnerable to disruptions due to a variety of factors, which may lead to interruptions, delays, and losses of opportunities or inability to consistently market and sell our lab-grown diamond. The occurrence of any of the foregoing could have a material adverse effect on our business.

***We may need to effectively manage rapid growth of our operations.***

Our ability to successfully offer diamond and to implement our business plan in new markets requires an effective planning and management process. We are in the process of increasing our operations and anticipate having to increase our headcount as well. Increasing our operations and potentially experiencing rapid growth would place a significant strain on our management systems, infrastructure and resources. We will need to continue to improve our



financial and managerial controls and reporting systems and procedures, and will need to continue to expand, train and manage our workforce.

Furthermore, we may be required to manage an increasing number of relationships with various users, customers and other third parties. Any failure to expand any of the foregoing areas efficiently and effectively could cause our business to suffer. We could experience a period of rapid and significant growth, which could continue over several years. We believe rapid growth would place a significant strain on our resources. Our ability to manage growth effectively will require us to implement and improve operational and financial systems and to expand, train and manage our employee base. We also may be required to manage multiple relationships with various suppliers, customers and other third parties. Our future operating results will also depend on our ability to expand sales and marketing, research and development and administrative support organizations. If the Company were unable to manage growth effectively, our business, financial condition and results of operations would be materially adversely affected.

***We will need to hire additional personnel.***

Our future success depends on our ability to identify, attract, hire, train, retain and motivate highly skilled executive, technical, managerial, sales and marketing and business development personnel. We intend to hire a number of executive, technical, sales, and marketing, business development and administrative personnel during the next one or two years. Competition for qualified personnel may prove intense, particularly in the technology markets. If we fail to successfully attract, assimilate and retain a sufficient number of qualified executives, technical, managerial, sales and marketing, business development and administrative personnel, our business could suffer.

***Our success depends upon achieving a critical mass of customers and strategic relationships.***

Our success is largely dependent upon achieving significant market acceptance for our diamond. The market for our diamond is at an early stage of development. Although we believe that our diamond will ultimately achieve broad market acceptance, our existing and potential competitors may offer diamond that could negatively affect the market acceptance of our product and damage our business prospects.

Our success is also dependent upon attracting significant numbers of distributors and strategic relationships in order to market our diamond. In particular, our ability to enter into beneficial distribution partnerships will depend in large part upon our success in convincing diamond gemstone consumers that our lab-grown diamond gemstone is of a desired quality. Failure to achieve and maintain a critical mass of market acceptance will seriously harm our business in the diamond gemstone industry.

***The current and future state of the global economy may curtail our operations and our anticipated revenues.***

Our business may be adversely affected by changes in domestic and international economic conditions, including inflation, changes in consumer preferences and changes in consumer spending rates, personal bankruptcy and the ability to collect our accounts receivable. Changes in global economic conditions may adversely affect the demand for our products and make it more difficult to collect accounts receivable, thereby negatively affecting our business, operating results and financial condition. The recent disruptions in credit and other financial markets and deterioration of national and global economic conditions could, among other things, impair the financial condition of some of our customers and suppliers, thereby increasing customer bad debts or non-performance by suppliers.

***Acts of war, terrorism or other unknown and unexpected events could disrupt our business and we could be required to cease our operations.***

Involvement in a war or other military action or acts of terrorism may cause significant disruption to commerce throughout the world. To the extent that such disruptions result in (i) delays or cancellations of customer orders, (ii) a general decrease in consumer spending, (iii) our inability to effectively market and distribute our products or (iv) our inability to access capital markets, our business and results of operations could be materially and adversely affected. We are unable to predict whether the involvement in a war or other military action will result in any long-term commercial disruptions or if such involvement or responses will have any long-term material adverse effect on our business, results of operations or financial condition.

***The Company continues to receive a “going concern” qualification in our financial statements that might create additional doubt about our ability to stay in business, which could result in a total loss of investment by our stockholders.***

We have not generated material revenues and have negative operating cash flows. These issues, among others, raise substantial doubt about our ability to continue as a “going concern.”

**Risks Related to Our Industry**

*The potential market for our lab-grown diamond is unproven and may not materialize.*

There currently is no widely-developed market for lab-grown diamond gemstones, and we believe that companies operating in the gemstone field may not be fully aware of the existence and attributes of our lab-grown diamond. As is the case with any new or potential product, market acceptance and demand are subject to a significant amount of uncertainty. Our future financial performance will depend upon consumer acceptance of lab-grown diamond as a realistic and comparable alternative to mined diamond and other gemstones. Because no widely-developed markets now exist for lab-grown diamond gemstones, it is difficult to predict the future growth rate, if any, and the size of the market for our lab-grown diamond gemstones. We may spend significant amounts of capital to acquire diamond production systems at a time when demand for our lab-grown diamond is not at a level to fund those expenditures. The market for our lab-grown diamond gemstones may never develop or may develop at a slower pace than expected due to a general lack of consumer acceptance of lab-grown diamond gemstones. If the market fails to develop or develops more slowly than expected, or if our lab-grown diamond gemstones do not achieve significant market acceptance, our business, operating results and financial condition would be materially adversely affected.

***We face significant competition.***

Our lab-grown gemstone diamond will face competition from established producers and sellers of earth-mined diamond and other known and potential manufacturers of lab-grown gemstones. Other companies could seek to introduce lab-grown diamond or other competing diamonds or to develop competing processes for production of lab-grown diamond gemstones. We believe that the more successful the Company is in creating market acceptance for Scio diamond which included lab-grown gemstone diamond, the more competition can be expected to increase. Increased competition could result in a decrease in the price charged by the Company for our diamond or reduce demand for our diamond, which would have a material adverse effect on our business, operating results and financial condition. Further, our current and potential competitors may have significantly greater financial, technical, manufacturing and marketing resources and greater access to distribution channels than the Company. There can be no assurance that we will be able to compete successfully with existing or potential competitors.

Widespread consumer acceptance of lab-grown diamond gemstones is still developing. At this time, the Company is aware that it may be competing with companies that produce lab-grown diamond for industrial and gemstone markets, including Pure Grown Diamond/IIa Technologies, Washington Group, D'Nea, Element Six, and Sumitomo. We believe that as lab-grown diamond continues to gain widespread commercial and consumer acceptance, the more competition can be expected to increase. Increased competition could result in a decrease in the price expected to be charged by the Company for our diamond or reduce demand for our diamond, which would have a material adverse effect on our business, operating results and financial condition.

Our potential competitors in the gemstone diamond industry may have significantly greater financial, technical, manufacturing and marketing resources and greater access to distribution channels than the Company. Our competitors will likely include large multi-national gemstone diamond companies as well as numerous start-up and development-stage gemstone diamond and technology companies, some of whom we may not be aware. We expect intense competition as we execute our business plan. It is believed that some of our existing and potential competitors, as well as potential entrants into our market, have longer operating histories, larger user bases, greater brand recognition and significantly greater financial, marketing and other resources than the Company. Many of these potential competitors may be able to devote substantially greater resources to promotion and systems development than we can. Barriers to developing competitive technology in our market may not be sufficient and current and competitors may be able to develop competing diamonds at a relatively low cost. Accordingly, we believe that our success will depend heavily upon achieving significant market acceptance before our potential competitors introduce competing products. There can be no assurance that we will be able to compete successfully with potential competitors.

***Rapid technological change will affect our business.***

Rapidly changing technology, industry standards, evolving consumer demands and frequent new product introductions are expected to define our market. Our market's early stage of development may exacerbate these characteristics. Our future success will depend in significant part on our ability to continuously improve the quality of lab-grown diamond and our production capabilities in response to both the evolving demands of the market and competitive product offerings. Efforts in these areas may not be successful.

***We expect to have limited protection of our intellectual property and proprietary rights.***

We regard the patents, trade secrets and similar intellectual property acquired via the Asset Purchase as critical to our success. We must rely on patent law, trade secret protection and confidentiality agreements with our employees, customers, strategic partners, advisors and others to protect those proprietary rights. Such measures, however, afford only limited protection, and we may not be able to maintain the propriety and/or confidentiality of the Diamond Technology. Despite these precautions, unauthorized third parties might use information that we regard as proprietary

to compete or help others to compete with us. There is no assurance that any of the existing patent applications or future patent applications, if made, will be granted, or, if granted, will not be invalidated or circumvented, or that the rights granted there under will provide us with a competitive advantage. Any misappropriation of our proprietary information by third parties could materially adversely affect our business. There can be no assurance that any other patents issued will provide any significant commercial protection to the Company, that the Company will have sufficient resources to prosecute its patents or that any patents will be upheld by a court should the Company seek to enforce its respective rights against an infringer.

There can be no assurances that:

- The scope of any patent protection will be effective to exclude competitors or provide competitive advantages to us;
  - We will be able to commercially exploit any issued patents before they expire;
  - Any of the patents held will be held valid if subsequently challenged;
- Others will not claim rights in or ownership of, the patents and other proprietary rights acquired or produced by the Company;
  - Our diamond will not infringe, or be alleged to infringe, the proprietary rights of others; or
- We will be able to protect meaningful rights in proprietary technology over which the party does not hold patents.

Furthermore, there can be no assurances that others have not developed or will not develop diamond which may duplicate any of the diamond produced using the Diamond Technology or our expected manufacturing processes, or those others will not design around any of the Company's patents. The existence of valid patents does not provide absolute prevention from other companies independently developing competing technologies. Existing producers of laboratory-created diamond may refine existing processes for growing diamond or develop new technologies for growing diamond in a manner that does not infringe any intellectual property rights of the Company.

Other parties may independently develop or otherwise acquire substantially equivalent techniques, gain access to our acquired proprietary technology or disclose such technology. In addition, whether or not we obtain additional patents, others may hold or receive patents covering components of diamond we independently develop in the future. There can be no assurances that third parties will not claim infringement by us, and seek substantial damages, with respect to current or future diamond-related activities. If we were to become involved in a dispute regarding intellectual property, whether ours or that of another company, we may become involved in material legal proceedings. Any such claims, with or without merit, could be time-consuming, result in costly litigation, cause product shipment delays and require us to:

- Cease manufacturing and selling the product in question, which could seriously harm us;
- Enter into royalty or licensing agreements; or
- Design commercially acceptable non-infringing alternative diamond.

There can be no assurances that we would be able to obtain royalty or licensing agreements, if required, on terms acceptable to us or at all, or that we would be able to develop commercially acceptable non-infringing alternative diamond. The failure to do so could have a material adverse effect upon our business, financial condition, operating results and cash flows. We cannot be absolutely certain that the Diamond Technology does not infringe issued patents or other intellectual property rights of others. In addition, because patent applications in the United States are not publicly disclosed until the patent is issued, applications may have been filed which relate to the Diamond Technology.

There can be no assurance that our business and ability to produce diamond will not be impaired by claims that we are infringing upon the intellectual property of others. We may be subject to future legal proceedings and claims from time to time in the ordinary course of our business, including claims of alleged infringement of the trademarks and other intellectual property rights of third parties. Intellectual property litigation is expensive and time-consuming and could divert the Company's management's attention from diamond production and operating our business. As a result of the foregoing, the limited protection of our acquired intellectual property rights and proprietary information could have a material adverse effect on the Company's business, operating results and financial condition.

***Substantial governmental regulation may restrict our ability to sell our lab-grown diamond.***

Certain federal and state laws and regulations govern the testing, creation and sale of the types of diamond we intend to produce. The United States Federal Trade Commission ("FTC") and other comparable regulatory authorities here and

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

in foreign countries may extensively and rigorously regulate our Scio Diamond Materials, product development activities and manufacturing processes. In the United States, the FTC regulates the introduction and labeling of gemstone diamond. We may be required to:

- Obtain clearance before we can market and sell our lab-grown diamond gemstones;
- Satisfy content requirements applicable to our labeling, sales and promotional materials;
- Comply with manufacturing and reporting requirements; and
- Undergo rigorous inspections.

The process of obtaining marketing clearance for new gemstone diamond from the FTC may prove costly and time consuming. The FTC has neither approved nor prohibited the use of the term “cultured” to describe the diamond the Company intends to sell as gemstones. However, in December 2006, the Jewelers’ Vigilance Committee submitted the Petition a petition (the “Petition”) to the FTC seeking amendment to the Guides for the Jewelry, Precious Metals, and Pewter Industries, 16 C.F.R. Part 23 (“Guides”) to include the term “cultured” as a proscribed term to describe laboratory-created diamond. By opinion, dated July 21, 2008, the FTC denied the Petition finding it did not demonstrate that the use of the term “cultured” to describe laboratory-created diamonds, when qualified by one of the terms provided in the Guides, is deceptive or unfair and declined to amend the Guides as requested by the Petition. The Company has not procured FTC clearance, and the FTC has not precluded the Company from selling diamond produced using the Diamond Technology. Despite its knowledge of the existing limited sales of lab-grown diamond gemstones and however unlikely, there can be no assurances that the FTC will not preclude the Company, or others similarly situated from marketing and selling lab-grown diamond gemstones.

The FTC has the power to restrict the offer and sale of diamond that could deceive or have the tendency or effect of misleading or deceiving purchasers or prospective purchasers with regard to the type, kind, quality, character, value, origin or other characteristics of a diamond gemstone. Under current guidelines issued by the FTC, the Company is permitted to market its diamond gemstones as “Scio-created,” “lab-created diamond”, “laboratory created diamond,” “laboratory grown diamond” or “cultured” so long as that term is accompanied by any of the foregoing and such designations may inhibit marketing descriptions that are more favorable to creating consumer demand. We may come under close scrutiny by governmental agencies and industry testing organizations and also by competitors in the gemstone industry, any of which may challenge our promotion and marketing of our lab-grown diamond. If our production or marketing is challenged by governmental agencies or competitors, or if regulations are issued that restrict our ability to produce and market our lab-grown diamond as “lab-grown diamond”, “lab-created diamond”, or otherwise as a mined diamond alternative, our business, operating results and financial condition could be materially adversely affected.

It is likely that our Scio Diamond Materials must also comply with similar laws and regulations of foreign countries in which we market such diamond. In general, the extent and complexity of diamond disclosure regulation is increasing worldwide. This trend may continue, and the cost and time required to obtain marketing clearance in any given country may increase as a result. Should it prove necessary, there can be no assurances that our Scio Diamond Materials will obtain any necessary foreign clearances on a timely basis, or at all. Our inability to satisfy specific requirements for approval by domestic and/or foreign regulatory agencies could materially adversely affect our ability to bring diamond to market and generate revenue.

Federal, state, local and foreign laws and regulations (especially those regarding approval of gemstone diamond) are always subject to change and could have a material adverse effect on the testing and sale of our diamond and, therefore, our business.

***Regulatory authorities may limit our business in the future.***

We will be subject to extensive regulatory requirements. Government authorities can withdraw marketing clearance due to our failure to comply with regulatory standards or due to the occurrence of unforeseen problems following initial clearance. Ongoing regulatory requirements are wide-ranging and govern, among other things:

- . Product manufacturing;
- . Annual inspections related to ISO certification of our quality system;
- . Supplier substitution;
- . Product changes;
- . Process modifications;
- . The process of assuring origin of mine and/or production of diamond;



Lab-grown diamond gemstone reporting and disclosure; and  
Product sales and distribution.

We expect that various government agencies may inspect our facilities from time to time to determine whether we are in compliance with applicable laws and regulations. Additionally, if we fail to comply or maintain compliance with laws and regulations pertaining to diamond gemstones, regulatory authorities may fine us and bar us from selling our lab-grown diamond gemstones. If a regulatory agency believes we are not in compliance with such laws or regulations, it may be able to:

- Seize our lab-grown diamond gemstones;
- Require a recall;
- Withdraw previously granted market clearances;
- Implement procedures to stop future violations; and/or
- Seek civil and criminal penalties against us.

**Risks Related to an Investment in our Common Stock**

*An investment in the Company involves a high degree of risk.*

An investment in the Company is speculative and involves a high degree of risk, including the loss of an investor's entire investment in the Company. There is no guaranteed rate of return on an investor's investment in the Company, and there is no assurance that investors will be able to resell their shares for the amount they paid for such shares or for any other amount. Investors should not invest in the Company unless such investors can afford to lose their entire investment.

*Recent settlement agreement resulted in restructured Board of Directors and shareholder voting agreement that results in our directors and officers controlling a large percentage of the Company's stock.*

On June 23, 2014, the Company entered into a settlement agreement (the "Settlement Agreement") by and among Edward S. Adams, Michael R. Monahan, Gerald McGuire, James Korn, Bruce Likly, Theodorus Strous, and Robert C. Linares, their present and past affiliates, such as Apollo Diamond, Inc., Apollo Diamond Gemstone Corporation, Adams Monahan LLP, Focus Capital Group, Inc. and Oak Ridge Financial Services Group, Inc., family members and spouses (the "Adams Group"), and Thomas P. Hartness, Kristoffer Mack, Paul Rapello, Glen R. Bailey, Marsha C. Bailey, Kenneth L. Smith, Bernard M. McPheely, James Carroll, Robert M. Daisley, Ben Wolkowitz, Craig Brown, Ronnie Kobrovsky, Lewis Smoak, Brian McPheely, Mark P. Sennott, the Sennott Family Charitable Trust, and their affiliates (the "Save Scio Group"), pursuant to which the Company and the Save Scio Group settled the previously pending consent contest for the election of directors. Pursuant to the Settlement Agreement, on June 23, 2014, Messrs. Adams, Strous, Linares and McGuire resigned as directors effective immediately; the Board expanded the size of the Board to 7 directors and appointed Messrs. McPheely, Wolkowitz, Smoak and Leaverton (the "Save Scio Nominees") to fill all but one of the resulting vacancies. In addition, the Company agreed to nominate each of Messrs. Korn and Likly (the "Adams Group Nominees") and the Save Scio Nominees for election to the Board at the Company's 2014 annual meeting of stockholders. Pursuant to the Settlement Agreement, the Adams Group and the Save Scio Group must vote their shares of Common Stock for the other's nominees for the next three years, and will also have replacement rights in the event these nominees are unable to serve as directors.

As of June 23, 2015, the Company had 57,516,499 shares of common stock outstanding. As of the date of the Settlement Agreement, the total number of shares subject to the voting agreements related to the settlement agreement is 17,492,928 or approximately 30% of the outstanding shares. Therefore, the Save Scio Group and the Adams Group collectively have considerable influence to:

- Elect or defeat the election of our directors;
- Amend or prevent amendment of our Articles of Incorporation or Bylaws;
- Effect or prevent a merger, sale of assets or other corporate transaction; and
- Determine the outcome of any other matter submitted to the stockholders for vote.

The limited ability of other stockholders to exercise control over the Company may adversely affect the future market price for our securities and the rights of our stockholders.

*Provisions in our Articles of Incorporation and bylaws or Nevada law might discourage, delay or prevent a change of control of us or changes in our management and, therefore, depress the trading price of the common stock.*

Nevada corporate law and our Articles of Incorporation and Bylaws contain other provisions that could discourage, delay or prevent a change in control of our Company or changes in its management that our stockholders may deem advantageous. These include provisions that:

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

- Deny holders of our common stock cumulative voting rights in the election of directors, meaning that stockholders owning a majority of our outstanding shares of common stock will be able to elect all of our directors;
- Require any stockholder wishing to properly bring a matter before a meeting of stockholders to comply with specified procedural and advance notice requirements; and
  - Allow any vacancy on the Board of Directors, however the vacancy occurs, to be filled by the directors.

***There is a limited active public market for any of our securities, which are not listed on any stock exchange, and transfer of our securities is restricted.***

There is presently a limited active public market for our securities, and there can be no assurance that a trading market will continue to develop or, if developed, that it will be maintained. Our common stock is not listed on any stock exchange and it is currently quoted on the OTC Bulletin Board and OTC PINK marketplace under the ticker "SCIO". We believe that we currently may not have enough stockholders or outstanding shares to support an active trading market, even if our common stock were listed on a recognized trading exchange. There can be no assurance that our investors will be able to resell any of our securities at any price. The Company makes no representation to investors regarding the value of its securities, and, particularly in light of the thin trading in the Company's securities; trading prices may or may not reasonably reflect the intrinsic value, if any, of the Company's securities.

We have been deemed to be a former shell company in accordance with the Securities Act. As a result, our shares of common stock may not be resold under Rule 144 of the Securities Act except pursuant to Rule 144(i). Resales under Rule 144(i) generally require, that, in addition to the normal Rule 144 requirements and limitations: (1) we are subject to the reporting requirements of the Securities Exchange Act of 1934 (the "Exchange Act"); (2) we have filed all Exchange Act reports required for the past 12 months; and (3) a minimum of one year has elapsed since we filed current Form 10 information on Form 8-K changing our status from a shell company to a non-shell company. An investment in the Company should be considered a long-term, illiquid investment, and investors should be able to withstand a complete loss of their investment.

Our Bylaws specifically provide that we shall not be required to effectuate the transfer of any shares of our common stock without first receiving from the transferring stockholder (i) an opinion of counsel satisfactory to the Company that a proposed transfer may be made lawfully without the registration of such shares pursuant to the Securities Act of 1933, as amended (the "Securities Act"), and applicable state securities laws, or (ii) evidence that the shares proposed to be transferred have been registered under the Securities Act. The existence of the foregoing restrictions may, therefore, adversely affect the future market price for our securities and the rights of our stockholders.

***Future stock issuances could severely dilute our current shareholders' interests.***

The future issuance of common stock may result in dilution in the percentage of our common stock held by our existing shareholders. Also, any stock we sell in the future may be valued on an arbitrary basis by us and the issuance of shares of common stock or preferred stock for future services, acquisitions or other corporate actions may have the effect of diluting the value of the shares held by our existing shareholders.

In addition, it is the Company's current intention (depending on the development of the business plan and other factors) to raise substantial additional capital during the fiscal year ending March 31, 2015, which we expect to result in substantial dilution in the percentage of our common stock held by our existing shareholders.

***Any additional funding we arrange through the sale of our common stock will result in dilution to existing stockholders' voting power and may result in dilution to the book value per share held by existing stockholders.***

We must raise additional capital in order for our business plan to succeed. A likely source of additional capital will be through the sale of additional shares of common stock. Such stock issuances would cause stockholders' voting interests in our Company to be diluted and may cause the book value per share held by existing stockholders to be diluted. Such dilution could negatively affect the value of investors' shares.

***We do not expect to pay cash dividends in the foreseeable future.***

We are not obligated to pay dividends with respect to our capital stock, and we do not anticipate the payment of cash dividends on our capital stock in the foreseeable future. Any decision to pay dividends will depend upon our profitability at the time, cash available, and other factors; however, it is currently anticipated that any future profits received from operations will be retained for operations. Therefore, no assurance can be given that there will ever be any such cash dividend or distribution in the future. Accordingly, investors must rely on sales of their capital stock after price appreciation, which may never occur, or a sale of our Company or other similar transaction as the only way to realize a gain on their investment.

***If we do not obtain additional financing, our business may fail.***

We anticipate that additional funding will be needed for general administrative expenses, operating costs and marketing costs. There is no guarantee that we will be able to raise the required cash and because of this our business may fail. We have generated limited revenues from operations to date. The specific cost requirements needed to maintain operations depends upon the production we are able to generate. If we are not able to raise the capital necessary to fund our business objectives, we may have to delay the implementation of our business plan. Obtaining additional funding will be subject to a number of factors, including general market conditions, investor acceptance of our business plan and initial results from our business operations. These factors may impact the timing, amount, terms or conditions of additional financing available to us. The most likely source of future funds available to us is through the sale of additional shares of common stock. There is no guarantee that we will be able to raise the funds required by the Company and, if we are not able to raise such funds, then our business may fail.

***Because our continuation as a going concern is in doubt, we may be forced to cease business operations unless we can generate profitable operations in the future.***

We will be incurring losses until we build a break-even level of revenue. Further losses are anticipated in the development of our business. As a result, there is substantial doubt about our ability to continue as a going concern. Our ability to continue as a going concern is dependent upon our ability to generate profitable operations in the future and/or to obtain the necessary financing to meet our obligations and repay our liabilities arising from normal business operations when they come due. We will require additional funds in order to provide proper service to our potential clients. At this time, we cannot assure investors that we will be able to obtain financing. If we are unable to raise needed financing, we may have to delay or abandon further operations. If we cannot raise financing to meet our obligations, we will be insolvent and may be forced to cease our business operations.

***If an active trading market for our common stock does not sufficiently develop, stockholders may be unable to sell their shares.***

There is currently a limited trading market for our common stock and we can provide no assurance that a significant market will develop. Our common stock currently trades on the OTC Bulletin Board and the OTC PINK marketplace. We may decide to apply for listing of our common stock on a U.S. and/or foreign exchange. However, we can provide no assurances that we will apply or that our common stock would be accepted for listing on any stock exchange. Accordingly, we can provide investors with no assurance that our shares will be traded on a U.S. and/or foreign exchange or, if traded, that a significant active public trading market will materialize. If no active trading market is ever developed for our shares, it will be difficult for stockholders to sell their shares.

***Our shares of common stock are subject to the “penny stock” rules of the SEC and the trading market in our securities will be limited, which will make transactions in our stock cumbersome and may reduce the value of an investment in our stock.***

The SEC has adopted rules that regulate broker-dealer practices in connection with transactions in “penny stocks.” Penny stocks generally are equity securities with a price of less than \$5.00 (other than securities registered on certain national securities exchanges or quoted on the NASDAQ system, provided that current price and volume information with respect to transactions in such securities is provided by the exchange or system). Penny stock rules require a broker-dealer, prior to a transaction in a penny stock not otherwise exempt from those rules, to deliver a standardized risk disclosure document prepared by the SEC, which specifies information about penny stocks and the nature and significance of risks of the penny stock market. A broker-dealer must also provide the customer with bid and offer quotations for the penny stock, the compensation of the broker-dealer, and sales person in the transaction, and monthly account statements indicating the market value of each penny stock held in the customer’s account. In addition, the penny stock rules require that, prior to a transaction in a penny stock not otherwise exempt from those rules; the broker-dealer must make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser’s written agreement to the transaction. These disclosure requirements may have the effect of reducing the trading activity in the secondary market for stock that becomes subject to those penny stock rules. If a trading market for our common stock develops, our common stock will probably become subject to the penny stock rules, and stockholders may have difficulty in selling their shares.

***Significant deficiencies in our disclosure controls and procedures or our failure to remediate such deficiencies could result in a material misstatement in our financial statements not being prevented or detected and could affect investor confidence in the accuracy and completeness of our financial statements, as well as our common stock price.***

We have identified significant deficiencies in our disclosure controls and procedures, including a lack of sufficient internal accounting resources, necessary to ensure that adequate review of our financial statements and notes thereto is performed, and have concluded that our internal control over financial reporting was not effective as of March 31, 2015. These significant deficiencies and our remediation plans are described further in Item 9A. Deficiencies in our disclosure controls and procedures could result in material misstatements in our financial statements not being prevented or detected. We may experience difficulties or delays in completing remediation or may not be able to successfully remediate significant deficiencies at all. Any material deficiency or unsuccessful remediation could affect our ability to file periodic reports on a timely basis and investor confidence in the accuracy and completeness of our financial statements, which in turn could harm our business and have an adverse effect on our stock price and our ability to raise additional funds.

**ITEM 1B. UNRESOLVED STAFF COMMENTS.**

Disclosure under this item is not applicable because the Company is a smaller reporting company.

**ITEM 2. PROPERTIES.**

Our corporate headquarters and production facility are located at 411 University Ridge, Greenville, South Carolina. The production facility includes approximately 3,200 square feet adjoining our headquarters office, and the facility overall has 9,470 square feet of space. We have five years remaining on the lease for this facility.

Annual rental payments for the next five fiscal years for these facilities are as follows:

2016	\$ 224,410
2017	224,410
2018	224,410
2019	224,410
2020	
2021 and thereafter	\$

**ITEM 3. LEGAL PROCEEDINGS.**

We are subject, from time to time, to various claims, lawsuits or actions that arise in the ordinary course of business. As of March 31, 2015 there were no material outstanding claims by the Company or against the Company.

In May 2014, the Company received a subpoena issued by the SEC ordering the provision of documents and related information concerning various corporate transactions between the Company and its predecessors and other persons and entities. The Company is fully cooperating with this ongoing inquiry.

**ITEM 4. MINE SAFETY DISCLOSURES.**

Not applicable.



**PART II****ITEM 5. MARKET FOR COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER PURCHASES OF EQUITY SECURITIES*****Market Information***

Our common stock is currently quoted on the OTC Bulletin Board and OTC PINK marketplace under the ticker “SCIO”. Because we are quoted on the OTC Bulletin Board, our common stock is less liquid, may receive less coverage by security analysts and news media, and generate lower prices than might otherwise be obtained if it were listed on a national securities exchange. The OTC Bulletin Board prices are quotations, which reflect inter-dealer prices without retail mark-up, mark-down, or commissions and may not represent actual transactions.

The following table sets forth the quarterly high and low bid prices for our common stock for the fiscal years ending March 31, 2014 and 2015, as reported by the OTC Bulletin Board. These quotations reflect inter-dealer prices, without retail mark-up, markdown, or commission, and may not represent actual transactions.

Fiscal Year Ended March 31, 2014	High	Low
First Fiscal Quarter	\$ 1.00	\$ 0.31
Second Fiscal Quarter	0.54	0.15
Third Fiscal Quarter	0.51	0.26
Fourth Fiscal Quarter	0.40	0.15
Fiscal Year Ended March 31, 2015	High	Low
First Fiscal Quarter	\$ 0.75	\$ 0.22
Second Fiscal Quarter	0.55	0.32
Third Fiscal Quarter	0.97	0.28
Fourth Fiscal Quarter	1.42	0.80

As of June 23, 2015, there were 57,516,499 shares of common stock outstanding held by approximately 790 stockholders of record.

***Dividends***

We have not declared or paid any cash dividends on our common stock since our inception, and we do not intend to declare cash dividends for the foreseeable future. Any decision to pay dividends will depend upon our profitability at the time, cash available, and other factors; however, it is currently anticipated that any future profits received from operations will be retained for operations.

***Recent Sales of Unregistered Securities***

Unless otherwise indicated, the issuances of our securities listed below were made in reliance on an exemption from registration under Section 4(a)(2) of the Securities Act, as we reasonably believed that the investors were sophisticated, that no general solicitations were involved and the transactions did not otherwise involve a public offering.

At the request of the then Board of Directors, the Company entered into an agreement, effective April 12, 2014, with Mr. Joseph Cunningham to provide consulting services to the Company. Under this agreement, the Company agreed to provide Mr. Cunningham \$4,000 and 20,000 shares of common stock per month in exchange for his professional services to the Company. This contract expired in August 2014. During the fiscal year ended March 31, 2015, the

## Edgar Filing: Scio Diamond Technology Corp - Form 10-K

Company issued 80,000 shares to Mr. Cunningham. These shares were valued at an average of \$0.43 per share based on the closing prices of the shares on the dates of grant and the Company recognized \$34,200 in professional and consulting fee expense for these shares during the fiscal year ended March 31, 2015.

On June 20, 2014, the then Board of Directors granted restricted stock grants to Mr. Michael Laub of 50,000 shares for previously performed services rendered to the Company. While the Company did not recognize expense for this restricted stock grant since it was in exchange for expenses previously accrued by the Company, the shares provided Mr. Laub were valued at \$0.24 per share.

On July 15, 2014, the Board of Directors approved the issuance and sale of up to 2,000,000 shares of common stock to accredited investors at a price of \$0.30. On September 25, 2014, the Board agreed to increase the size of the offering up to 6,666,667 shares to raise up to \$2,000,000. The Company completed the offering on December 23, 2014 and issued 6,666,664 shares of common stock, at a price of \$0.30 per share, for total cash proceeds of \$2,000,000.

On October 30, 2014, the Board of Directors approved the issuance of 50,000 shares to Bradley Robb to settle \$15,000 of liabilities for services rendered to the Company. Also on this date, the Board approved the issuance of 95,522 shares of stock to an affiliate of our landlord to settle \$28,657 of outstanding rent liabilities. The shares issued in each of these transactions were valued at \$0.30 per share.

On March 12, 2015, the Board of Directors approved the issuance of 333,333 shares to Neil Koppel to settle \$100,000 of liabilities for inventory provided to the Company. The shares issued in this transaction were valued at \$0.30 per share, the closing price of our stock on the date the inventory was acquired.

#### **ITEM 6. SELECTED FINANCIAL DATA.**

Not applicable.

#### **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

*You should read the following discussion in conjunction with the financial statements of the Company, and the notes to those statements, included elsewhere in this Form 10-K, as well as the rest of this Annual Report on Form 10-K. The statements in this discussion regarding outlook, our expectations regarding our future performance, liquidity and capital resources and other non-historical statements in this discussion are forward-looking statements. These forward-looking statements are subject to numerous risks and uncertainties, including, but not limited to, the risks and uncertainties described in the "Risk Factors" and "Cautionary Notice Regarding Forward Looking Statements" sections of this Annual Report on Form 10-K. Our actual results may differ materially from those contained in or implied by any forward- looking statements.*

#### **GENERAL**

##### *Corporate History*

We were incorporated on September 17, 2009 in the State of Nevada under the name Krossbow Holdings Corporation ("Krossbow"). Krossbow did not implement its original business plan and decided to acquire existing technology to seek to efficiently and effectively produce man-made diamond. In connection with this change in business purpose, Krossbow changed its name to Scio Diamond Technology Corporation to reflect its new business direction.

On August 5, 2011, Edward S. Adams and Michael R. Monahan acquired control of the Company through the purchase of shares of the Company's issued and outstanding common stock from Jason Kropp, Krossbow's sole director and executive officer at that time. Messrs. Monahan and Adams served on the Company's Board of Directors until their resignations from the Board on June 30, 2013, and June 23, 2014, respectively. Additionally, on August 5, 2011, the Company executed an Asset Purchase Agreement with another privately-held Nevada corporation that also had the name "Scio Diamond Technology Corporation" ("Private Scio"). Under the terms of the Asset Purchase Agreement, the Company purchased the name "Scio Diamond Technology Corporation" and acquired other rights from Private Scio for 13,000,000 newly issued shares of common stock of the Company.

On August 31, 2011, the Company acquired certain assets of ADI, consisting primarily of diamond growing machines and intellectual property related thereto, for which the Company paid ADI an aggregate of \$2,000,000. In connection with the ADI Asset Purchase, the Company also agreed to provide certain current and former stockholders of ADI qualifying as accredited investors the opportunity to acquire up to approximately 16 million shares of common stock of the Company for \$0.01 per share.

On June 5, 2012, the Company acquired substantially all of the assets of ADGC, consisting primarily of lab-grown diamond gemstone-related know-how, inventory, and various intellectual property, in exchange for \$100,000 in cash and the opportunity for certain current and former stockholders of ADGC qualifying as accredited investors to acquire up to approximately 1 million shares of common stock of the Company for \$0.01 per share.

In December 2011, the Company began a build-out of its Greenville, South Carolina production facility. Construction was largely completed in March 2012 and equipment was moved from ADI's former facility in Massachusetts to South Carolina over the first calendar quarter of 2012. The Company began initial production with ten diamond growing machines in July 2012. Our initial production was focused on industrial cutting tool products supplied to a single customer. Since March 2013, the Company has expanded its product focus to include gemstone diamond material.

On September 16, 2013, the Company entered into the Grace Rich Agreements to form a joint venture with operations in the People's Republic of China to deploy at least 100 Scio designed diamond growing machines. Under the Grace Rich Agreements, the Company has agreed to license its proprietary technology for the manufacture of diamond gemstones of agreed upon specifications. In exchange for the license, the Company will receive licensing and development revenue and a 30% ownership position in the joint venture. In addition to the licensed technology, the Grace Rich Agreements include obligations for the Company to provide and be compensated for technology consulting services to the joint venture to support the start-up of operations. The Company is not required to make any on-going funding contributions to the joint venture and its ownership stake cannot be reduced from 30%.

On December 16, 2014, the Company entered into the Grower Sale-Lease Agreement with HGI. Pursuant to the Grower Sale-Lease Agreement, the Company agreed to a sale-leaseback arrangement for certain diamond growers produced by the Company during the term of the Grower Sale-Leaseback Agreement by which the Company will sell diamond growers to HGI and then lease the growers back from HGI. The direct profit margin generated from the growers will be split between the Company and HGI in accordance with the Grower Sale-Lease Agreement. The Grower Sale-Lease Agreement requires the Company to operate and service the growers, and requires HGI to up-fit certain existing growers and to make capital improvements to the new growers under certain circumstances. The Company will also have the right to repurchase the leased growers upon the occurrence of certain events.

On December 18, 2014 entered into an arrangement with Renaissance creating RCDC. The Company and Renaissance are each 50% members of RCDC. The arrangement was entered into in order to facilitate the development of procedures and recipes for, and to market and sell, lab-grown fancy-colored diamonds. RCDC will purchase rough diamond material from the Company and process and finish the material into finished gemstones for sale to various retailers and other participants in the market for gemstones. Profits generated by RCDC's operations will be distributed between the Company and Renaissance according to the terms of the LLC Agreement.

### *Business Overview*

The Company's primary mission is the development of profitable and sustainable commercial production of its diamond materials, which are suitable for known, emerging and anticipated industrial, technology and consumer applications. The Company intends to pursue progressive development of its core diamond materials technologies and related intellectual property that the Company hopes will evolve into product opportunities across various applications. We believe these opportunities may be monetized through a combination of end product sales, joint ventures and licensing arrangements with third parties, and through continued development of intellectual property. Anticipated application opportunities for the Company's diamond materials include the following: precision cutting devices, diamond gemstone jewelry, power switches, semiconductor processors, optoelectronics, geosciences, water purification, and MRI and other medical science technology.

While the Company product offering continues to include industrial products, as of March 31, 2015 nearly all of the Company's production capacity is being sold as gemstone materials. As of March 31, 2015, we had generated \$3,026,282 in net revenue since inception from sales of our diamond materials and licensing of our technology. To date, over 50% of our product has been sold overseas and 100% of these sales have been to external customers and our joint venture partners as discussed in Item 8, Notes 10 and 11. We expect continued development of an international market for our diamond materials.

See Part I, Item 1. (Business) for additional information regarding our business.

### *Significant Partner Agreements*

On September 16, 2013, the Company entered into the Grace Rich Agreements to form a joint venture with operations in the People's Republic of China to deploy at least 100 Scio designed diamond growing machines. Under the Grace

Rich Agreements, the Company has agreed to license its proprietary technology for the manufacture of diamond gemstones of agreed upon specifications. In exchange for the license, the Company will receive licensing and development revenue and a 30% ownership position in the joint venture. In addition to the licensed technology, the Grace Rich Agreements include obligations for the Company to provide and be compensated for technology consulting services to the joint venture to support the start-up of operations. The Company is not required to make any on-going funding contributions to the joint venture and its ownership stake cannot be reduced from 30%.

On December 16, 2014, the Company entered into the Grower Sale-Lease Agreement with HGI. Pursuant to the Grower Sale-Lease Agreement, the Company agreed to a sale-leaseback arrangement for certain diamond growers produced by the Company during the term of the Grower Sale-Leaseback Agreement by which the Company will sell diamond growers to HGI and then lease the growers back from HGI. The direct profit margin generated from the growers will be split between the Company and HGI in accordance with the Grower Sale-Lease Agreement. The Grower Sale-Lease Agreement requires the Company to operate and service the growers, and requires HGI to up-fit certain existing growers and to make capital improvements to the new growers under certain circumstances. The Company will also have the right to repurchase the leased growers upon the occurrence of certain events.

On December 18, 2014 entered into an arrangement with Renaissance creating RCDC. The Company and Renaissance are each 50% members of RCDC. The arrangement was entered into in order to facilitate the development of procedures and recipes for, and to market and sell, lab-grown fancy-colored diamonds. RCDC will purchase rough diamond material from the Company and process and finish the material into finished gemstones for sale to various retailers and other participants in the market for gemstones. Profits generated by RCDC's operations will be distributed between the Company and Renaissance according to the terms of the LLC Agreement.

#### *Critical Accounting Policies*

We have adopted various accounting policies that govern the application of accounting principles generally accepted in the United States ("GAAP"). We describe our significant accounting policies in the notes to our audited financial statements as of March 31, 2015.

Some of the accounting policies involve significant judgments and assumptions by us that have a material impact on the carrying value of our assets and liabilities. We consider these accounting policies to be critical accounting policies. The judgment and assumptions we use are based on historical experience and other factors that we believe to be reasonable under the circumstances. Because of the nature of the judgments and assumptions we make, actual results could differ from these judgments and estimates and could materially affect the carrying values of our assets and liabilities and our results of operations.

The following is a summary of the more significant judgmental estimates and complex accounting principles, which represent our critical accounting policies.

#### *Revenue Recognition*

We recognize product revenue when persuasive evidence of an arrangement exists, delivery of products has occurred, the sales price is fixed or determinable, and collectability is reasonably assured. For our Company, this generally means that we recognize revenue when we or our fabrication vendor has shipped finished product to the customer. Our sales terms do not allow for a right of return except for matters related to any manufacturing defects on our part.

For product sales to our joint venture partners for further processing and finishing, we currently defer all revenues when products are shipped. We currently recognize revenue when the joint venture partner sells the finished goods manufactured from our materials. Licensing and development revenues are recognized in the month as detailed in appropriate licensing and development contracts. In the event that licensing funds are received prior to the contractual commitment, The Company will recognize deferred revenue (liability) for the amount received.

#### *Inventories*

Inventories are stated at the lower of average cost or market. The carrying value of inventory is reviewed and adjusted based upon slow moving and obsolete items. Inventory costs include material, labor, and manufacturing overhead and are determined by the "first-in, first-out" (FIFO) method. The components of inventories include raw materials and supplies, work in process and finished good.

The Company has periodically experienced selling prices that were lower than cost and as a result has recorded a lower of cost or market write down to the value of our inventory. The estimation of the total write-down to inventory involves management judgments and assumptions, including assumptions regarding future selling price forecasts, the estimated costs to complete and disposal costs.

#### *Property, Plant and Equipment*

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

Depreciation of property, plant and equipment is on a straight-line basis beginning at the time it is placed in service, based on the following estimated useful lives:

	Years
Machinery and equipment	3 15
Furniture and fixtures	3 10
Engineering equipment	5 12

25



Leasehold improvements are depreciated at the lesser of the remaining term of the lease or the life of the asset (generally three to seven years).

Expenditures for major renewals and betterments that extend the useful lives of property and equipment are capitalized. Expenditures for maintenance and repairs are charged to expense as incurred.

### *Intangible Assets*

Intangible assets, such as acquired in-process research and development (“IPRD”) costs, are considered to have an indefinite useful life until such time as they are put into service at which time they will be amortized on a straight-line basis over the shorter of their economic or legal useful life. Management’s estimate of useful life of any patents when placed in service is a critical judgment. Management evaluates indefinite life intangible assets for impairment on an annual basis and on an interim basis if events or changes in circumstances between annual impairment tests indicate that the asset might be impaired. The ongoing evaluation for impairment of its indefinite life intangible assets requires significant management estimates and judgment. Management reviews definite life intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

A substantial portion of the Company’s patent portfolio is considered in service due to the inherent value of the patents to our on-going manufacturing operations. Through March 31, 2015, the Company has allocated \$8,135,063 to patents that are being amortized over a period ranging from 6.75 years to 19.46 years corresponding to their remaining life.

The Company continues to classify the remaining patent portfolio as IPRD and believes that the IPRD has alternative future use and value. Applicable accounting guidance requires an indefinite life for IPRD assets until such time as the commercialization can be reasonably estimated, at which time the assets will be available for their intended use. At such time as those requirements are met, we believe that consideration of the legal life of the intellectual property protection should be of considerable importance in determining the useful life. Upon commercialization and determination of the useful life of the intellectual property assets, consideration will be given to the eventual expiration of the intellectual property rights underlying certain critical aspects of our manufacturing process.

## **RESULTS OF OPERATIONS**

### *Fiscal Year Ended March 31, 2015 Compared to the Fiscal Year Ended March 31, 2014*

During the fiscal year ended March 31, 2015, we recorded net revenue of \$726,193, compared to \$1,418,341 in net revenue during the fiscal year ended March 31, 2014. A portion of this decrease is due to the Company receiving \$375,000 in licensing fees from the Grace Rich joint venture during the fiscal year ended March 31, 2015, while we received \$625,000 in the prior period. The Company does not anticipate receiving any additional licensing revenues from the Grace Rich joint venture until it is expected to be operational during calendar year 2016. Product revenues for the fiscal year ended March 31, 2015 were \$351,193 versus \$793,341 in the prior period. The Company deferred \$215,375 in product revenues for sales to the RCDC joint venture during the fiscal year ended March 31, 2015. The remaining reduction in revenue is due to reduced product sales and lower product prices during the fiscal year ended March 31, 2015.

Cost of goods sold was \$1,497,465 for the fiscal year ended March 31, 2015 versus \$2,321,534 for the fiscal year ended March 31, 2014. The Company deferred costs related to deferred revenue from sales to the RCDC joint venture of \$179,969 during the fiscal year ended March 31, 2015. Cost of goods sold includes direct and indirect labor costs of \$397,767 during the fiscal year ended March 31, 2015 and \$577,200 during the fiscal year ended March 31, 2014. Depreciation expense of \$603,604 and \$683,572 was recorded in cost of goods sold during the fiscal years ended March 31, 2015 and 2014, respectively. The overall decrease in cost of goods sold was due to reduced product sales, increased deferred costs, reduced depreciation, and lower labor expenses included in cost of goods sold during the

fiscal year ended March 31, 2015 versus the year ended March 31, 2014.

We incurred a net amount of \$566,154 in professional and consulting fees during the fiscal year ended March 31, 2015. This amount includes reductions of \$343,556 related to the reversal of expenses from the Settlement Agreement, and a reduction of \$168,015 for payments made for legal fees from the prior fiscal year by our insurance carrier. Without these adjustments, professional and consulting fees were \$1,077,725 compared to \$1,272,212 for the fiscal year ended March 31, 2014. This reduction of \$194,487 is largely due to reduced legal fees. Salary and benefit expenses recognized as general and administrative expenses were \$821,272 and \$723,805 during the fiscal years ended March 31, 2015 and 2014, respectively. This increase of \$97,467 is the result of the Company recognizing \$305,077 in executive severance offset by reductions in compensation expense during the fiscal year ended March 31, 2015 versus the fiscal year ended March 31, 2014.

The other components of our general and administrative expenses were relatively consistent between the fiscal year ended March 31, 2015 and 2014. Rent, equipment lease and facilities expenses were \$145,252 and \$150,502, respectively; marketing costs were \$59,727 and \$49,216, respectively; depreciation and amortization expenses were \$798,477 and \$799,928, respectively; and corporate general and administrative expenses were \$345,263 and \$379,552, respectively.

The Company reached an agreement with a former legal services provider that allowed the Company to settle outstanding past legal fees from prior fiscal years. This settlement of \$165,453 was recorded as forgiveness of legal accounts payable during the fiscal year ended March 31, 2015.

During the fiscal year ended March 31, 2015, management evaluated intangible assets included in IPRD and determined that certain projects will no longer be pursued for further development resulting in an impairment charge of \$418,065 recognized during the period. There were no impairment charges during the fiscal year ended March 31, 2014.

During the fiscal year ended March 31, 2015, the Company evaluated fixed assets acquired from ADI and disposed of obsolete equipment with a book value of \$162,609 and assets held for sale of \$20,000. The Company made a similar evaluation in the fiscal year ending March 31, 2014 that resulted in a loss on disposal of fixed assets of \$129,308 and an impairment of fixed assets charge of \$381,798 during that fiscal year.

We have continued to generate limited revenue to offset our expenses, and so we have incurred net losses. Our net loss for fiscal year ended March 31, 2015 was \$4,141,653, compared to a net loss of \$4,950,953 during the fiscal year ended March 31, 2014. Our net loss per share for the fiscal year ended March 31, 2015 was \$(0.08) per share, compared to a net loss per share of \$(0.10) for the fiscal year ended March 31, 2014. The weighted average number of shares outstanding was 53,025,462 and 49,548,045, for the fiscal years ended March 31, 2015 and 2014, respectively.

### ***FINANCIAL CONDITION***

At March 31, 2015, we had total assets of \$12,231,394 compared to total assets of \$12,850,139 at March 31, 2014. This decrease in assets was primarily related to write downs and depreciation of fixed assets and impairment charges and amortization of intangibles, more than offsetting increases in current assets. We had cash of \$767,214 at March 31, 2015 compared to \$47,987 at March 31, 2014. This increase is due to the Company increasing its borrowings on its notes payable and proceeds from common stock sales. At March 31, 2015 the Company's accounts receivables had increased by \$201,844 from March 31, 2014. This increase is due to outstanding receivables from RCDC. At March 31, 2015, the Company had deferred \$179,969 of contract costs related to deferred revenues from sales to the RCDC joint venture. There were no deferred contract costs at March 31, 2014. The increase in inventory of \$142,943 was primarily due to higher finished goods inventory including gemstone materials of \$70,664 and higher diamond seed material included in raw material and supplies of \$22,847.

Total liabilities at March 31, 2015 were \$4,098,772 compared to total liabilities of \$2,920,722 at March 31, 2014. This increase is largely the result of the Company's borrowings under our notes payable and deferred revenue from sales to RCDC during the year ended March 31, 2015.

The Company had positive working capital (defined as current assets less current liabilities) of \$86,254 at March 31, 2015 versus \$(2,402,369) at March 31, 2014. The most substantial change in working capital was due to the Company's refinancing of short-term notes payable into long-term notes payable. This refinancing improved the working capital of the Company by \$1,412,060. Beyond this refinancing, the major reason for the improvement in working capital was the increase in borrowing on our long-term notes payable and our sale of common stock that provided the Company additional cash resources.

Total shareholders' equity was \$8,132,622 at March 31, 2015, compared to \$9,929,417 at March 31, 2014. Shareholders' equity decreased during the year primarily due to continuing net losses increasing the Company's accumulated deficit more than offsetting increase in additional paid in capital from our common stock offerings.

## ***CASH FLOWS***

### *Operating Activities*

The Company has not generated positive cash flows from operating activities. For the year ended March 31, 2015, net cash flows used in operating activities were \$(2,131,217) compared to \$(1,364,820) for the year ended March 31, 2014. The net cash flow used in operating activities for the year ended March 31, 2015 consists primarily of a net loss of \$(4,141,653) offset by depreciation and amortization of \$1,476,916, loss on disposal of equipment of \$182,609, loss on impairment of in-process research and development of \$418,065, expenses for stock issued in exchange for services of \$77,858, employee stock based compensation of \$155,000, income of \$(29,041) from joint venture, an increase in current assets of \$(157,706) and a decrease in current and other liabilities of \$(113,265).

### *Investing Activities*

For the year ended March 31, 2015, net cash flows used in investing activities were \$(237,496), consisting primarily of the purchases of property, plant, and equipment. Net cash flows used in investing activities were \$(71,889) for the year ended March 31, 2014. This increase is due to the Company's purchases of fixed assets for the expansion of its production facility during the year ended March 31, 2015.

### *Financing Activities*

We have financed our operations primarily through advancements or the issuance of equity and debt instruments. For the years ended March 31, 2015 and March 31, 2014, we generated \$3,087,940 and \$1,261,439 from financing activities, respectively. The cash generated during the year ended March 31, 2015 was primarily from the sale of common stock and the net additional borrowings on the Company's note payable facility.

### **LIQUIDITY AND CAPITAL RESOURCES**

We expect that working capital requirements will continue to be funded through a combination of our existing funds, further issuances of securities, and future credit facilities or corporate borrowings. Our working capital requirements are expected to increase in line with the growth of our business.

As of March 31, 2015, our cash balance was \$767,214. This amount is not expected to be adequate to fund our operations over the next fiscal year ending March 31, 2016. As of March 31, 2015, we had no additional lines of credit or other bank financing arrangements other than as described in Item 8, Note 3. Generally, we have financed operations through March 31, 2015 through the proceeds of sales of our common stock and borrowings under our existing credit facilities. The Company is pursuing additional issuances of equity capital to meet operating cash requirements.

Additional issuances of equity or convertible debt securities will result in dilution to our current stockholders. Such securities might have rights, preferences or privileges senior to our common stock. Additional financing may not be available upon acceptable terms, or at all. If adequate funds are not available or are not available on acceptable terms, we may not be able to take advantage of prospective new business endeavors or opportunities, which could significantly and materially restrict our business operations and could result in the shutdown of operations.

### **MATERIAL COMMITMENTS AND ARRANGEMENTS**

On September 16, 2013, the Company entered into the Grace Rich Agreements with SAAMABA, LLC and S21 Research Holdings to form a joint venture with operations in the People's Republic of China to deploy Scio designed diamond growing machines. Under the Grace Rich Agreements, the Company has agreed to license its proprietary technology for the manufacture of diamond gemstones of agreed upon specifications. In exchange for the license, the Company received licensing and development revenue and a minority ownership position in the joint venture. In addition to the licensed technology, the Grace Rich Agreements include obligations for the Company to provide and be compensated for technology consulting services to the joint venture to support the start-up of operations.

On December 16, 2014, the Company entered into an agreement for the sale and lease of growers with HGI. Pursuant to the Grower Sale-Lease Agreement, the Company agreed to a sale-leaseback arrangement for certain diamond growers produced by the Company during the term of the Grower Sale-Leaseback Agreement by which the Company will sell diamond growers to HGI and then lease the growers back from HGI. The direct profit margin generated from the growers will be split between the Company and HGI in accordance with the Grower Sale-Lease Agreement. The Grower Sale-Lease Agreement requires the Company to operate and service the growers, and requires HGI to up-fit certain existing growers and to make capital improvements to the new growers under certain

circumstances. The Company will also have the right to repurchase the leased growers upon the occurrence of certain events.

On December 18, 2014 entered into an arrangement with Renaissance creating RCDD. The Company and Renaissance are each 50% members of RCDC. The arrangement was entered into in order to facilitate the development of procedures and recipes for, and to market and sell, lab-grown fancy-colored diamonds. RCDC will purchase rough Diamond material from the Company and process and finish the material into finished gemstones for sale to various retailers and other participants in the market for gemstones. Profits generated by RCDC's operations will be distributed between the Company and Renaissance according to the terms of the LLC Agreement.

***OFF BALANCE SHEET ARRANGEMENTS***

As of the date of this Annual Report, we do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

**ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

Not required because the Company is a smaller reporting company.

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.**

***REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM***

To the Board of Directors and

Shareholders of Scio Diamond Technology Corporation

We have audited the accompanying balance sheets of Scio Diamond Technology Corporation (the “Company”) as of March 31, 2015 and 2014, and the related statements of operations, shareholders’ equity, and cash flows for the years then ended. The Company’s management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Scio Diamond Technology Corporation as of March 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has generated limited revenue, incurred net losses and incurred negative operating cash flows since inception and will require additional financing to fund the continued development of products. The availability of such financing cannot be assured. These conditions raise substantial doubt about its ability to continue as a going concern. Management’s plans regarding those matters also are described in Note 1. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Cherry Bekaert LLP

Greenville, South Carolina

June 29, 2015



**SCIO DIAMOND TECHNOLOGY CORPORATION****BALANCE SHEETS  
As of March 31, 2015 and 2014**

	March 31, 2015	March 31, 2014
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 767,214	\$ 47,987
Accounts receivable	243,929	42,085
Other receivables		89,192
Deferred contract costs	179,969	
Inventory	295,760	152,817
Prepaid expenses	57,012	79,078
Prepaid rent	23,050	23,050
 Total current assets	 1,566,934	 434,209
Property, plant and equipment		
Facility	904,813	899,499
Manufacturing equipment	2,927,761	3,171,656
Other equipment	71,059	71,059
Construction in progress	207,252	
 Total property, plant and equipment	 4,110,885	 4,142,214
Less accumulated depreciation	(1,543,652)	(1,029,212)
Net property, plant and equipment	2,567,233	3,113,002
Intangible assets, net		
Prepaid rent, noncurrent	19,238	42,288
Investment in joint venture RCDC	30,041	
Other assets		20,000
 <b>TOTAL ASSETS</b>	 <b>\$ 12,231,394</b>	 <b>\$ 12,850,139</b>
 <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current Liabilities:		
Notes payable	\$	\$ 1,412,060
Accounts payable	708,760	671,782
Customer deposits	38,603	179,610
Deferred revenue	215,375	
Accrued expenses	517,942	573,126
 Total current liabilities	 1,480,680	 2,836,578
 Notes payable, non-current	 2,500,000	
Other liabilities	118,092	84,144

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

TOTAL LIABILITIES	4,098,772	2,920,722
Common stock, \$0.001 par value, 75,000,000 shares authorized; 56,531,499 and 50,739,312 shares issued and outstanding at March 31, 2015 and 2014, respectively	56,532	50,739
Additional paid-in capital	26,815,005	24,476,940
Accumulated deficit	(18,738,915)	(14,597,262)
Treasury stock, no and 1,000,000 shares at March 31, 2015 and 2014, respectively		(1,000)
Total stockholders' equity	8,132,622	9,929,417
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 12,231,394	\$ 12,850,139

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

**SCIO DIAMOND TECHNOLOGY CORPORATION**

**STATEMENTS OF OPERATIONS**  
**For the years ended March 31, 2015 and 2014**

	Year Ended March 31, 2015	Year Ended March 31, 2014
Revenue		
Product revenue, net	\$ 351,193	\$ 793,341
Licensing revenue	375,000	625,000
Revenues, net	726,193	1,418,341
Cost of goods sold		
Cost of goods sold	1,497,465	2,321,534
Gross margin (deficit)	(771,272)	(903,193)
General and administrative expenses		
Professional and consulting fees	566,154	1,272,212
Salaries and benefits	821,272	723,805
Rent, equipment lease and facilities expense	145,252	150,502
Marketing costs	59,727	49,216
Depreciation and amortization	798,477	799,928
Corporate general and administrative	345,263	379,552
Forgiveness of legal accounts payable	(165,453)	
Loss on impairment of in-process research and development	418,065	
Loss on disposal of equipment	182,609	129,308
Loss on impairment of fixed assets		381,798
Total general and administrative expenses	3,171,366	3,886,321
Loss from operations	(3,942,638)	(4,789,514)
Other income (expense)		
Income from joint venture RCDC	29,041	
Interest expense	(228,056)	(161,439)
Net loss	\$ (4,141,653)	\$ (4,950,953)
Loss per share		
Basic:		
Weighted average number of shares outstanding	53,025,462	49,548,045
Loss per share	\$ (0.08)	\$ (0.10)
Fully diluted:		
Weighted average number of shares outstanding	53,025,462	49,548,045
Loss per share	\$ (0.08)	\$ (0.10)

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



**SCIO DIAMOND TECHNOLOGY CORPORATION**

**STATEMENTS OF CASH FLOW**  
**For the years ended March 31, 2015 and 2014**

	Year Ended March 31, 2015	Year Ended March 31, 2014
Cash flows from operating activities:		
Net loss	\$ (4,141,653)	\$ (4,950,953)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,476,916	1,574,418
Loss on disposal of equipment	182,609	129,308
Loss on impairment of fixed assets		381,798
Loss on impairment of in-process research and development	418,065	
Expense for stock and inventory issued in exchange for operating expenses	77,858	421,496
Income from joint venture RCDC	(29,041)	
Employee stock based compensation	155,000	193,150
Inventory write down	68,722	100,557
Changes in assets and liabilities:		
Decrease in accounts receivable	13,531	26,957
Decrease/(increase) in other receivables	89,192	(89,192)
Decrease/(increase) in prepaid expenses, rent and other assets	(37,517)	44,260
Decrease/(increase) in inventory	(291,634)	258,127
Increase in accounts payable	36,978	386,131
(Decrease)/increase in customer deposits	(141,007)	179,610
Decrease in accrued expenses	(43,184)	(54,436)
Increase in other liabilities	33,948	33,949
 Net cash used in operating activities	 (2,131,217)	 (1,364,820)
Cash flows from investing activities:		
Purchase of property, plant and equipment	(236,496)	(71,889)
Investment in joint venture RCDC	(1,000)	
 Net cash used in investing activities	 (237,496)	 (71,889)
Cash flows from financing activities:		
Proceeds from sale of common stock - net of fees	2,000,000	129
Proceeds from notes payable	2,653,615	1,412,060
Finance charges paid on note payable		(150,750)
Payments on notes payable	(1,565,675)	
 Net cash provided by financing activities	 3,087,940	 1,261,439
 Change in cash and cash equivalents	 719,227	 (175,270)
Cash and cash equivalents, beginning of period	47,987	223,257
 Cash and cash equivalents, end of period	 \$ 767,214	 \$ 47,987

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

(continued)

**SCIO DIAMOND TECHNOLOGY CORPORATION**

**STATEMENTS OF CASH FLOW**  
**For the years ended March 31, 2015 and 2014**  
**(Continued)**

	Year Ended March 31, 2015	Year Ended March 31, 2014
Supplemental cash flow disclosures:		
Cash paid during the year for:		
Interest	\$ 84,165	\$ 18,874
Income taxes	\$	\$
Non-cash investing and financing activities:		
Payment of accounts payable and accrued expenses with common stock	\$ 112,000	\$ 81,761
Manufacturing equipment transferred to assets held for sale	\$	\$ 20,000

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

## SCIO DIAMOND TECHNOLOGY CORPORATION

STATEMENTS OF SHAREHOLDERS' EQUITY  
For the years ended March 31, 2015 and 2014

	Common Stock Shares	Common Stock Amount	Additional Paid in Capital	Treasury Stock Shares	Treasury Stock Amount	Accumulated Deficit	Total
Balance, April 1, 2013	47,736,812	\$ 47,737	\$ 23,789,478	(1,000,000)	\$ (1,000)	\$ (9,646,309)	\$ 14,189,906
Common stock issued in exchange for consulting services	1,002,500	1,002	318,198				319,200
Common stock issued in exchange for past legal services	1,000,000	1,000	163,000				164,000
Administrative fee received for previous stock issuance			129				129
Common stock issued for indemnification of legal settlement	1,000,000	1,000	(1,000)				
Employee stock based compensation			193,150				193,150
Warrants issued in exchange for consulting services			13,985				13,985
Net loss for the fiscal year ended March 31, 2014						(4,950,953)	(4,950,953)
Balance, March 31, 2014	50,739,312	50,739	24,476,940	(1,000,000)	(1,000)	(14,597,262)	9,929,417
Common stock issued in exchange for operating expenses and	558,856	559	177,299				177,858



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

inventory					
Common stock issued in exchange for past consulting services	50,000	50	11,950		12,000
Retirement of treasury stock	(1,000,000)	(1,000)		1,000,000	1,000
Common stock issued for cash @ \$0.30 per share	6,666,664	6,667	1,993,333		2,000,000
Common stock returned to Company and cancelled	(1,000,000)	(1,000)	1,000		
Employee stock based compensation	516,667	517	154,483		155,000
Net loss for the fiscal year ended March 31, 2015					(4,141,653)
Balance, March 31, 2015	56,531,499	\$ 56,532	\$ 26,815,005	\$	\$ (18,738,915)
					\$ 8,132,622

The accompanying notes are an integral part of these 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.

These factors raise substantial doubt about the Company’s ability to continue as a going concern. During the year ended March 31, 2015, management has responded to these circumstances by taking the following actions:

- Raised \$2 million in equity investment in the Company in the form of private placements of common shares to accredited investors. Funds have been used to fund current operations;
- Raised \$2.5 million in investment in the Company in the form of secured debt. Funds have been used to re-finance higher interest rate secured debt, the expansion of our operations and to fund current operations;
- Established a joint venture with Renaissance Diamonds, Inc. focused on the creation of recipes and procedures to develop, market, and sell lab-grown fancy-colored diamonds; and
- Enhanced efforts on expanding and optimizing production of existing manufacturing capabilities.

### *Accounting Basis*

The financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”).

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. On an ongoing basis, the Company evaluates its estimates, including those related to revenue recognition, provision for doubtful accounts, sales returns, provision for inventory obsolescence, fair value of acquired intangible assets, useful lives of intangible assets and property and equipment, employee stock options, and contingencies and litigation, among others. The Company generally 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 amounts recorded could differ materially from those estimates

In accordance with Accounting Standards Codification (“ASC”) 323, *Investments Equity Method and Joint Ventures*, the Company uses the equity method of accounting for investments in corporate joint ventures for which the Company has the ability to exercise significant influence but does not control and is not the primary beneficiary. Significant influence typically exists if the Company has a 20% to 50% ownership interest in the venture unless predominant evidence to the contrary exists. Under this method of accounting, the Company records its proportionate share of the net earnings or losses of equity method investees and a corresponding increase or decrease to the investment balances. Cash payments to equity method investees such as additional investments, loans and advances and expenses incurred on behalf of investees, as well as payments from equity method investees such as dividends, distributions and repayments of loans and advances are recorded as adjustments to investment balances. When the Company’s carrying value in an equity method investee is reduced to zero, no further losses are recorded in the Company’s financial statements unless the Company guaranteed obligations of the equity method investee or has

committed additional funding. When the equity method investee subsequently reports income, the Company will not record its share of such income until it equals the amount of its share of losses not previously recognized. The Company evaluates its equity method investments for impairment whenever events or changes in circumstances indicate that the carrying amounts of such investments may not be recoverable.

*Fair Value of Financial Instruments*

The carrying value of cash and cash equivalents, accounts receivable, accounts payable and notes payable approximate their fair value due to the short-term nature of these instruments.

*Cash and Cash Equivalents*

For purposes of the statement of cash flows, the Company considers highly liquid financial instruments purchased with an original maturity of three months or less when purchased to be cash equivalents. At March 31, 2015 and 2014, the Company held no cash equivalents.

*Basic and Diluted Net Loss per Share*

Net loss per share is presented under two formats: basic net loss per common share, which is computed using the weighted average number of common shares outstanding during the period, and diluted net loss per common share, which is computed using the weighted average number of common shares outstanding, and the weighted average dilutive potential common shares outstanding, computed using the treasury stock method. Currently, for all periods presented, diluted net loss per share is the same as basic net loss per share as the inclusion of weighted average shares of common stock issuable upon the exercise of options and warrants would be anti-dilutive.

The following table summarizes the number of securities outstanding at each of the periods presented, which were not included in the calculation of diluted net loss per share as their inclusion would be anti-dilutive:

	March 31,	
	2015	2014
Common stock options and warrants	5,799,295	9,609,295

*Allowance for Doubtful Accounts*

An allowance for uncollectible accounts receivable is maintained for estimated losses from customers' failure to make payment on accounts receivable due to the Company. Management determines the estimate of the allowance for uncollectible accounts receivable by considering a number of factors, including: (1) historical experience, (2) aging of accounts receivable and (3) specific information obtained by the Company on the financial condition and the current credit worthiness of its customers. The Company also maintains a provision for estimated returns and allowances based upon historical experience. The Company has determined that an allowance was not necessary at March 31, 2015 or 2014.

*Other Receivables*

As of March 31, 2014, the Company considered a pending insurance settlement over the actions of a Company supplier of \$89,192 as an other receivable. This settlement was paid during the fiscal year ended March 31, 2015.

*Inventories*

Inventories are stated at the lower of average cost or market. The carrying value of inventory is reviewed and adjusted based upon slow moving and obsolete items. Inventory costs include material, labor, and manufacturing overhead and are determined by the "first-in, first-out" (FIFO) method. The components of inventories are as follows:

	March 31, 2015	March 31, 2014
Raw materials and supplies	\$ 58,390	\$ 35,543
Work in process	31,371	25,611
Finished goods	205,999	91,663
	\$ 295,760	\$ 152,817

During the first fiscal quarter of the fiscal year ended March 31, 2015, we experienced selling prices that were lower than cost and as a result recorded a lower of cost or market write down of \$68,722 to the value of our inventory which is included in cost of good sold. During the fiscal year ended March 31, 2014, the Company recorded a lower of cost or market write down to inventory of \$100,557 which is included in cost of goods sold. The estimation of the total write-down to inventory involves management judgments and assumptions, including assumptions regarding future selling price forecasts, the estimated costs to complete and disposal costs.

*Property, Plant and Equipment*

Depreciation of property, plant and equipment is on a straight line basis beginning at the time it is placed in service, based on the following estimated useful lives:

	Years
Machinery and equipment	3 15
Furniture and fixtures	3 10
Engineering equipment	5 12

Leasehold improvements which are included in facility fixed assets on the balance sheet are depreciated over the lesser of the remaining term of the lease or the life of the asset (generally three to seven years).

Expenditures for major renewals and betterments that extend the useful lives of property and equipment are capitalized. Expenditures for maintenance and repairs are charged to expense as incurred. Manufacturing equipment was placed into service beginning July 1, 2012. The Company incurred total depreciation expense of \$619,656 and \$700,690 for the years ended March 31, 2015 and 2014, respectively.

During the fiscal year ended March 31, 2015, the Company disposed of assets held for sale of \$20,000 and of fixed assets that were no longer necessary for the Company's operations with a net book value of \$162,609. During the fiscal year ended March 31, 2014, the Company closed its operations in Hudson, Massachusetts and recognized a loss of \$129,308 for the disposal of certain fixed assets at the location. Concurrent with the closing of the Hudson facility, the Company re-evaluated the useful life of certain fixed assets acquired from ADI in 2012 and decided that an impairment charge related to these assets of \$381,798 was appropriate.

#### *Intangible Assets*

Intangible assets, such as acquired in-process research and development costs, are considered to have an indefinite useful life until such time as they are put into service at which time they will be amortized on a straight-line basis over the shorter of their economic or legal useful life. Management evaluates indefinite life intangible assets for impairment on an annual basis and on an interim basis if events or changes in circumstances between annual impairment tests indicate that the asset might be impaired. The ongoing evaluation for impairment of its indefinite life intangible assets requires significant management estimates and judgment. Management reviews definite life intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. During the fiscal year ended March 31, 2015, management evaluated assets included in IPRD and determined that certain projects will no longer be pursued for further development resulting in an impairment charge of \$418,065 being recognized during the fiscal year. There were no impairment charges during the fiscal year ended March 31, 2014.

#### *Income Taxes*

Income taxes are accounted for under the asset and liability method. Deferred income taxes reflect the tax consequences on future years of differences between the tax bases of assets and liabilities and their financial reporting amounts. Valuation allowances are provided against deferred tax assets when it is more likely than not that an asset will not be realized in accordance with ASC 740, *Accounting for Income Taxes*.

Management has evaluated the potential impact in accounting for uncertainties in income taxes and has determined that it has no significant uncertain income tax positions as of March 31, 2015 or 2014. Income tax returns subject to review by taxing authorities include March 31, 2010 through March 31, 2015.

#### *Stock-based Compensation*

Stock-based compensation for the value of stock options is estimated on the date of the grant using the Black-Scholes option-pricing model. The Black-Scholes model takes into account implied volatility in the price of the Company's stock, the risk-free interest rate, the estimated life of the equity-based award, the closing market price of the

Company's stock on the grant date and the exercise price. The estimates utilized in the Black-Scholes calculation involve inherent uncertainties and the application of management judgment.

*Concentration of Credit Risk*

During the year ended March 31, 2015 the Company had 31 different customers and one customer accounted for more than 10% of our total revenues. This customer was Grace Rich LTD, our joint venture partner that accounted for \$385,801 of total revenue. At the end of the fiscal year ended March 31, 2015, the Company was selling substantially all of its production to the RCDC joint venture and had a receivable from RCDC at March 31, 2015 of \$241,950. The Company expects this concentration of sales to RCDC to continue in the future.

38

### *Revenue Recognition*

We recognize product revenue when persuasive evidence of an arrangement exists, delivery of products has occurred, the sales price is fixed or determinable, and collectability is reasonably assured. For our Company, this generally means that we recognize revenue when we or our fabrication vendor has shipped finished product to the customer. Our sales terms do not allow for a right of return except for matters related to any manufacturing defects on our part.

For product sales to our joint venture partners for further processing and finishing, we currently defer all revenues when products are shipped. We currently recognize revenue when the joint venture partner sells the finished goods manufactured from our materials. Licensing and development revenues are recognized in the month as detailed in appropriate licensing and development contracts. In the event that licensing funds are received prior to the contractual commitment, the Company will recognize deferred revenue (liability) for the amount received.

### *Recent Accounting Pronouncements*

In July 2012, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2012-02, *Testing Indefinite-Lived Intangible Assets for Impairment* (the revised standard). Under the amendments in this updates, a company has the option first to assess qualitative factors to determine whether the existence of events and circumstances indicates that the it is more likely than not that the indefinite-lived intangible asset is impaired as a basis for determining whether it is necessary to perform the qualitative impairment test in accordance with Topic 350. The more likely than not threshold is defined as having a likely-hood of more than fifty percent. If after assessing the qualitative factors, a company determines it does not meet the more likely than not threshold, a company is required to perform the quantitative impairment test by calculating the fair value of an indefinite-lived intangible asset and comparing the fair value with the carrying amount of the asset. The Amendments in this update are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. The Company adopted this new standard in the fiscal year ended March 31, 2014 and the adoption did not have a significant impact on its financial statements.

In July 2013, the FASB issued ASU 2013-11, *Income Taxes Presentation of an Unrecognized Tax benefit When a Net Operation Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* ("ASU 2013-11") which is part of ASC 740, *Income Taxes*. The new guidance requires and entity to present an unrecognized tax benefit and an NOL carryforward, a similar tax loss or a tax credit carryforward on a net basis as part of a deferred tax asset, unless the unrecognized tax benefit is not available to reduce the deferred tax asset component or would not be utilized for that purpose, then a liability would be recognized. ASU 2013-11 is effective for annual and interim periods for fiscal years beginning after December 15, 2013. The Company is currently evaluating the impact of the April 1, 2014 adoption of this guidance on its financial statements.

In May 2014, the FASB issued ASU 2014-9, *Revenue from Contracts with Customers (Topic 606)*. This guidance requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This guidance is effective for annual reporting periods beginning after December 15, 2016 and early adoption is not permitted. The Company will adopt this standard in fiscal year 2018. The Company has not yet determined the effect, if any, that the adoption of this standard will have on the Company's financial position or results of operations.

On May 28, 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)," which affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards. The guidance supersedes the revenue recognition guidance in Topic 605, "Revenue Recognition", and most industry-specific guidance throughout the Industry Topics of the Codification. The guidance also supersedes some cost guidance included in Subtopic 605-35, "Revenue Recognition- Contract-Type and Production-Type Contracts". On April 1, 2015, the FASB voted to propose to defer the effective date of the pronouncement by one year. ASU 2014-9, as



amended, is effective for annual periods, and interim periods within those years, beginning after December 15, 2016, or December 31, 2017, if deferred. An entity is required to apply the amendments using one of the following two methods: i) retrospectively to each prior period presented with three possible expedients: a) for completed contracts that begin and end in the same reporting period no restatement is required, b) for completed contract with variable consideration an entity may use the transaction price at completion rather than restating estimated variable consideration amounts in comparable reporting periods and c) for comparable reporting periods before date of initial application reduced disclosure requirements related to transaction price; ii) retrospectively with the cumulative effect of initially applying the amendment recognized at the date of initial application with additional disclosures for the differences of the prior guidance to the reporting periods compared to the new guidance and an explanation of the reasons for significant changes. We are required to adopt ASU 2014-09 in the first quarter of fiscal 2018, or in the first quarter of fiscal 2019, if deferred, and we are currently assessing the impact of this pronouncement on our financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which requires management to assess, at each annual and interim reporting period, the entity's ability to continue as a going concern within one year after the date that the financial statements are issued and provide related disclosures. The ASU is effective for the year ended March 31, 2017, with early adoption permitted. The Company has assessed the impact of this standard and does not believe that it will have a material impact on the Company's financial statements or disclosures.

There are currently no other accounting standards that have been issued but not yet adopted by the Company that will have a significant impact on the Company's financial position, results of operations or cash flows upon adoption.

## NOTE 2 INTANGIBLE ASSETS

The assigned values of all patents considered in service by the Company are being amortized on a straight-line basis over the remaining effective lives of the patents.

Intangible assets, such as acquired in-process research and development costs, are considered to have an indefinite useful life until such time as they are put into service at which time they will be amortized on a straight-line basis over the shorter of their economic or legal useful life.

Intangible assets consist of the following:

	Life	March 31, 2015	March 31, 2014
Patents, gross	6.75 19.46	\$ 8,135,063	\$ 8,135,063
In-process research and development	Indefinite	1,832,370	2,250,435
		9,967,433	10,385,498
Accumulated amortization		(1,919,485)	(1,144,858)
Net intangible assets		\$ 8,047,948	\$ 9,240,640

During the fiscal year ended March 31, 2015, management evaluated assets included in IPRD and determined that certain projects will no longer be pursued for further development resulting in an impairment charge of \$418,065.

Total amortization expense during the years ended March 31, 2015 and 2014 was \$774,627 and \$775,011, respectively.

Total annual amortization expense of finite lived intangible assets is estimated to be as follows:

Fiscal Year Ending	
March 31, 2016	\$ 774,840
March 31, 2017	774,840
March 31, 2018	774,840
March 31, 2019	774,840
March 31, 2020	595,159
Thereafter	\$ 2,521,059

## NOTE 3 NOTES PAYABLE

On October 16, 2014, the Company entered into a Second Amendment to Loan Agreement ("Amendment No. 2") with Platinum Capital Partners, LP ("Platinum") to its existing loan agreement dated as of June 21, 2013 with

Platinum, as modified by the First Amendment to Loan Agreement dated as of October 11, 2013. Under the terms of Amendment No. 2, Platinum, among other things, consolidated the Company's credit facilities into one \$1,500,000 note and deferred \$63,619 of interest that was due and payable on September 30, 2014 under the Loan Agreement until December 19, 2014. The Company also executed two new promissory notes concurrently with Amendment No. 2: (i) a Revolving Promissory Note dated as of October 17, 2014 in the principal amount of \$1,500,000 in favor of Platinum (the "New Revolving Promissory Note"), which replaced the Company's Promissory Note dated as of June 21, 2013, in the principal amount of \$1,000,000 in favor of Platinum, and the Company's Promissory Note dated as of October 11, 2013, in the principal amount of \$500,000 in favor of Platinum; and (ii) a Deferred Interest Promissory Note dated as of September 30, 2014, in the principal amount of \$63,619 in favor of Platinum (the "Deferred Interest Promissory Note"). The New Revolving Promissory Note had a maturity date of June 30, 2015 and interest on the outstanding principal accrued at a rate of 18% per annum, compounded annually. The Deferred Interest Promissory Note had a maturity date of December 19, 2014 and interest on the outstanding principal accrued at a rate of 18% per annum, compounded annually. The loan agreement contained a number of restrictions on the Company's business, including restrictions on its ability to merge, sell assets, create or incur liens on assets, make distributions to its shareholders and sell, purchase or lease real or personal property or other assets or equipment. The loan agreement also contains affirmative covenants and events of default.

On December 16, 2014 the Company entered into a Loan Agreement (the “HGI Loan Agreement”) and a Security Agreement (the “HGI Security Agreement”) with Heritage Gemstone Investors, LLC (“HGI”) providing for a \$2,000,000 secured non-revolving line of credit (the “HGI Loan”). The HGI Loan, which is represented by a Promissory Note dated as of December 15, 2014 (the “HGI Note”), matures on December 15, 2017. Borrowings accrue interest at the rate of 7.25% per annum and the Company intends to make monthly interest payments. On December 18, 2014, \$2,000,000 was drawn on the HGI Loan. The Company utilized funds drawn on the HGI Loan to repay its existing indebtedness to Platinum and to continue to fund its ongoing operations. The HGI Loan Agreement contains a number of restrictions on the Company’s business, including restrictions on its ability to merge, sell assets, create or incur liens on assets, make distributions to its stockholders and sell, purchase or lease real or personal property or other assets or equipment. The HGI Loan Agreement contains standard provisions relating to a default and acceleration of the Company’s payment obligations thereunder upon the occurrence of an event of default, which includes, among other things, the failure to pay principal, interest, fees or other amounts payable under the agreement when due; failure to comply with specified agreements, covenants or obligations; cross-default with other indebtedness; the making of any material false representation or warranty; commencement of bankruptcy or other insolvency proceedings by or against the Company; and failure by the Company to maintain a book net worth of at least \$4.0 million at all times. The Company’s obligations under the HGI Loan Agreement are not guaranteed by any other party. The Company may prepay borrowings without premium or penalty upon notice to HGI as provided in the HGI Loan Agreement. The HGI Loan Agreement requires the Company to enter into the HGI Security Agreement. Under the HGI Security Agreement, the Company grants HGI a first priority security interest in the Company’s inventory, equipment, accounts and other rights to payments and intangibles as security for the HGI Loan.

Also on December 16, 2014, the Company entered into an agreement for the Sale and Lease of Growers (the “Grower Sale-Lease Agreement”) with HGI to allow for the expansion of current growers and the purchase of new growers. Pursuant to the Grower Sale-Lease Agreement, the Company agreed to a sale-leaseback arrangement for certain diamond growers produced by the Company during the term of the Grower Sale-Leaseback Agreement by which the Company will sell diamond growers to HGI and then lease the growers back from HGI. The term of the Grower Sale-Leaseback Agreement is ten years. For the new and upgraded growers, the direct profit margin generated from the growers will be split between the Company and HGI in accordance with the Grower Sale-Lease Agreement. The Grower Sale-Lease Agreement requires the Company to operate and service the growers, and requires HGI to up-fit certain existing growers and to make capital improvements to the new growers under certain circumstances. At the end of the Grower Sale-Leaseback Agreement the Company takes ownership of the leased equipment. The Company will also have the right to repurchase the leased growers upon the occurrence of certain events prior to the expiration of the Grower Sale-Leaseback Agreement.

As of March 31, 2015, HGI has advanced the Company \$300,000 to fund improvements to our current growers that will expand manufacturing capacity in our production facility. In addition, HGI has advanced the Company \$200,000 for the purchase of new grower equipment under the Sale-Leaseback Agreement. As of March 31, 2015, the Company considers both of these advances totaling \$500,000 as notes payable. The Company anticipates completing the grower expansion and new equipment purchases during the first half of the fiscal year ending March 31, 2016.

#### NOTE 4 CAPITAL STOCK

The authorized capital of the Company is 75,000,000 common shares with a par value of \$ 0.001 per share.

At the request of the then Board of Directors, the Company entered into an agreement, effective April 12, 2014, with Mr. Joseph Cunningham to provide consulting services to the Company. Under this agreement, the Company agreed to provide Mr. Cunningham \$4,000 and 20,000 shares of common stock per month in exchange for his professional services to the Company. This contract expired in August 2014. During the fiscal year ended March 31, 2015, the Company issued 80,000 shares to Mr. Cunningham. These shares were valued at an average of \$0.43 per share based

on the closing prices of the shares on the dates of grant and the Company recognized \$34,200 in professional and consulting fee expense for these shares during the fiscal year ended March 31, 2015.

On June 20, 2014, the then Board of Directors granted restricted stock grants to Mr. Michael Laub of 50,000 shares for previously performed services rendered to the Company. The Company did not recognize expense for this restricted stock grant since it was in exchange for expenses previously accrued by the Company.

On June 23, 2014, the Company, members of its Board of Directors and various plaintiffs (See NOTE 12 LITIGATION) reached a settlement agreement that resulted in the return and cancellation of 1,000,000 share of common stock to the Company.

On July 15, 2014, the Board of Directors approved the issuance and sale of up to 2,000,000 shares of common stock to accredited investors at a price of \$0.30 per share. On September 25, 2014, the Board agreed to increase the size of the offering up to 6,666,667 shares to raise up to \$2,000,000. The Company completed the offering on December 23, 2014 and issued 6,666,664 shares of common stock, at a price of \$0.30 per share, for total cash proceeds of \$2,000,000.

On October 30, 2014, the Board of Directors approved the issuance of 50,000 shares to Bradley Robb to settle \$15,000 of liabilities for services rendered to the Company. Also on this date, the Board approved the issuance of 95,522 shares of stock to an affiliate of our landlord to settle \$28,658 of outstanding rent liabilities. The shares issued in each of these transactions were valued at \$0.30 per share.

On March 12, 2015, the Board of Directors approved the issuance of 333,333 shares to an affiliate of Renaissance Diamond, Inc. to settle \$100,000 of liabilities for diamond seed inventory purchased by the Company. The shares issued in this transaction were valued at \$0.30 per share, which was the market price of our stock when the inventory was purchased.

In addition, on March 12, 2015, the Board of Directors approved the retirement of all 1,000,000 shares held in treasury by the Company.

The Company had 56,531,499 shares of common stock issued and outstanding as of March 31, 2015.

The Company had 5,566,795 warrants outstanding with a weighted average exercise price of \$1.53 per share as of March 31, 2015. No warrants were issued or exercised during the fiscal year ended March 31, 2015. 4,891,250 warrants with an exercise price of \$1.60 will expire if not exercised during our next fiscal year ending March 31, 2016.

#### NOTE 5 SHARE-BASED COMPENSATION

The Company currently has one equity-based compensation plan under which stock-based compensation awards can be granted to directors, officers, employees and consultants providing bona fide services to or for the Company. The Company's 2012 Share Incentive Plan was adopted on May 7, 2012 (the "2012 Share Incentive Plan" or "Plan") and allows the Company to issue up to 5,000,000 shares of its common stock pursuant to awards granted under the 2012 Share Incentive Plan. The Plan permits the granting of stock options, stock appreciation rights, restricted or unrestricted stock awards, phantom stock, performance awards, other stock-based awards, or any combination of the foregoing. The only awards that have been issued under the Plan are stock options. Because the Plan has not been approved by our shareholders, all such stock option awards are non-qualified stock options.

On September 25, 2014, the Company entered into a severance agreement with our former Chief Executive Officer, Mr. Michael McMahon, whereby the Company granted him 416,667 shares of fully vested restricted common stock valued at \$0.30 per share for a total value of \$125,000. In addition, the Company agreed to provide Mr. McMahon 100,000 shares of restricted stock as compensation for the vested options that expired due to his termination. The Company valued these shares at \$0.30 per share and recognized \$30,000 in stock based compensation expense during the fiscal year ended March 31, 2015. In total the Company recognized \$305,077 in severance expense in our salaries and benefit expenses during the year ended March 31, 2015.

The following sets forth the options to purchase shares of the Company's stock issued and outstanding as of March 31, 2015:

Weighted-	Weighted-Average
-----------	------------------

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

Options	Shares	Average Exercise Price	Remaining Contractual Term
Options Outstanding April 1, 2013	4,092,500	\$ 0.87	2.29
Granted	706,250	0.36	
Exercised			
Expired/Cancelled	(456,250)	0.73	
Options Outstanding March 31, 2014	4,342,500	\$ 0.77	1.75
Granted			
Exercised			
Expired/cancelled	(4,110,000)	0.79	
Options Outstanding March 31, 2015	232,500	\$ 0.35	1.45
Exercisable at March 31, 2015	23,125	\$ 0.44	1.20

The intrinsic value of options outstanding and exercisable at March 31, 2015 and 2014 was \$17,071 and \$0, respectively.

The Company did not issue any options during the fiscal year ended March 31, 2015.

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

A summary of the status of non-vested shares as of March 31, 2015 and changes during the year ended March 31, 2015 is presented below.

Non-vested Shares	Shares	Weighted Average Grant-Date Fair Value
Non-vested at April 1, 2013	2,466,167	\$ 0.65
Granted	706,250	0.22
Vested	(575,625)	0.45
Expired/cancelled: non-vested	(182,000)	0.38
Non-vested at March 31, 2014		