

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

NOCOPI TECHNOLOGIES INC/MD/
Form 10QSB
August 15, 2005

U.S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

Form 10-QSB

(Mark One)

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

For the quarterly period ended June 30, 2005.

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

For the transition period from _____ to _____

Commission file number 0-20333

NOCOPI TECHNOLOGIES, INC.

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

MARYLAND

87-0406496

(State or other jurisdiction of
incorporation or organization)

(IRS Employer Identification No.)

9C Portland Road, West Conshohocken, PA 19428

(Address of principal executive offices)

(610) 834-9600

(Issuer's telephone number)

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

State the number of shares outstanding of each of the issuer's classes of
common equity, as of August 1, 2005: Common stock, par value \$.01 per share:
50,586,181 shares.

Transitional Small Business Disclosure Format (check one): Yes No

NOCOPI TECHNOLOGIES, INC.

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

INDEX

Part I. FINANCIAL INFORMATION	PAGE
Item 1. Financial Statements	
Statements of Operations for Three and Six Months Ended June 30, 2005 and June 30, 2004	1
Balance Sheet at June 30, 2005	2
Statements of Cash Flows for Six Months Ended June 30, 2005 and June 30, 2004	3
Notes to Financial Statements	4-5
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	6-11
Item 3. Controls and Procedures	12
Part II. OTHER INFORMATION	13
SIGNATURES	14

PART I - FINANCIAL INFORMATION			
ITEM 1. FINANCIAL STATEMENTS			
Nocopi Technologies, Inc. Statements of Operations* (unaudited)			
	Three Months ended June 30		Six Months ended
	2005	2004	2005
	-----	-----	-----
Revenues			
Licenses, royalties and fees	\$ 82,300	\$ 95,300	\$ 161,900
Product and other sales	53,300	49,000	95,800
	-----	-----	-----
	135,600	144,300	257,700
Cost of sales			
Licenses, royalties and fees	27,100	28,700	55,900
Product and other sales	22,900	22,300	46,400
	-----	-----	-----
	50,000	51,000	102,300
Gross profit	-----	-----	-----
	85,600	93,300	155,400
Operating expenses			
Research and development	35,700	42,000	74,600
Sales and marketing	26,000	38,000	60,400

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

General and administrative (exclusive of legal expenses)	37,500	104,800	100,800
Legal expenses	27,300	28,900	47,800
	-----	-----	-----
	126,500	213,700	283,600
	-----	-----	-----
Loss from operations	(40,900)	(120,400)	(128,200)
Other income (expenses)			
Interest income	--	--	100
Interest expense and bank charges	(500)	(3,300)	(1,100)
	-----	-----	-----
	(500)	(3,300)	(1,000)
	-----	-----	-----
Net loss	(\$41,400)	(\$123,700)	(\$129,200)
	=====	=====	=====
Basic and diluted loss per common share	(\$.00)	(\$.00)	(\$.00)
Weighted average common shares outstanding	50,586,181	45,972,241	50,586,181

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

1

Nocopi Technologies, Inc.
Balance Sheet*
(unaudited)

	June 30 2005

Assets	
Current assets	
Cash and cash equivalents	\$ 6,4
Accounts receivable less \$15,000 allowance	77,1
Arbitration settlement receivable	50,0
Prepaid and other	42,8

Total current assets	176,3
Fixed assets	
Leasehold improvements	71,2
Furniture, fixtures and equipment	476,2

	547,4
Less: accumulated depreciation	503,8

	43,6
Other assets	
Arbitration settlement receivable	50,0

Total assets	\$ 269,9
	=====

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Liabilities and Stockholders' Deficiency	
Current liabilities	
Accounts payable	\$ 439,1
Accrued expenses	272,9
Deferred revenue	34,9

Total current liabilities	746,9
Stockholders' deficiency	
Common stock, \$.01 par value	
Authorized - 75,000,000 shares	
Issued and outstanding - 50,586,181 shares	505,9
Paid-in capital	11,497,4
Accumulated deficit	(12,480,3

	(477,0

Total liabilities and stockholders' deficiency	\$ 269,9
	=====

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

2

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

	Six Months ended June 30	
	2005	2004
	-----	-----
Operating Activities		
Net loss	(\$129,200)	(\$235,100)
Adjustments to reconcile net loss to cash from operating activities		
Depreciation	8,400	10,200
Compensation expense - stock option grants	--	58,000
	-----	-----
	(120,800)	(166,900)
(Increase) decrease in assets		
Accounts receivable	26,400	(15,800)
Arbitration settlement receivable	50,000	50,000
Prepaid and other	(13,600)	18,700
Increase (decrease) in liabilities		
Accounts payable and accrued expenses	30,400	52,600
Deferred revenue	10,000	(20,000)
	-----	-----
	103,200	85,500
	-----	-----
Cash used in operating activities	(17,600)	(81,400)
Investing Activities		
Additions to fixed assets	--	(800)
	-----	-----
Cash used in investment activities	--	(800)
	-----	-----
Decrease in cash and cash equivalents	(17,600)	(82,200)

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Cash and cash equivalents - beginning of period	24,000	89,900
	-----	-----
Cash and cash equivalents - end of period	\$ 6,400	\$ 7,700
	=====	=====

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

3

NOCOPI TECHNOLOGIES, INC.

NOTES TO FINANCIAL STATEMENTS
(UNAUDITED)

NOTE 1. FINANCIAL STATEMENTS

The accompanying unaudited condensed financial statements have been prepared by Nocopi Technologies, Inc. (the Company). These statements include all adjustments (consisting only of normal recurring adjustments) which management believes necessary for a fair presentation of the statements and have been prepared on a consistent basis using the accounting policies described in the summary of Accounting Policies included in the Company's 2004 Annual Report on Form 10-KSB. Certain financial information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations, although the Company believes that the accompanying disclosures are adequate to make the information presented not misleading. The Notes to Financial Statements included in the 2004 Annual Report on Form 10-KSB should be read in conjunction with the accompanying interim financial statements. The interim operating results for the three and six months ended June 30, 2005 may not be necessarily indicative of the operating results expected for the full year.

NOTE 2. GOING CONCERN

Since its inception, the Company has incurred significant losses and, as of June 30, 2005, had accumulated losses of \$12,480,300. For the years ended December 31, 2004 and 2003, the Company's losses from operations were \$328,500 and \$441,300, respectively. In addition, the Company had negative working capital of \$570,600 at June 30, 2005. The Company may incur further operating losses and experience negative cash flow in the future. Achieving profitability and positive cash flow depends on the Company's ability to generate and sustain significant increases in revenues and gross profits from its traditional business. There can be no assurances that the Company will be able to generate sufficient revenues and gross profits to achieve and sustain profitability and positive cash flow in the future.

During 2004, the Company raised \$161,000 (\$152,100 net of offering expenses) in a private placement whereby 1,610,000 shares of the Company's common stock were sold to three non-affiliated individual investors pursuant to a valid private placement. These investments, combined with the receipt of \$900,000 in June 2003 in conjunction with the settlement of its arbitration proceedings with Euro-Nocopi, S.A. and annual payments of \$50,000 in 2004 and 2005 in accordance with the settlement agreement, have permitted the Company to continue in

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

operation to the current date. As a result of the settlement, the significant legal fees incurred in the arbitration have been eliminated. Additionally, the Company has reduced staff and, in 2003, completed its relocation to a new facility that it believes will enable the Company to further reduce its operating expenses. Management of the Company believes that it will need to obtain additional capital in the immediate future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases can be realized. There can be no assurances that the Company will be successful in obtaining sufficient additional capital, or if it does, that the additional capital will enable the Company to improve its business so as to have a material positive effect on the Company's operations and cash flow. The Company believes that without additional capital, whether in the form of debt, equity or both, it may be forced to cease operations during the second half of 2005.

4

NOTE 3. INCOME TAXES

There is no provision for income taxes for the three months and six months ended June 30, 2005 and June 30, 2004 since Management has determined that the realization of the net deferred tax asset is not assured and has created a valuation allowance for the entire amount of such benefits.

NOTE 4. LOSS PER SHARE

Because the Company reported a net loss for the three and six months ended June 30, 2005 and June 30, 2004, common stock equivalents, consisting of stock options, were anti-dilutive.

NOTE 6. STOCK OPTIONS ISSUED TO EMPLOYEES

On April 30, 2004, the Company granted options to two officers to purchase a total of 250,000 shares of its common stock at an exercise price of \$0.17 per share, which was the market price on grant date, expiring in five years and vesting at various dates through April 30, 2005.

The Company applies Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations in accounting for the issuance of its stock options. Accordingly, no compensation cost was recognized for its stock options issued during the six months ended June 30, 2004. Had compensation cost for the Company's issuance of vested stock options been determined based on the fair value at grant dates for options consistent with the method of SFAS No. 123, the Company's net loss would have been increased to the pro forma amounts indicated below. The net loss per share would not change. Fair value amounts were estimated using the Black-Scholes model with the following assumptions: no dividend yield, expected volatility of 60%, and a risk-free interest rate of 4% for the three and six months ended June 30, 2004. There were no stock options issued during the three and six months ended June 30, 2005.

Three Months Ended
June 30, 2004

Six Months Ended
June 30, 2004

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Net loss	As reported	(\$123,700)	(\$235,100)
	Pro forma	(\$146,700)	(\$258,100)
Net loss per share	As reported	(\$0.00)	(\$0.01)
	Pro forma	(\$0.00)	(\$0.01)

NOTE 7. MAJOR CUSTOMER INFORMATION

The Company's largest non-affiliate customers accounted for approximately 64% and 71% of revenues in the second quarter and first half of 2005, respectively, approximately 67% and 65% of revenues in the second quarter and first half of 2004, respectively and approximately 41% of accounts receivable at June 30, 2005. The Company performs ongoing credit evaluations of its customers and generally does not require collateral. The Company also maintains allowances for potential credit losses.

5

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FORWARD-LOOKING INFORMATION

The following Management's Discussion and Analysis of Results of Operations and Financial Condition should be read in conjunction with our audited Financial Statements and Notes thereto for the year ended December 31, 2004 included in our Annual Report on Form 10-KSB filed with the Securities and Exchange Commission.

The information in this discussion contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause our actual results, performance or achievements or industry results to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Such factors include those described in "Risk Factors." The forward-looking statements included in this report may prove to be inaccurate. In light of the significant uncertainties inherent in these forward-looking statements, you should not consider this information to be a guarantee by us or any other person that our objectives and plans will be achieved. The Company does not undertake to publicly update or revise its forward-looking statements even if experience or future changes make it clear that any projected results (expressed or implied) will not be realized.

RESULTS OF OPERATIONS

The Company's revenues are derived from royalties paid by licensees of the Company's technologies, fees for the provision of technical services to licensees and from the direct sale of products incorporating the Company's technologies, such as inks, security paper and pressure sensitive labels, as well as equipment used to support the application of the Company's technologies, such as ink-jet printing systems. Royalties consist of guaranteed minimum royalties payable by the Company's licensees and/or additional royalties which typically vary with the licensee's sales or production of products incorporating

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

the licensed technology. Technical services, in the form of on-site or telephone consultations by members of the Company's technical staff, may be offered to licensees of the Company's technologies. The consulting fees are billed at agreed upon per diem or hourly rates at the time the services are rendered. Service fees and sales revenues vary directly with the number of units of service or product provided.

The Company recognizes revenue on its lines of business as follows:

a) License fees and royalties are recognized when the license term begins. Upon inception of the license term, revenue is recognized in a manner consistent with the nature of the transaction and the earnings process, which generally is ratably over the license term;

b) Product sales are recognized upon shipment of products, when the price is fixed or determinable and collectibility is reasonably assured; and

c) Fees for technical services are recognized when (i) the service has been rendered; (ii) an arrangement exists; (iii) the price is fixed or determinable based upon a per diem or hourly rate; and (iv) collectibility is reasonably assured.

6

While the Company's fixed costs have been reduced as a result of its relocation to a new location in 2003 and because the Company believes that further fixed cost reductions may not be achievable, its operating results are substantially dependent on revenue levels. Because revenues derived from licenses and royalties carry a much higher gross profit margin than other revenues, operating results are also substantially affected by changes in revenue mix.

Both the absolute amounts of the Company's revenues and the mix among the various sources of revenue are subject to substantial fluctuation. The Company has a relatively small number of substantial customers rather than a large number of small customers. Accordingly, changes in the revenue received from a significant customer can have a substantial effect on the Company's total revenue and on its revenue mix and overall financial performance. Such changes may result from a customer's product development delays, engineering changes, changes in product marketing strategies and the like. In addition, certain customers have, from time to time, sought to renegotiate certain provisions of their license agreements and, when the Company agrees to revise terms, revenues from the customer may be affected. The addition of a substantial new customer or the loss of a substantial existing customer may also have a substantial effect on the Company's total revenue, revenue mix and operating results.

Revenues for the second quarter of 2005 were \$135,600 compared to \$144,300 in the second quarter of 2004, a 6% decline. Licenses, royalties and fees decreased by \$13,000, or 14%, to \$82,300 in the second quarter of 2005 from \$95,300 in the second quarter of 2004. The decrease in licenses, royalties and fees is due primarily to the non-renewal of one license agreement at the end of 2004 offset in part by the inception during the second quarter of 2005 of license arrangements with two customers. Product sales were \$53,300 in the second quarter of 2005 compared to \$49,000 in the second quarter of 2004, a 9% increase due primarily to higher sales of the Company's inks offset in part by lower sales of security paper. For the first six months of 2005, revenues were \$257,700, 10% lower than revenues of \$284,900 in the first six months of 2004. Licenses, royalties and fees of \$161,900 in the first half of 2005 were 6% lower than the \$172,900 in the first half of 2004 due primarily to the non-renewal of one license over the preceding twelve months offset in part by the inception of three new license arrangements over the same period. Product sales were \$95,800

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

in the first half of 2005 compared to \$112,000 in the first half of 2004, a 14% decline. The decrease in product sales reflects lower sales of the Company's line of security papers offset in part by higher sales of inks during the first half of 2005 compared to the first half of 2004.

The Company's gross profit decreased to \$85,600 in the second quarter of 2005 or 63% of revenues from \$93,300 or 64% of revenues in the second quarter of 2004. Licenses, royalties and fees carry a substantially higher gross profit than product sales, which generally consist of supplies or other manufactured products which incorporate the Company's technologies or equipment used to support the application of its technologies. These items (except for inks which are manufactured by the Company) are generally purchased from third-party vendors and resold to the end-user or licensee and carry a significantly lower gross profit than licenses, royalties and fees. The modestly lower gross profit in the second quarter of 2005 compared to the second quarter of 2004 resulted principally from a decrease in revenues represented by licenses, royalties and fees offset in part by lower fixed costs of production.

For the first six months of 2005, the gross profit was \$155,400, or 60% of revenues compared to \$171,400, or 60% of revenues, in the first half of 2004. The decrease in the gross profit in absolute dollars in the first half of 2005 compared to the first half of 2004 resulted from a lower level of revenues in the first half of 2005 compared to the first half of 2004.

7

Research and development expenses decreased to \$35,700 in the second quarter of 2005 from \$42,000 in the second quarter of 2004. For the first six months of 2005, research and development expenses were \$74,600 compared to \$94,000 in the first half of 2004. The decrease in both the second quarter and first half of 2005 was due primarily to a reduction of staff during the third quarter of 2004.

Sales and marketing expenses were \$26,000 in the second quarter of 2005 compared to \$38,000 in the second quarter of 2004. For the first six months of 2005, sales and marketing expenses were \$60,400 compared to \$83,000 in the first six months of 2004. The decrease in both the second quarter and first half of 2005 compared to 2004 reflects lower travel, sales promotion and business show expense as certain expenses associated with the introduction of the Company's new Rub-n-Color product for the Educational and Toy Market in the second quarter and first half of 2004 were not incurred in the second quarter and first half of 2005.

General and administrative expenses (exclusive of legal expenses) decreased by \$67,300 to \$37,500 in the second quarter of 2005 from \$104,800 in the second quarter of 2004. The decrease in the second quarter of 2005 compared to the second quarter of 2004 is due primarily to \$58,000 in expenses recorded in the second quarter of 2004 in connection with the issuance to members of the Company's Board of Directors and two consultants of 900,000 options to purchase shares of the Company's common stock. No options were issued in 2005. For the first six months, general and administrative expenses (exclusive of legal expense) decreased by \$59,700 to \$100,800 in 2005 from \$160,500 in 2004 primarily as a result of the same factor as the second quarter decrease.

Legal expenses of \$27,300 in the second quarter of 2005 approximated the \$28,900 in the second quarter of 2004. Legal expenses for the first half of 2005 decreased to \$47,800 from \$62,300 in the first half of 2004 resulting from a lower level of legal counseling required by the Company in its compliance with securities regulations and other matters during the first six months of 2005.

Other income (expense) decreased in the second quarter and first half of

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

2005 compared to the second quarter and first half of 2004 as interest expense on the demand loans was eliminated due to their conversion to common stock of the Company in September 2004.

The net loss of \$41,400 and \$129,200, respectively, in the second quarter and first half of 2005 compared to the net loss of \$123,700 and \$235,100, respectively, in the second quarter and first half of 2004 was due to the non-recurrence of the expense associated with the issuance of stock options to Directors and consultants in the second quarter of 2004, lower sales and marketing expenses and a reduction of staff during 2004 offset in part by a lower gross margin resulting from lower revenues.

PLAN OF OPERATION, LIQUIDITY AND CAPITAL RESOURCES

The Company's cash and cash equivalents decreased to \$6,400 at June 30, 2005 from \$24,000 at December 31, 2004. The cash was used to fund operations over the six-month period.

8

The loss of a number of customers during the past three years and the loss of periodic fees under the license agreement with Euro-Nocopi, S.A. commencing in 2000 have had a material adverse effect on the Company's revenues and results of operations and upon its liquidity and capital resources. During 2004, the Company raised \$161,000 (\$152,100 net of offering expenses) in a private placement whereby 1,610,000 shares of the Company's common stock were sold to three non-affiliated individual investors pursuant to a valid private placement. This investment, combined with the receipt of \$900,000 in June 2003 in conjunction with the settlement of its arbitration proceedings with Euro-Nocopi, S.A. and annual payments of \$50,000 in 2004 and 2005 in accordance with the settlement agreement, have permitted the Company to continue in operation to the current date. As a result of the settlement, a significant ongoing expense for related legal fees has been eliminated. Additionally, the Company has reduced staff and, during the third quarter of 2003, completed its relocation to a new facility that it believes will enable the Company to further reduce its operating expenses. Management of the Company believes that it will need to obtain additional capital in the future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases can be realized. There can be no assurances that the Company will be successful in obtaining sufficient additional capital, or if it does, that the additional capital will enable the Company to improve its business so as to have a material positive effect on the Company's operations and cash flow. The Company believes that without additional investment, it may be forced to cease operations during the second half of 2005.

The Company, in response to the ongoing adverse liquidity situation, has maintained a cost reduction program including staff reductions and curtailment of discretionary research and development and sales and marketing expenses, where possible.

RISK FACTORS

The Company's operating results, financial condition and stock price are subject to certain risks, some of which are beyond the Company's control. These risks could cause actual operating and financial results to differ materially from those expressed in the Company's forward looking statements, including the risks described below and the risks identified in other documents which are filed and furnished with the SEC:

Inability to Continue in Operation Without New Equity Investment. The Company

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

had a negative working capital of \$570,600 at June 30, 2005 and experienced negative cash flow from operations of \$17,600 in the six months ended June 30, 2005. Additionally, it experienced negative cash flow from operations of \$217,200 in the year ended December 31, 2004. Management of the Company believes that while certain staff reductions initiated in 2003 and continuing into 2004 as well as the move of the Company's operations to a new facility in 2003, will reduce the Company's negative cash flow, it anticipates that the negative cash flow will continue until it can achieve revenue increases. Management believes that it will need to obtain additional capital in the future both to fund investments needed to increase its operating revenues to levels that will sustain its operations and to fund operating deficits that it anticipates will continue until revenue increases can be realized. There can be no assurances that the Company will be successful in obtaining sufficient additional capital, or if it does, that the additional capital will enable the Company to improve its business so as to have a material positive effect on the Company's operations and cash flow. The Company believes that without additional investment, it may be forced to cease operations during the second half of 2005. It is uncertain whether the Company's assets will retain any value if the Company ceases operations. There are no assurances that the Company will be able to secure additional equity investment before it may be forced to cease operations.

9

Possible Inability to Develop New Business. Even if the Company is able to raise cash through additional capital or otherwise, it must quickly improve its operating cash flow. Because the Company has already significantly reduced its operating expenses, Management believes that any significant improvement in the Company's cash flow must result from increases in its revenues from traditional sources and from new revenue sources. The Company's ability to develop new revenues may depend on the extent of both its marketing activities and its research and development activities. There are no assurances that the resources the Company, even with additional capital, can devote to marketing and to research and development will be sufficient to increase the Company's revenues to levels resulting in positive cash flow.

Inability to Obtain Raw Materials and Products for Resale. The Company's adverse financial condition has required it to significantly defer payments due vendors who supply raw materials and other components of the Company's security inks, security paper that the Company purchases for resale and professional and other services. As a result, the Company is on credit hold with certain of its suppliers and is required to pay cash in advance of shipment to others. Delays in shipments to customers caused by the Company's inability to obtain materials on a timely basis and the possibility that certain current vendors may permanently discontinue to supply the Company with needed products could impact the Company's ability to service its customers and adversely affect its customer and licensee relationships. Management of the Company believes that, without significant capital investment in the very near term, the Company will not be able to maintain acceptable relationships with its vendors and professional service providers. There are no assurances that the Company will be able to secure sufficient capital investment to maintain its vendor accounts on satisfactory terms.

Uneven Pattern of Quarterly and Annual Operating Results. The Company's revenues, which are derived primarily from licensing and royalties, are difficult to forecast due to the long sales cycle of the Company's technologies, the potential for customer delay or deferral of implementation of the Company's technologies, the size and timing of inception of individual license agreements, the success of the Company's licensees and strategic partners in exploiting the market for the licensed products, modifications of customer budgets, and uneven patterns of royalty revenue and product orders. As the Company's revenue base is

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

not substantial, delays in finalizing license contracts, implementing the technology to initiate the revenue stream and customer ordering decisions can have a material adverse effect on the Company's quarterly and annual revenue expectations and, as the Company believes that further reductions in the fixed component of the Company's operating expenses may not be achievable, income expectations will be subject to a similar adverse outcome.

Volatility of Stock Price. The market price for the Company's common stock has historically experienced significant fluctuations and may continue to do so. The Company has, since its inception, operated at a loss and has not produced revenue levels traditionally associated with publicly traded companies. The Company's common stock is not listed on a national or regional securities exchange and, consequently, the Company receives limited publicity regarding its business achievements and prospects, few securities analysts and traders follow it and it is thinly traded. The market price may be affected by announcements of new relationships or modifications to existing relationships. The stock prices of many developing public companies, particularly those with small capitalizations, have experienced wide fluctuations not necessarily related to operating performance. Such fluctuations may adversely affect the market price of the Company's common stock.

10

Intellectual Property. The Company relies on a combination of protections provided under applicable international patent, trademark and trade secret laws. It also relies on confidentiality, non-analysis and licensing agreements to establish and protect its rights in its proprietary technologies. While the Company actively attempts to protect these rights, the Company's technologies could possibly be compromised through reverse engineering or other means. In addition, the Company's ability to enforce its intellectual property rights through appropriate legal action has been and will continue to be limited by the Company's adverse liquidity. There can be no assurances that the Company will be able to protect the basis of its technologies from discovery by unauthorized third parties or to preclude unauthorized persons from conducting activities that infringe on the Company's rights. The Company's adverse liquidity situation has also impacted its ability to obtain patent protection on its intellectual property and to maintain protection on previously issued patents. While the Company has been advised by its patent counsel that patent maintenance fees approximating \$12,000 will be due during 2005, it presently intends to keep in force patents, whose maintenance fees are approximately \$1,000, that are applicable to its current and prospective product offerings. There can be no assurances that the Company will be able to continue to prosecute new patents and maintain issued patents. As a result, the Company's customer and licensee relationships could be adversely affected and the value of the Company's technologies and intellectual property (including their value upon a liquidation of the Company) could be substantially diminished.

OFF-BALANCE SHEET ARRANGEMENTS

The Company does not have any off-balance sheet arrangements.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In December 2004, the FASB revised SFAS 123, "Accounting for Stock-Based Compensation" to require all companies to expense the fair value of employee stock options. SFAS 123R is effective at the beginning of the next fiscal year beginning after December 15, 2005 for a small business issuer.

The following recently issued accounting pronouncements are currently not applicable to the Company.

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

In January 2003, subsequently revised December 2003, the FASB issued FASB Interpretation No. 46R ("FIN 46R"), Consolidation of Variable Interest Entities - An Interpretation of AARB N. 51. FIN 46R requires that if any entity has a controlling financial interest in a variable interest entity, the assets, liabilities and results of activities of the variable interest entity should be included in the consolidated financial statements of the entity. FIN 46R provisions are effective for all arrangements entered into after January 31, 2003. FIN 46R provisions are required to be adopted for the first period ending after December 15, 2004 for a small business issuer.

FAS 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity, requires financial instruments within its scope to be classified as liabilities (or assets in some circumstances). The Statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise effective at the beginning of the first interim period beginning after June 15, 2003, except for certain mandatorily redeemable financial instruments. It is to be implemented by reporting the cumulative effect of a change in an accounting principle for financial instruments created before the issuance date of the Statement and still existing at the beginning of the interim period of adoption. Restatement is not permitted. The effective date of certain provisions of Statement 150 for certain mandatorily redeemable financial instruments has been deferred by FSP FAS 150-3. Under the FSP, certain mandatorily redeemable shares are subject to the provisions of Statement 150 for the first fiscal period beginning after December 15, 2004. Other mandatorily redeemable shares are deferred indefinitely but may be subject to classification or disclosure provisions of the Statement.

11

ITEM 3. DISCLOSURE CONTROLS AND PROCEDURES

The Company's disclosure controls and procedures are designed to provide reasonable assurance that material information required to be included in its periodic SEC reports is recorded, processed, summarized and reported within the time periods specified in the relevant SEC rules and forms. The Company has carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, of the effectiveness of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-15. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded, as of the end of the period covered by this report, that the Company's disclosure controls and procedures are effective.

There have been no changes in the Company's internal controls over financial reporting during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

12

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Edgar Filing: NOCOPI TECHNOLOGIES INC/MD/ - Form 10QSB

Not Applicable
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Not Applicable
Item 3. Defaults Upon Senior Securities

Not Applicable
Item 4. Submission of Matters to a Vote of Security Holders

Not Applicable
Item 5. Other Information

Not Applicable
Item 6. Exhibits

(a) Exhibits

- 31.1 Certificate of Chief Executive Officer required by Rule 13a-14(a).
- 31.2 Certificate of Chief Financial Officer required by Rule 13a-14(a).
- 32. Certificate of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

13

SIGNATURES

Pursuant to the requirement 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.

NOCOPI TECHNOLOGIES, INC.

DATE: August 15, 2005

/s/ Michael A. Feinstein, M.D.

Michael A Feinstein, M.D.
Chairman of the Board

DATE: August 15, 2005

/s/ Rudolph A. Lutterschmidt

Rudolph A. Lutterschmidt
Vice President & Chief Financial Officer

14