

PRECISION OPTICS CORPORATION, INC.
Form 10-Q
November 14, 2017

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2017

or

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

For the transition period from _____ to _____

Commission File Number: 001-10647

PRECISION OPTICS CORPORATION, INC.

(Exact name of registrant as specified in its charter)

Massachusetts

04-2795294

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

22 East Broadway, Gardner, Massachusetts 01440-3338

(Address of principal executive offices) (Zip Code)

(978) 630-1800

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The number of shares outstanding of the issuer's common stock, par value \$0.01 per share, at October 31, 2017 was 10,095,139 shares.

PRECISION OPTICS CORPORATION, INC.

Table of Contents

	Page
<u>PART I — FINANCIAL INFORMATION</u>	3
<u>Item 1. Financial Statements</u>	3
<u>Consolidated Balance Sheets</u>	3
<u>Consolidated Statements of Operations for the Three Months Ended September 30, 2017 and 2016</u>	4
<u>Consolidated Statements of Cash Flows for the Three Months Ended September 30, 2017 and 2016</u>	5
<u>Notes to Consolidated Financial Statements</u>	6
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	9
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	12
<u>Item 4. Controls and Procedures</u>	12
<u>PART II — OTHER INFORMATION</u>	14
<u>Item 1. Legal Proceedings</u>	14
<u>Item 1A. Risk Factors</u>	14
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	14
<u>Item 3. Defaults Upon Senior Securities</u>	14
<u>Item 4. Mine Safety Disclosures (Not applicable.)</u>	14
<u>Item 5. Other Information</u>	14
<u>Item 6. Exhibits</u>	15

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements.****PRECISION OPTICS CORPORATION, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****(UNAUDITED)**

	September 30, 2017	June 30, 2017
ASSETS		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 194,714	\$ 118,405
Accounts Receivable, net	613,961	468,548
Inventories, net	967,285	1,055,447
Prepaid Expenses	51,394	55,985
Total Current Assets	1,827,354	1,698,385
PROPERTY AND EQUIPMENT		
Machinery and Equipment	2,507,190	2,507,190
Leasehold Improvements	553,596	553,596
Furniture and Fixtures	148,303	148,303
	3,209,089	3,209,089
Less: Accumulated Depreciation and Amortization	(3,145,585)	(3,136,835)
Net Fixed Assets	63,504	72,254
Patents, net	30,086	30,086
TOTAL ASSETS	\$ 1,920,944	\$ 1,800,725
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current Portion of Capital Lease Obligation	\$ 8,531	\$ 8,391
Accounts Payable	663,302	694,958
Customer Advances	122,495	180,137
Accrued Employee Compensation	144,873	189,783
Accrued Professional Services	91,500	71,000
Accrued Warranty Expense	25,000	25,000

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Other Accrued Liabilities	41,175	49,512
Total Current Liabilities	1,096,876	1,218,781
Capital Lease Obligation, net of current portion	21,378	23,564
STOCKHOLDERS' EQUITY		
Common Stock, \$0.01 par value - Authorized - 50,000,000 shares; Issued and Outstanding – 9,428,472 shares at September 30, 2017 and 8,872,916 shares at June 30, 2017	94,285	88,729
Additional Paid-in Capital	45,407,922	45,140,383
Accumulated Deficit	(44,699,517)	(44,670,732)
Total Stockholders' Equity	802,690	558,380
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 1,920,944	\$ 1,800,725

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

PRECISION OPTICS CORPORATION, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF OPERATIONS****FOR THE THREE MONTHS ENDED****SEPTEMBER 30, 2017 AND 2016****(UNAUDITED)**

	Three Months Ended September 30,	
	2017	2016
Revenues	\$1,028,746	\$849,548
Cost of Goods Sold	642,004	682,497
Gross Profit	386,742	167,051
Research and Development Expenses, net	118,427	116,992
Selling, General and Administrative Expenses	296,584	343,782
Gain on Sale of Assets	–	(315)
Total Operating Expenses	415,011	460,459
Operating Loss	(28,269)	(293,408)
Interest Expense	(516)	–
Net Loss	\$(28,785)	\$(293,408)
Loss Per Share:		
Basic	\$(0.00)	\$(0.04)
Diluted	\$(0.00)	\$(0.04)
Weighted Average Common Shares Outstanding:		
Basic	9,108,423	7,539,582
Diluted	9,108,423	7,539,582

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

PRECISION OPTICS CORPORATION, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF CASH FLOWS****FOR THE THREE MONTHS ENDED****SEPTEMBER 30, 2017 AND 2016****(UNAUDITED)**

	Three Months Ended September 30,	
	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Loss	\$(28,785)	\$(293,408)
Adjustments to Reconcile Net Loss to Net Cash Provided From (Used In) Operating Activities -		
Depreciation and Amortization	8,750	7,621
Gain on Sale of Assets	-	(315)
Stock-based Compensation Expense	26,057	60,901
Non-cash Consulting Expense	(7,425)	8,550
Changes in Operating Assets and Liabilities -		
Accounts Receivable, net	(145,413)	184,327
Inventories, net	88,162	140,979
Prepaid Expenses	4,591	6,297
Accounts Payable	5,381	60,085
Customer Advances	(57,642)	11,025
Accrued Liabilities	(25,322)	(28,274)
Net Cash Provided From (Used In) Operating Activities	(131,646)	157,788
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additional Patent Costs	-	(340)
Purchases of Property and Equipment	-	(3,500)
Proceeds from Sale of Assets	-	315
Net Cash Used In Investing Activities	-	(3,525)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payment of Capital Lease Obligation	(2,046)	(1,916)
Gross Proceeds from Private Placement of Common Stock	210,001	-
Net Cash Provided From (Used In) Financing Activities	207,955	(1,916)
NET INCREASE IN CASH AND CASH EQUIVALENTS	76,309	152,347
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	118,405	50,059
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$194,714	\$202,406

SUPPLEMENTAL DISCLOSURE OF NON-CASH FINANCING AND INVESTING
ACTIVITIES:

Issuance of Common Stock in Settlement of Accounts Payable	\$40,000	\$-
Offering Costs Included in Accounts Payable	\$2,963	\$-

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

PRECISION OPTICS CORPORATION, INC.

NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Operations

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

These consolidated financial statements have been prepared by the Company, without audit, and reflect normal recurring adjustments which, in the opinion of management, are necessary for a fair statement of the results of the first quarter of the Company's fiscal year 2018. These consolidated financial statements do not include all disclosures associated with annual consolidated financial statements and, accordingly, should be read in conjunction with footnotes contained in the Company's consolidated financial statements for the year ended June 30, 2017, together with the Report of Independent Registered Public Accounting Firm filed under cover of the Company's 2017 Annual Report on Form 10-K, filed with the Securities and Exchange Commission on September 28, 2017.

Use of Estimates

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

Income (Loss) Per Share

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Basic income (loss) per share is computed by dividing net income or net loss by the weighted average number of shares of common stock outstanding during the period. Diluted income (loss) per share is computed by dividing net income or net loss by the weighted average number of shares of common stock outstanding during the period, plus the number of potentially dilutive securities outstanding during the period such as stock options and warrants. For the three months ended September 30, 2017 and 2016, the effect of such securities was antidilutive and not included in the diluted calculation because of the net loss generated in these periods.

The following is the calculation of loss per share for the three months ended September 30, 2017 and 2016:

	Three Months Ended September 30,	
	2017	2016
Net Income (Loss) – Basic and Diluted	\$(28,785)	\$(293,408)
Basic and Diluted Weighted Average Shares Outstanding	9,108,423	7,539,582
Loss Per Share		
Basic	\$(0.00)	\$(0.04)
Diluted	\$(0.00)	\$(0.04)

The number of shares issuable upon the exercise of outstanding stock options and warrants that were excluded from the computation as their effect was antidilutive was approximately 1,745,067 and 4,169,000 for the three months ended September 30, 2017 and 2016, respectively.

Income Taxes

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

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

2. INVENTORIES

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

	September 30, 2017	June 30, 2017
Raw Materials	\$412,847	\$501,346
Work-In-Progress	356,278	388,614
Finished Goods	198,160	165,487
Total Inventories	\$967,285	\$1,055,447

3. CAPITAL LEASE OBLIGATION

The Company entered into a five-year capital lease obligation in January 2016 for the acquisition of manufacturing equipment totaling \$51,252. At September 30, 2017, future minimum lease payments under the capital lease obligation are as follows:

Fiscal Year Ending June 30:	Amount
2018	\$7,688
2019	10,250
2020	10,250
2021	5,126
Total minimum payments	33,314
Less: amount representing interest	3,405
Present value of minimum lease payments	29,909
Less: current portion	8,531
	\$21,378

4. STOCK-BASED COMPENSATION

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Stock-based compensation costs recognized during the three months ended September 30, 2017 and 2016 amounted to \$26,057 and \$60,901 respectively, and the costs were included in the accompanying consolidated statements of operations in: selling, general and administrative expenses (2017 - \$10,696; 2016 - \$42,915), research and development expenses (2017 - \$6,692, 2016 - \$9,317) and cost of goods sold (2017 - \$8,669; 2016 - \$8,669). No compensation has been capitalized because such amounts would have been immaterial.

The following tables summarize stock option activity for the three months ended September 30, 2017:

	Options Outstanding		Weighted Average
	Number of	Weighted Average	Contractual Life
	Shares	Exercise Price	
Outstanding at June 30, 2017	1,078,400	\$0.78	7.01 years
Granted	—		
Expired or Cancelled	—		
Outstanding at September 30, 2017	1,078,400	\$0.78	6.76 years

Information related to the stock options outstanding as of September 30, 2017 is as follows:

Range of Exercise Prices	Number of Shares	Weighted-Average Remaining Contractual Life (years)	Weighted-Average Exercise Price	Exercisable Number of Shares	Exercisable Weighted-Average Exercise Price
\$0.27	40,000	3.79	\$ 0.27	40,000	\$ 0.27
\$0.40	15,000	9.58	\$ 0.40	5,000	\$ 0.40
\$0.48	60,000	8.50	\$ 0.48	40,000	\$ 0.48
\$0.50	80,000	8.73	\$ 0.50	45,000	\$ 0.50
\$0.50	20,000	3.72	\$ 0.50	20,000	\$ 0.50
\$0.55	29,500	4.36	\$ 0.55	29,500	\$ 0.55
\$0.73	539,500	7.63	\$ 0.73	479,500	\$ 0.73
\$0.85	9,000	5.26	\$ 0.85	9,000	\$ 0.85
\$0.90	9,000	6.26	\$ 0.90	9,000	\$ 0.90
\$0.95	65,000	6.78	\$ 0.95	65,000	\$ 0.95
\$1.20	207,800	4.42	\$ 1.20	207,800	\$ 1.20
\$1.25	1,200	1.15	\$ 1.25	1,200	\$ 1.25
\$1.35	1,200	2.15	\$ 1.35	1,200	\$ 1.35
\$7.75	1,200	0.16	\$ 7.75	1,200	\$ 7.75
\$0.27-\$7.75	1,078,400	6.76	\$ 0.78	953,400	\$ 0.81

The aggregate intrinsic value of the Company's "in-the-money" outstanding and exercisable options as of September 30, 2017 was \$7,950 and \$7,450, respectively.

5. WARRANTS

As of September 30, 2017, there were warrants outstanding for the issuance of an aggregate of 666,667 shares of common stock, \$0.01 par value at a purchase price of \$0.01 per share. The warrants were exercisable beginning on October 2, 2017 and expired on October 16, 2017. All warrants for 666,667 shares were exercised before October 16, 2017, by payment to the Company for the aggregate purchase price of \$6,667.

Warrants previously outstanding for the issuance of an aggregate of 2,994,893 shares of common stock, \$0.01 par value at an average exercise price of \$0.75 per share expired on September 28, 2017. None of these warrants were exercised before their expiration.

6. SALE OF STOCK

On August 22, 2017, the Company entered into agreements with accredited investors for the sale and purchase of 466,668 unregistered shares of its common stock, \$0.01 par value at a purchase price of \$0.45 per share. The Company received \$210,001 in gross proceeds from the offering. The Company is using the net proceeds from this placement for general working capital purposes.

Concurrently with the placement, the Company entered into an agreement with an investor for the sale of 88,888 unregistered shares of its common stock for services provided to the Company at a price of \$0.45 per share.

In connection with the placement, the Company also entered into a registration rights agreement with the investors, whereby the Company is obligated to file a registration statement with the Securities Exchange Commission on or before 90 calendar days after August 22, 2017 to register the resale by the investors of 555,556 shares of our common stock purchased in the placement.

7. SALE OF ASSETS

During the three months ended September 30, 2016, the Company sold equipment that was previously written off for proceeds totaling \$315 and recorded gains of \$315, which is included within operating expenses in the accompanying consolidated statements of operations.

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

The following discussion of our financial condition and results of operations should be read in conjunction with the unaudited condensed consolidated financial statements and notes to those statements included elsewhere in this Quarterly Report on Form 10-Q for the quarter ended September 30, 2017 and with our audited consolidated financial statements for the year ended June 30, 2017 included in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission on September 28, 2017.

This Quarterly Report on Form 10-Q contains forward-looking statements. When used in this report, the words "anticipate," "suggest," "estimate," "plan," "project," "continue," "ongoing," "potential," "expect," "predict," "believe," "intend," "may," "will," "should," "could," "would" and similar expressions are intended to identify forward-looking statements. You should not place undue reliance on these forward-looking statements. Our actual results could differ materially from those anticipated in the forward-looking statements for many reasons, including the risks described in this report, the risks described in our Annual Report on Form 10-K for the year ended June 30, 2017 and other reports we file with the Securities and Exchange Commission. Although we believe the expectations reflected in the forward-looking statements are reasonable, they relate only to events as of the date on which the statements are made. We do not intend to update any of the forward-looking statements after the date of this report to conform these statements to actual results or to changes in our expectations, except as required by law.

Overview

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

Our unique proprietary technology in the areas of micro optical lenses and prisms, micro medical fiber and CMOS based cameras, and custom design of medical grade instruments, combined with recent developments in the areas of 3D displays, has allowed us to begin commercialization of related product and service offerings to a widening group of customers addressing various medical device, defense and aerospace applications. Thus, a portion of our revenues are now derived from engineering and design services we performed for our customers to incorporate our technologies and capabilities into their medical device products. We believe that new products based on these technologies provide

enhanced imaging for existing surgical procedures and can enable development of many new medical device products and related medical procedures.

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

The markets in which we do business are highly competitive and include both foreign and domestic competitors. Many of our competitors are larger and have substantially greater resources than we do. Furthermore, other domestic or foreign companies, some with greater financial resources than we have, may seek to produce products or services that compete with ours. We routinely outsource specialized production efforts as required to obtain the most cost effective production.

We believe that competition for sales of our medical products and services, which have been principally sold to original equipment manufacturers, or OEM, customers, is based on our ability to design and produce technical features, performance, engineering service and production scheduling, on-time delivery, quality control and product reliability, and competitive pricing.

We believe that our future success depends to a large degree on our ability to develop new optical products and services to enhance the performance characteristics and methods of manufacture of existing products. Accordingly, we expect to continue to seek and obtain product-related design and development contracts with customers and to selectively invest our own funds on research and development, particularly in the areas of Microprecision™ optics, micro medical cameras and 3D endoscopes.

For the quarter ended September 30, 2017, approximately 81% of our sales were made to seven customers. Of these, four are medium to large, international, medical device companies and one is a large defense contractor. Each of these customers has been our customers for numerous years. The other two customers are early-stage companies developing endoscopic products that incorporate our unique design capabilities. Sales to these seven customers include both products we developed over five years ago and products we are currently developing which rely heavily on our unique, proprietary Microprecision™ lens technology and optical visualization system expertise.

Current sales and marketing activities are intended to broaden awareness of the benefits of our new technology platforms, which we believe are ready for general application to medical device projects requiring surgery-grade visualization from sub-millimeter sized devices and 3D endoscopy. We market directly to established medical device companies primarily in the United States that we believe could benefit from our advanced endoscopy visualization systems. Through this direct marketing, referrals, attendance at trade shows including Medical Design and Manufacturing West and MD&M East, and periodically a presence in online professional association websites, we have expanded our on-going pipeline of projects to significant medical device companies as well as well-funded emerging technology companies. We expect our customer pipeline to continue to expand as development projects transition to production orders and new customer projects enter the development phase.

General

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

There have been no significant changes in our critical accounting policies as disclosed in the Notes to our Financial Statements contained in our Annual Report on Form 10-K for the year ended June 30, 2017 filed with the Securities and Exchange Commission on September 28, 2017.

Results of Operations

Our total revenues for the quarter ended September 30, 2017, were \$1,028,746, as compared to \$849,548 for the same period in the prior year, an increase of \$179,198, or 21.1%. Revenues increased during the quarter ended September 30, 2017 compared to the same quarter of the prior year in the engineering services and production categories by 22% and 20%, respectively. The majority of our revenues are derived from engineering design and manufacturing services related to products marketed or under development by our OEM customers. Therefore, our revenues are subject to fluctuations on a product by product basis from period to period. Production revenue during the quarter ended September 30, 2017 when compared to the same quarter of the prior year included a reduction in sales of a traditional product, offset by a larger increase in sales of optical components to a defense contractor customer. Engineering service revenue during the quarter ended September 30, 2017 when compared to the same quarter of the prior year included a large reduction of sales to one customer, which was offset by a larger increase in engineering and design revenues from numerous customers developing new products. We believe each of these engineering design projects have the potential to generate production revenues when our customers achieve commercialization of the products currently under design.

Gross profit for the quarter ended September 30, 2017 was \$386,742, compared to \$167,051 for the same period in the prior year, reflecting an increase of \$219,691, or 131.5%. Gross profit for the quarter ended September 30, 2017 as a percentage of our revenues was 37.6%, an increase from the gross profit percentage of 19.7% for the same period in the prior year. Quarterly gross profit and gross profit percentage depend on a number of factors, including overall sales volume, facility utilization, product sales mix, and the costs of engineering services and initial production in connection with new products. The improvement in our gross profit performance during the quarter ended September 30, 2017 resulted from increased revenues absorbing a higher percentage of fixed manufacturing costs, stable gross margins throughout all production projects during the quarter ended September 30, 2017, and targeted or better margins on seven different engineering projects which accounted for 81% of engineering revenue during the same quarter.

Research and development expenses were \$118,427 for the quarter ended September 30, 2017, compared to \$116,992 for the same period in the prior year, an increase of \$1,435, or 1.2%. The vast majority of our engineering, research and development activities are consumed in revenue generating engagements with our customers for the development of their products. In-house research and development and certain internal functions not directly related to customer engagements are classified as research and development expenses.

Selling, general and administrative expenses were \$296,584 for the quarter ended September 30, 2017, compared to \$343,782 for the same period in the prior year, a decrease of \$47,198, or 13.7%. The decrease in the quarter ended September 30, 2017, compared to the same periods in the prior year was primarily due to reduced stock based compensation expense of \$50,819 relating to stock options and stock accrued for consulting services, plus reduced wages resulting from the retirement of a sales person in January 2017. The expense reductions were partially offset by a \$25,000 increase in the reserve for doubtful accounts receivable relating to one specific customer.

No income tax provision was recorded in the quarters ended September 30, 2017 and 2016 because of the losses generated in those periods.

Liquidity and Capital Resources

We have sustained recurring net losses for several years. During the quarters ended September 30, 2017 and 2016, we incurred net losses of \$28,785 and \$293,408, respectively. We also incurred net losses of \$1,006,457 and \$1,034,765 during the fiscal years ended June 30, 2017 and 2016, respectively, and used cash in operating activities of \$667,434 and \$876,298 during the same fiscal periods, respectively. As of September 30, 2017, cash and cash equivalents were \$194,714, accounts receivable were \$613,961, and current liabilities were \$1,096,876. Our working capital consisted of \$730,478 and \$479,604 at September 30, 2017 and June 30, 2017, respectively.

We have traditionally funded working capital needs through product sales, management of working capital components of our business, and by cash received from public and private offerings of our common stock, warrants to purchase shares of our common stock or convertible notes. We have incurred quarter to quarter operating losses during our efforts to develop current products including Microprecision™ optical elements, micro medical camera assemblies and 3D endoscopes. Our management believes that the opportunities represented by these products have the potential to generate sales increases to achieve breakeven and profitable results. However, our current financial condition may raise doubt regarding our ability to continue as a going concern, as referenced by the Report of our Independent Registered Public Accounting Firm on our financial statements for the year ended June 30, 2017, included in our Annual Report on Form 10-K.

We recognize that the working capital described above and our cash and accounts receivable as of September 30, 2017 is low considering the level of cash historically used in our operations at our current sales levels. Our accounts receivable and cash balances are subject to significant fluctuations based on the timing and amount of customer billings and accounts receivable collections as well as the terms of vendor payment obligations. If we are unable to increase quarterly sales revenues to near cash breakeven in the next six to nine months, we may be required to obtain cash for operations from non-working capital sources, which may not be available, in which case we would have to significantly decrease or cease operations.

The sale of additional equity or convertible debt securities would result in additional dilution to our current stockholders, and debt financing, if available, may involve restrictive covenants that could restrict our operations or finances. Financing may not be available in amounts or on terms acceptable to us, if at all. If we are unable to secure additional capital, we may be required to curtail our research and development initiatives and take additional measures to reduce costs in order to conserve our cash in amounts sufficient to sustain operations and meet our obligations.

Capital equipment expenditures during the quarters ended September 30, 2017 and 2016 were \$0 and \$3,500, respectively. Future capital equipment expenditures will be dependent upon future sales and success of on-going research and development efforts.

We have contractual cash commitments related to open purchase orders as of September 30, 2017 of approximately \$235,000, including a \$29,909 commitment remaining under a five-year capital lease obligation for the acquisition of equipment (see Note 3. Capital Lease Obligation). We have no other contractual cash commitments since leased facilities are currently on a month-to-month basis.

Off-Balance Sheet Arrangements

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

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

Item 4. Controls and Procedures.

Management's Evaluation of Disclosure Controls and Procedures

Our Chief Executive Officer and our Chief Financial Officer evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer have concluded that our disclosure controls and procedures, including internal control over financial reporting, were not effective, as of September 30, 2017, to ensure the information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934, as amended (i) is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (ii) is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Our disclosure controls and procedures are intended to be designed to provide reasonable assurance that such information is accumulated and communicated to our management. Based on this evaluation, our management concluded that our internal control over financial reporting was not effective as of September 30, 2017.

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

Segregation of Duties: As previously disclosed in our Annual Reports on Form 10-K for the fiscal years ended June 30, 2008-2017, our management identified a control deficiency during the 2008 fiscal year because we lacked sufficient staff to segregate accounting duties. We believe the control deficiency resulted primarily because we have the equivalent of one and one-half persons performing all accounting-related on-site duties. As a result, we did not maintain adequate segregation of duties within our critical financial reporting applications, the related modules and financial reporting processes. This control deficiency could result in a misstatement of balance sheet and income statement accounts in our interim or annual consolidated financial statements that would not be detected. Accordingly, management has determined that this control deficiency constitutes a material weakness. During the period beginning with fiscal year 2008 through June 30, 2017, no audit adjustments resulting from this condition were required.

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

We believe that the step outlined above strengthens our internal control over financial reporting and mitigates the material weakness described above. As part of our assessment of internal control over financial reporting for the fiscal year ended June 30, 2017, our management has evaluated this additional control and has determined that it is operating effectively.

Inventory Valuation: As previously disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2017, we reported a material weakness with respect to the valuation of our inventories. Specifically, the amounts used to value our inventory at June 30, 2009 with respect to overhead rates and purchased items were often inconsistent with the supporting documentation, due to year-to-year changes in overhead rates and costs of purchased items that were not properly reflected in inventory valuation. Accordingly, management had determined that this control deficiency constituted a material weakness as of June 30, 2009. Audit adjustments of approximately \$58,000 and \$41,000 to our audited financial statements as of June 30, 2011 and June 30, 2017, respectively, were necessary as a result of this condition.

Changes in Internal Control over Financial Reporting

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

To address and remediate the material weakness in internal control over financial reporting described above, beginning in the quarter ended September 30, 2009 and continuing through the quarter ended September 30, 2017, we implemented processes to improve our inventory controls and documentation surrounding inventory valuation for overhead rates, and performed procedures to ensure that the pricing of inventory items was consistent with the supporting documentation. We believe that the step outlined above strengthens our internal control over financial reporting and mitigates the material weakness described above.

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

PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

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

Item 1A. Risk Factors.

Other than as described below, there have been no material changes from the risk factors previously disclosed in our annual report on Form 10-K for the fiscal year ended June 30, 2017, as filed with the Securities and Exchange Commission on September 28, 2017.

As of September 30, 2017, we may not have sufficient cash to continue operations for the next six to nine months.

As of September 30, 2017, we had \$194,714 in cash and cash equivalents, \$613,961 in accounts receivable, and \$1,096,876 in current liabilities. We incurred net losses of 28,785 and \$1,006,457 during the quarter ended September 30, 2017 and the fiscal year ended June 30, 2017, respectively. If quarterly sales revenues do not increase to near cash breakeven in the next six to nine months, we may be required to obtain cash for operations from non-working capital sources, which may not be available, in which case we would have to significantly decrease or cease operations. We are currently evaluating several options to manage cash flow and raise capital if necessary, including issuing debt, equity or entering into a strategic alliance. The sale of additional equity or convertible debt securities would result in additional dilution to our stockholders, and debt financing, if available, may involve restrictive covenants that could restrict our operations or finances. Financing, if necessary, may not be available in amounts or on terms acceptable to us, if at all. If we cannot raise funds on acceptable terms or achieve positive cash flow, we may not be able to continue to conduct operations, develop new products, grow market share, take advantage of future opportunities or respond to competitive pressures or unanticipated requirements, any of which would negatively impact our business, operating results and financial condition.

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

Other than as previously disclosed, we did not issue any unregistered equity securities during the quarter ended September 30, 2017.

Item 3. Defaults Upon Senior Securities.

Not applicable.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

Item 6. Exhibits.

Exhibit Description

- 2.1 Asset Purchase Agreement between the Company and Optometrics Corporation, dated January 18, 2008 (included as Exhibit 2.1 to the Form 8-K filed January 25, 2008 and incorporated herein by reference).
- 3.1 Articles of Organization of Precision Optics Corporation, Inc., as amended (included as Exhibit 3.1 to the Form SB-2 filed March 16, 2007, and incorporated herein by reference).
- 3.2 Bylaws of Precision Optics Corporation, Inc. (included as Exhibit 3.2 to the Form S-1 filed December 18, 2008, and incorporated herein by reference).
- 3.3 Articles of Amendment to the Articles of Organization of Precision Optics Corporation, Inc., dated November 25, 2008 and effective December 11, 2008 (included as Exhibit 3.1 to the Form 8-K filed December 11, 2008, and incorporated herein by reference).
- 3.4 Amended and Restated Bylaws of Precision Optics Corporation, Inc. (included as Exhibit 3.1 to the Company's Current Report on Form 8-K filed July 11, 2014, and incorporated herein by reference).
- 4.1 Form of Warrant to Purchase Shares of Common Stock, dated September 28, 2012 (included as Exhibit 4.1 to the Form 8-K filed October 2, 2012, and incorporated herein by reference).
- 4.2 Registration Rights Agreement by and among the Company and each investor named therein, dated September 28, 2012 (included as Exhibit 4.2 to the Form 8-K filed October 2, 2012, and incorporated herein by reference).
- 4.3 Warrant to Purchase Shares of Common Stock issued to Loewen, Ondaatje, McCutcheon USA LTD, dated September 28, 2012 (included as Exhibit 4.3 to the Form 8-K filed October 2, 2012, and incorporated herein by reference).
- 4.4 Form of Warrant to Purchase Shares of Common Stock (Special Situations Settlement), dated February 12, 2013 (included as Exhibit 4.1 to the Form 8-K filed February 13, 2013, and incorporated herein by reference).
- 4.5 Registration Rights Agreement by and among the Company, Special Situations Fund III OP, L.P. and Special Situations Private Equity Fund, L.P., dated February 12, 2013 (included as Exhibit 4.2 to the Form 8-K filed February 13, 2013, and incorporated herein by reference).
- 4.6 Form of Warrant to Purchase Shares of Common Stock (Pitlor and Schumsky Settlement), dated February 12, 2013 (included as Exhibit 4.3 to the Form 8-K filed February 13, 2013, and incorporated herein by reference).
- 4.7 Form of Warrant, by and among Precision Optics Corporation, Inc. and several Investors, dated November 22, 2016 (included as Exhibit 10.3 to the Form 8-K filed November 29, 2016, and incorporated herein by reference).

reference).

- 10.1 Precision Optics Corporation, Inc. 2006 Equity Incentive Plan (included as Exhibit 99.1 to the Form 8-K filed December 4, 2006, and incorporated herein by reference).
- 10.2 Form of Incentive Stock Option Certificate (included as Exhibit 10.1 to the Form 10-QSB filed February 14, 2007, and incorporated herein by reference).
- 10.3 Form of Nonstatutory Stock Option Certificate (included as Exhibit 10.2 to the Form 10-QSB filed February 14, 2007, and incorporated herein by reference).
- 10.4 Compensation Agreement with Joseph N. Forkey, dated December 3, 2010 (included as Exhibit 10.12 to the Form 8-K filed December 6, 2010, and incorporated herein by reference).

15

- 10.5 Asset Purchase Agreement between the Company and Intuitive Surgical Operations, Inc., dated July 27, 2011 (included as Exhibit 10.1 to the Form 8-K filed August 3, 2011, and incorporated herein by reference).
- 10.6 Precision Optics Corporation, Inc. 2011 Equity Incentive Plan, dated October 13, 2011 (included as Exhibit 10.2 to Form S-8 filed October 14, 2011, and incorporated herein by reference.)
- 10.7 Precision Optics Corporation, Inc. 2011 Deferred Compensation Plan, dated October 13, 2011 (included as Exhibit 10.3 to Form S-8 filed October 14, 2011, and incorporated herein by reference.)
- 10.8 Side Letter Agreement to the Compensation Agreement with Joseph N. Forkey, dated October 14, 2011 (included as Exhibit 10.5 to the Form 8-K filed October 19, 2011, and incorporated herein by reference).
- 10.9 Endorsement to 10% Senior Secured Convertible Note by the Company, dated October 31, 2011, and accepted by Special Situations Private Equity Fund, L.P. (included as Exhibit 10.2 to the Form 8-K filed November 3, 2011, and incorporated herein by reference).
- 10.10 Endorsement to 10% Senior Secured Convertible Note by the Company, dated October 31, 2011, and accepted by Special Situations Fund III OP, L.P. (included as Exhibit 10.3 to the Form 8-K filed November 3, 2011, and incorporated herein by reference).
- 10.11 Endorsement to 10% Senior Secured Convertible Note by the Company, dated July 31, 2012, and accepted by Arnold Schumsky (included as Exhibit 10.27 to the Form 10-K filed October 15, 2012, and incorporated herein by reference.)
- 10.12 Endorsement to 10% Senior Secured Convertible Note by the Company, dated August 31, 2012, and accepted by Arnold Schumsky (included as Exhibit 10.28 to the Form 10-K filed October 15, 2012, and incorporated herein by reference.)
- 10.13 Notice of Repayment of 10% Senior Secured Convertible Note in Full by the Company, dated September 28, 2012, and accepted by Arnold Schumsky (included as Exhibit 10.29 to the Form 10-K filed October 15, 2012, and incorporated herein by reference.)
- 10.14 Purchase Agreement by and among the Company and each investor named therein, dated September 28, 2012 (included as Exhibit 10.1 to the Form 8-K filed October 2, 2012, and incorporated herein by reference).
- 10.15 Settlement Agreement by and among the Company, Special Situations Fund III OP, L.P. and Special Situations Private Equity Fund, L.P., dated February 12, 2013 (included as Exhibit 10.1 to the Form 8-K filed February 13, 2013, and incorporated herein by reference).
- 10.16 Settlement Agreement by and between the Company and Joel Pitlor, dated February 12, 2013 (included as Exhibit 10.2 to the Form 8-K filed February 13, 2013, and incorporated herein by reference).
- 10.17 Settlement Agreement by and between the Company and Arnold Schumsky, dated February 12, 2013 (included as Exhibit 10.3 to the Form 8-K filed February 13, 2013, and incorporated herein by reference).
- 10.18

Form of Purchase Agreement by and among the Company and Investor (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed July 7, 2014, and incorporated herein by reference).

- 10.19 Form of Registration Rights Agreement by and among the Company and Investor (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed July 7, 2014, and incorporated herein by reference).

- 10.20 Precision Optics Corporation, Inc. Amended 2011 Equity Incentive Plan, dated October 14, 2011, as amended on April 16, 2015 (included as Exhibit 10.1 to the Company's Registration Statement on Form S-8 filed April 20, 2015, and incorporated herein by reference).

- 10.21 Form of Purchase Agreement by and among the Company and Investor (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed October 23, 2015, and incorporated herein by reference).

- 10.22 Form of Registration Rights Agreement by and among the Company and Investors (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on October 23, 2015, and incorporated herein by reference).

- 10.23 Consulting Agreement with Donald A. Major dated June 15, 2016 (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on June 23, 2016, and incorporated herein by reference).
- 10.24 Form of Purchase Agreement, by and among Precision Optics Corporation, Inc. and several Investors, dated November 22, 2016 (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed November 29, 2016, and incorporated herein by reference).
- 10.25 Form of Registration Rights Agreement, by and among Precision Optics Corporation, Inc. and several Investors, dated November 22, 2016 (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on November 29, 2016, and incorporated herein by reference).
- 10.26 Form of Purchase Agreement, by and among Precision Optics Corporation, Inc. and several Investors, dated August 22, 2017 (included as Exhibit 10.1 to the Company's Current Report on Form 8-K filed on August 25, 2017, and incorporated herein by reference).
- 10.27 Form of Registration Rights Agreement, by and among Precision Optics Corporation, Inc. and several Investors, dated August 22, 2017 (included as Exhibit 10.2 to the Company's Current Report on Form 8-K filed on August 25, 2017, and incorporated herein by reference).
- 14.1 Precision Optics Corporation, Inc. Corporate Code of Ethics and Conduct (included as Exhibit 14.1 to the Form 10-K filed September 28, 2008, and incorporated herein by reference).
- 31.1* Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2* Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1* Certification of Officers pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS* XBRL Instance Document
- 101.SCH* XBRL Taxonomy Extension Schema Document
- 101.CAL* XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF* XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB* XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE* XBRL Taxonomy Extension Presentation Linkbase Document

*Filed herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PRECISION OPTICS CORPORATION, INC.

Date: November 14, 2017 By: /s/ Joseph N. Forkey
Joseph N. Forkey
Chief Executive Officer

(Principal Executive Officer)

Date: November 14, 2017 By: /s/ Donald A. Major
Donald A. Major
Chief Financial Officer

(Principal Financial Officer and Principal Accounting Officer)

