

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

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For The Fiscal Year Ended December 31, 2022

Commission File Number: 0-31641

SCI ENGINEERED MATERIALS, INC.

(Exact name of registrant as specified in its charter)

Ohio
(State or other jurisdiction of
incorporation or organization)

31-1210318
(I.R.S. Employer
Identification No.)

2839 Charter Street
Columbus, Ohio 43228
(Address of principal executive offices)
Registrant's telephone number, including area code: **(614) 486-0261**

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

None
Common Stock, without par value (Title of Class)
OTCQB (Name of each exchange on which registered)

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 15(d) of the Exchange 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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (section 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 ☒ 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 has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☐

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

The aggregate market value of the Registrant's common equity held by non-affiliates of the Registrant was approximately \$9,971,863 on June 30, 2022. For purposes of this disclosure, shares of common stock held by persons who hold more than 10% of the outstanding shares of common stock and shares held by executive officers and directors of the registrant have been excluded because such persons may be deemed to be affiliates. This determination of executive officer or affiliate status is not necessarily a conclusive determination for other purposes. There were 4,519,524 shares of the Registrant's Common Stock outstanding on February 2, 2023.

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

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common stock, without par value	SCIA	OTCQB

DOCUMENTS INCORPORATED BY REFERENCE

Portions of our Proxy Statement for the 2023 Annual Meeting of Stockholders are incorporated by reference in Part III.

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Note Regarding Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 26A of the Securities Act of 1933, as amended. The words "anticipate," "believe," "expect," "estimate," and "project" and similar words and expressions identify forward-looking statements, which speak only as of the date hereof. Investors are cautioned that such statements involve risks and uncertainties that could cause actual results to differ materially from historical or anticipated results due to many factors, including, but not limited to, the factors discussed in "Risk Factors." The Company undertakes no obligation to publicly update or revise any forward-looking statements.

PART I

ITEM 1. BUSINESS

Introduction

SCI Engineered Materials, Inc. ("SCI", "we" or the "Company"), an Ohio corporation, was incorporated in 1987. We operate in one segment as a global supplier and manufacturer of advanced materials for Physical Vapor Deposition ("PVD") thin film applications. We are focused on markets within the PVD industry including Aerospace, Automotive, Defense, Glass, Optical Coatings, and Solar. Substantially all revenues are generated from customers with multi-national operations. The Company develops innovative customized solutions enabling commercial success through collaboration with end users and Original Equipment Manufacturers.

History of the Company

The late Dr. Edward Funk, Sc.D., and his late wife Ingeborg founded SCI in 1987. Dr. Funk, formerly a Professor of Metallurgy at The Ohio State University and a successful entrepreneur, envisioned significant market potential for the then newly discovered High Temperature Superconductivity ("HTS") material YBCO (T_c of 90° K). Our first product was a 99.999% pure, co-precipitated YBCO 1-2-3 powder. Over the years we expanded our product line by adding other High T_c Powders, sintered shapes, single crystal substrates, and non-superconducting sputtering targets. At this time, we are not pursuing this market, but these early years of development are the foundation on which our material science experience is built.

We opened a subdivision, Target Materials Inc. ("TMI"), in 1991 to supply the increasing worldwide demand for sputtering and laser ablation targets. We became a full-service manufacturer of high-performance thin film materials, providing a wide selection of metals, ceramics, and alloys for sputtering targets, evaporation sources, and other PVD applications. We served the Research and Development market as well as the Industrial and Decorative Coating markets. During this time, we began to manufacture targets for the photovoltaic, flat panel display, and semiconductor industries.

SCI and TMI were merged in 2002. We continued to manufacture complex ceramic, metal, and alloy products for the photonic, photovoltaic, media storage, flat panel display, and semiconductor industries. The Company's name was changed to SCI Engineered Materials, Inc. from Superconductive Components, Inc. in 2007 to reflect its expanded market focus.

In January 2017, we received ISO 9001:2015 registration, an internationally recognized quality standard. We received ISO 9001:2008 registration in April 2010 and prior to that time we were ISO 9001:2000 registered.

For more than three decades we have been developing considerable expertise in the development and manufacturing ramp-up of innovative materials, such as Transparent Conductive Oxides (TCO)s. The Company is committed to finding further growth and is pursuing opportunities that can benefit from this expertise. Today, we serve a diverse base of domestic and multi-national corporations, universities, and leading research institutions. We actively seek to partner with organizations to provide solutions for difficult material challenges.

Business

We are a supplier of materials to the PVD industry. Customers need our materials to produce nano layers of metals and oxides for advanced material systems. Applications for PVD coatings range from everyday items to complex computer processors. Every day applications include automotive, transparent anti-scratch coatings on eyeglasses, coatings on kitchen faucets, as well as low emissivity glass for household windows and commercial buildings. More technically advanced applications for our products include semiconductors, thin film solar, flat panel displays, defense, aerospace, and photonics.

We continue to pursue niche opportunities where our core competencies give us an advantage and complement our manufacturing capabilities allowing us to enter new markets with minimal capital investment. This disciplined approach enables us to focus on those opportunities that are the best fit for our capabilities and offer the greatest long-term return. Considerations include our core strengths, resource requirements, and time-to-market.

The Photonics industry includes a number of diverse markets which represents the best fit for our applications. We and our customers are continually identifying new materials that improve the utility of optical coatings. This includes improvements in their ability to focus, filter or reflect light, all of which increase the potential demand for the types and volume of products we sell in this market. Photonic applications continue to expand as new methods are found to manipulate light waves to enhance the various applications.

In 2018, we began to supply target materials to the roll-to-roll coating industry. Roll-to-roll PVD coating is an emerging market in which intermediate manufacturers use our advanced materials to coat flexible substrates for a wide range of applications. In a roll-to-roll coating system, multiple layers of varied materials can be deposited over large areas on flexible substrates without costly down time associated with disrupting the vacuum manufacturing process. These coated substrates can be used as standalone products in high volume consumer goods or can be laminated into electronic and optical components such as solar panels, architectural glass and displays. Our rotatable bonding technology, compounded with our material development capabilities, position us well in this emerging market for potential growth.

We continue to invest in developing new products for SCI's chosen markets with emphasis on accelerating time to market.

For the year ended December 31, 2022, we had total revenue of \$23,467,030 compared to \$13,448,021 for the year ended December 31, 2021. Higher pricing, primarily attributable to increased raw material costs, higher volume and product mix were key factors that contributed to the increase.

Our largest customer represented approximately 73% of total revenues in 2022 and 63% in 2021. This year-over-year increase was attributable to the factors noted above including additional products.

Marketing and Sales

Europe and Asia, as well as the Americas, have high demand for sputtering targets. We continue to seek ways to expand our global marketing reach. We use various distribution channels for specific end markets through direct sales by our employees and manufacturers' representatives for international markets. We have manufacturer's representatives in the Chinese, Korean and Taiwanese markets. Also, the internet provides tremendous opportunities for us to reach new customers with compatible product needs.

Our corporate website is www.sciengineeredmaterials.com. The website is designed to serve customers, suppliers, and investors with additional information in an easy-to-use format and includes expanded mobile access. There are also social media components, including LinkedIn®, Facebook®, and Twitter® to enhance the Company's visibility and communication with customers and shareholders. For customers and suppliers, there is also expanded information about our product focus as well as a library of detailed product data sheets that continues to be updated. Investors can access current and archived information about the Company utilizing multiple electronic platforms.

Ceramics

We are capable of producing ceramic powders via several different processing techniques including solid state and precipitation. Ceramic targets can also be produced in a variety of ways depending on the end user applications. Production techniques include sintering, cold isostatic pressing and hot pressing.

Most of our products are manufactured from component chemicals and metal oxides supplied by various vendors. We have also identified several suppliers that are capable of minimizing potential disruption in our business.

Metals

In addition to the ceramic targets previously mentioned, we produce metal sputtering targets and backing plates. The targets are often bonded to the backing plates for applications in the PVD industry. These targets can be produced by casting, hot pressing and machining of metals and metal alloys depending on the application.

Applications for metal targets are highly varied ranging from applying decorative coatings for end uses such as sink faucets to the production of various electronic, photonic and semiconductor products.

We purchase various metals of reasonable high purity (often above 99.9%) for our applications. We are not dependent on a sole source for these metals and do not believe losing a vendor would materially affect our business.

We have continually added production processes and testing equipment to enable us to manufacture and qualify many product compositions that can be used as PVD applications by end users and Original Equipment Manufacturers.

Competition

We have several domestic and international competitors in the ceramic and metal fields, including Vacuum Engineering & Materials, Process Materials, Inc., and Materion, who also supply targets.

Suppliers

Principal suppliers in 2022 were Johnson Matthey, Rhenium Alloys, and Six Nine Metals. In every case, we have established alternate vendors that can be used to ensure availability of required materials. As volume grows, we may enter into alliances or purchasing contracts with these or other vendors.

Research and Development

We continue to invest in developing new applications for our markets including electrically conductive Zinc Tin Oxide for Solar, Architectural Glass, and Thin-Film Transistors. Specialty materials are being researched for use in niche markets such as additive manufacturing. Our development efforts utilize a disciplined innovation approach focused on accelerating time to market for these applications and involve ongoing research and development expense. We are developing sputtering targets for transparent electronic applications, which could be used to produce transparent thin film transistors via PVD processing.

We may seek funded research opportunities within our core competencies that maintain and expand technical understanding within our company.

We have certain proprietary knowledge and trade secrets related to the manufacture of metal and metal oxide PVD materials. This includes specific patents directly related to our products and market focus (see Intellectual Property section below).

New Product Initiatives

We are committed to increasing our core competencies in growth areas through development of innovative applications, continuing to pursue stronger customer relationships, and entry into compatible niche markets.

Building on more than three decades of materials science expertise, we have developed several new applications for select markets. For example, we recently achieved commercial success with an electrically conductive Molybdenum Oxide material that led to initial development of a commercially feasible rotary target with similar properties. Molybdenum Oxide is used in photovoltaic and optoelectronic markets which value rotary target geometry in their commercial processes. We have a patent pending on our high-power density bond process which has been initially well received by customers in the aerospace industry.

Utilizing our expertise in Vacuum Hot Pressing we are exploring additional defense applications for domestically manufactured Boron Carbide Armor. This same formulation also has potential use in controlling fuel rods in nuclear reactors as well as radiation protection. We are also exploring material applications, such as tungsten and molybdenum, in multiple manufacturing areas that can capitalize on our expertise and industry relationships.

Consistent with our growth strategy, we have also identified niche markets that can benefit from our expertise in custom powder solutions, such as near infrared doped phosphors and short-wave infrared applications. These applications enable extended life of phosphors for specific nighttime identification needs of defense personnel and first responders.

Our research and development team includes a Ph.D. with a degree in Material Science. This knowledge base benefits our achievement of innovative product solutions and new applications through collaboration with customers, which requires a deeper understanding beyond material properties. Our team provides knowledge in the areas of optical and electrical properties for these applications.

Intellectual Property

Our patent titled “Process for the Removal of Contaminants from Sputtering Target Substrates” (US Patent No. 10,138,545 B2) was issued on November 27, 2018. This provides a process for the removal of contaminants on a spent sputtering target used in Plasma Vapor Deposition.

We have the rights to multiple patents for technology related to the application of Zinc Oxide based Transparent Conductive Oxide in Displays. Our patent titled “Display Having a Transparent Conductive Oxide Layer Comprising Metal Doped Zinc Oxide Applied by Sputtering” (US patent No. 9,927,667) was issued on March 27, 2018; a related patent having the same title was issued on April 7, 2020 (US Patent No. 10,613,397), and we have a corresponding patent issued in Sweden. The transparent conductive oxides (TCOs) we developed in these patents have excellent electro-optical performance, high transmittance, high conductivity, and good chemical resistance. These patents have various applications that include LCDs, micro-LED, OLED, smart windows and mirrors, AR/VR goggles, e-papers, and wearable electronics. Our clients, in relevant applications, are entitled to use the patent number when referring to the devices covered by the patent and benefit from it. We believe the TCOs claimed and protected in these patents have wide and innovative applications which can put SCI in a unique position in the market as well as bring us additional business opportunities.

We also have an additional patent application pending in the US Patent and Trademark Office relating to specific technology that protects our processes used in achieving superior bonding in planar and rotatable targets which we intend to prosecute to issuance.

During 2016 we were granted a federal trademark registration for “SCI Engineered Materials”. We have additional rights in common law trademarks and services marks, as well as in our branding properties, including our blue logo.

We rely on a combination of patent and trademark law, license agreements, internal procedures, and nondisclosure agreements to protect our intellectual property; however, it should be noted that these measures may be invalidated, circumvented, or challenged. In addition, the laws of some foreign countries in which our products may be produced or sold may not protect our intellectual property rights to the same extent as the laws of the United States.

In the future, we may submit additional patent applications covering various inventions which have been developed by us. Although we cannot be guaranteed that these submissions will result in the issuance of patent. For example, the publication of U.S. patent applications can be delayed for up to one year, and tend to lag actual discoveries, and so that we may not be the first creator of inventions covered by pending patent applications or the first to file patent applications for such inventions. Additionally, other parties may independently develop similar technologies, duplicate our technologies or, if patents are issued to us or rights licensed by us, they may design around the patented aspects of any technologies we have developed or licensed.

Employees

We had 21 full-time employees as of December 31, 2022, and 2021. One of these employees holds a PhD in Material Science. We have never experienced a work stoppage and consider our relations with employees to be good. The employees do not have a bargaining unit. We are committed to continuing to provide an open and accountable workplace where employees feel empowered to speak up and raise issues. With this in mind, we provide multiple channels to communicate, ask for guidance, and report concerns. We also provide employees with paid time off to volunteer in local communities. We are committed to creating value for our communities including volunteerism and advocacy, and by operating our business in a socially and environmentally responsible way.

Environmental Matters

We handle all materials according to federal, state, and local environmental regulations and include Safety Data Sheets (SDS) with all shipments to customers. We maintain a collection of SDS sheets for all raw materials used in the manufacture of products and maintenance of equipment and ensure that all personnel follow the handling instructions contained in the SDS for each material. We contract with a reputable, fully permitted hazardous waste disposal company to dispose of the small amount of hazardous waste generated.

Collections and Write-offs

We collected receivables in an average of 38 days in 2022. We have occasionally written-off negligible amounts of accounts receivable as uncollectible and there were none in 2022 and 2021. We consider credit management critical to our success.

Seasonal Trends

We have not experienced and do not expect to experience seasonal trends in future business operations.

ITEM 1A. RISK FACTORS

We operate in a dynamic and rapidly changing environment that involves numerous risks and uncertainties. Certain factors may have a material adverse effect on our business, prospects, financial condition, and results of operations, and you should carefully consider them. Accordingly, in evaluating our business, we encourage you to consider the following discussion of risk factors, in its entirety, in addition to other information contained in this Annual Report on Form 10-K and our other public filings with the Securities and Exchange Commission (the "SEC"). Other events that we do not currently anticipate or that we currently deem immaterial may also affect our business, prospects, financial condition, and results of operations.

We desire to take advantage of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. The following factors have affected or could affect actual results and could cause such results to differ materially from those expressed in any forward-looking statements made. Investors should consider the following risks and speculative factors inherent in and affecting the business of SCI and an investment in our common stock.

Risks Relating to the Company

We have had operating losses in the past and may incur losses in the future.

Prior to 2017, the Company frequently reported annual net losses. Our results for 2022 reflect the sixth consecutive year of net income; however, while assurances cannot be provided that we will be able to operate profitably in the future, management continuously monitors business conditions and responds through proactive actions. We continue to invest in developing new products for all our markets. These efforts include accelerating time to market for those products and involve ongoing research and development expense.

During 2022 we reduced our accumulated deficit by \$1,957,024 to \$4,104,593 at December 31, 2022. Management's plans include continuing to grow our business in current and additional niche markets, developing new products, and increasing our revenue and presence in those markets. Management believes the actions that began during the last several years and continue today provide the opportunity for maintaining and improving liquidity and profitability. However, no assurances are made that such actions will result in sustained profitability.

A substantial portion of our sales has been dependent upon certain principal customers, the loss of whom could materially negatively affect the Company's total sales.

Revenue attributable to these customers includes the sale of multiple applications. Our top two customers accounted for approximately 89% of our net sales for the fiscal year ended December 31, 2022. Although they have been major customers of the Company for nearly twenty years, we do not have written agreements with these customers that require any minimum purchase obligations, and the customers could stop buying the Company's products at any time and for any reason. A reduction, delay, or cancellation of orders from these customers or the loss of these customers could significantly reduce our future revenues and profits. We cannot provide assurance that these customers or any of our other current customers will continue to place orders, that orders by existing customers will continue at current or historical levels or that we will be able to obtain orders from new customers.

We have limited marketing and sales capabilities outside North America.

We continue to develop our marketing and sales capabilities through targeted marketing, sales, technical, customer service and distribution capabilities. This includes increased participation in industry specific trade shows which attract representatives from domestic and international companies. We may enter into agreements with third parties to also provide these services to successfully market our products outside North America.

Our success depends on our ability to retain key management personnel.

Our success depends in large part on our ability to attract and retain highly qualified management, administrative, manufacturing, sales, and research and development personnel. Due to the specialized nature of our business, it may be difficult to locate and hire qualified personnel. The loss of services of one of our executive officers or other key personnel, or our failure to attract and retain other executive officers or key personnel could have a material adverse effect on our business, operating results, and financial condition. Jeremy Young was named president and chief executive officer in 2019 and has an employment agreement with the Company that contains non-competition provisions as well as severance payments. Mr. Young has been with the Company for more than seventeen years. All other key management personnel have entered into non-competition agreements with the Company. Although we have been successful in planning for and retaining highly capable and qualified successor management in the past, there can be no assurance that we will be able to do so in the future.

Competition for employees is intense, and we may not be able to attract and retain the qualified and skilled employees needed to support our business.

We believe a key portion of future success depends on the efforts and talent of our employees, including technical and skilled mechanical personnel. This will be dependent on continuing to attract, develop, motivate, and retain qualified and skilled employees. Competition for highly skilled technical, risk management and financial personnel is expected to remain intense. We may not be able to hire and retain qualified personnel at compensation levels consistent with our compensation and salary structure. Some of the companies with which we compete for experienced employees may have greater resources than we have and may be able to offer more attractive terms of employment.

We invest considerable time and expense in training our employees and we continue to implement new employee retention strategies. If we fail to retain our employees, we could incur significant expenses in hiring and training new employees, and the quality of our services and our ability to serve our customers could decline, resulting in a material adverse effect to our business.

Changes in the strategies of key trade customers may adversely affect our business.

Our products are sold in a highly competitive global marketplace which continues to experience increased concentration. We may be negatively affected by changes in the strategies of our trade customers, such as inventory de-stocking, delisting of our products, and other conditions.

Changes in global economic conditions could adversely affect our business.

The Company continues to actively monitor and respond to changes in national and global economic conditions, which include, but are not limited to, inflation, supply chain disruptions, and a global semiconductor chip shortage. Changes in these conditions could impact implementation of our growth plans and access to capital markets. Customer demand and supply-related issues could result in increased operating, transportation and shipping, material, wages, and labor costs. An economic recession (of whatever scale) has the potential to change customer purchasing patterns which could negatively impact our revenue and profitability.

Global conflicts could have impact on raw materials which could negatively impact our business.

Political uncertainties could affect global markets and thus could have a negative effect on our business. We currently have no customers or vendors in Russia or Ukraine; however, we are actively monitoring the situation as some raw materials for the PVD industry are sourced from Russia. We continue to actively monitor this situation through ongoing contact with current suppliers and customers, and adding alternate suppliers that can be used to ensure availability of required materials. In addition, supply chain disruptions continue to adversely impact customers in certain markets we serve. Thus far, we have not experienced material adverse effects regarding product shipments; however, late deliveries and sourcing of certain materials could have a negative impact on our business.

Our property is subject to risks from natural disasters such as earthquakes and severe weather, and other potential risks associated with the effects of climate change.

Our manufacturing facility may suffer harm as a result of natural or man-made disasters such as storms, earthquakes, tornadoes, floods, fires, and other extreme weather conditions. Such events could disrupt our operations, harm our employees, or severely damage or destroy manufacturing equipment. Any combination of these factors could adversely impact our business, reputation, and financial performance in ways that cannot currently be predicted.

Public health epidemics or outbreaks could adversely impact our business.

In December 2019, a novel strain of coronavirus (COVID-19) emerged in China. While initially the outbreak was largely concentrated in China and caused significant disruptions to its economy, it spread to other countries and infections were reported globally. The extent to which the coronavirus and subsequent strains impact our operations will continue to depend on future developments, which are highly uncertain and cannot be predicted with confidence, including the duration of the outbreak, new information which may emerge concerning the severity of the coronavirus and the actions to contain the coronavirus or treat its impact, among others. Since we are a manufacturer, it is not possible for our production facility to operate with some of our employees not in the facility. As a result, any prolonged “stay at home” order or similar restriction could have a material adverse effect on our operations.

Our competitors may have greater financial and other resources than us.

The market for PVD materials is substantial with significant competition in both ceramic and metal materials. While we believe that our products enjoy certain competitive advantages in design, function, quality, and availability, considerable competition exists from well-established firms such as Vacuum Engineering & Materials, Process Materials, Inc., and Materion, all of which may have more financial resources than us. We cannot provide assurance that developments by others will not render our products or technologies obsolete or less competitive.

Additional development of our products may be necessary due to uncertainty regarding development of markets.

Some of our products are in the early stages of commercialization and we believe it will be several years before these products have significant commercial end-use applications, and significant development work may be necessary to improve the commercial feasibility and acceptance of these products. There can be no assurance that we will be able to commercialize any of the products currently under development.

Our failure to comply with our debt covenants could have a material adverse effect on our business, financial condition, or results of operations.

Our debt agreements contain certain covenants. A breach of any of these covenants could result in a default under the applicable agreement. In the past our lenders have granted us a waiver or amendment when we sought relief from covenants. If a default were to occur, we would likely seek a waiver of that default, attempt to reset the covenant, or refinance the instrument and accompanying obligations. If we were unable to obtain this relief, the default could result in the acceleration of the total due related to that debt obligation. If a default were to occur, we may not be able to pay our debts or borrow sufficient funds to refinance them. Any of these events, if they occur, could materially adversely affect our results of operations, financial condition, and cash flows.

A lack of credit and/or limited financing availability to the Company, its vendors, or end users could adversely affect our business.

The Company has a line of credit with Fifth Third Bank for \$1 million which expires on August 29, 2023. However, our liquidity and financial condition could be materially and adversely affected if our ability to borrow money from new or existing lenders to finance our operations is reduced or eliminated. Similar adverse effects may also result if we realize reduced credit availability from trade creditors. Additionally, many of our customers require availability of financing to facilitate the purchase of our products. As a result, a continuing period of reduced credit availability in the marketplace could have adverse effects on our business.

Our business requires us to make capital expenditures to maintain and improve our facilities.

Our facilities sometimes require capital expenditures to address ongoing required maintenance and upgrade our capabilities. In addition, we often are required to make significant capital expenditures to satisfy customer requirements and produce newly developed products.

Our business could be negatively impacted by cyber and other security threats or disruptions.

We face various cyber and other security threats, including attempts to gain unauthorized access to sensitive information and networks; employee threats; threats to the safety of our directors, officers, and employees; threats to the security of our facilities and infrastructure; and threats from terrorist acts or other acts of aggression. Our customers and vendors face similar threats. Although we utilize internal and external independent controls to monitor and mitigate the risk of these threats, including periodic Information Technology training for all employees, there can be no assurance that these procedures and controls will be sufficient. Our security measures may also be breached due to employee error, malfeasance, system errors or vulnerabilities, or otherwise. Additionally, outside parties may attempt to fraudulently induce employees, users, or customers to disclose sensitive information to gain access to our data or our user's or customer's data. These threats could lead to losses of sensitive information or capabilities, harm to personnel, infrastructure, or products, and/or damage to our reputation as well as our vendor's ability to perform on our contracts.

Cyber threats are evolving and include, but are not limited to, ransomware, malicious software, destructive malware, attempts to gain unauthorized access to data, disruption or denial of service attacks, and other electronic security breaches that could lead to disruptions in critical systems, unauthorized release of confidential, personal, or otherwise protected information (ours or that of our employees, customers, or vendors), and corruption of data, networks, or systems.

The impact of these factors is difficult to predict, but one or more of them could result in the loss of information or capabilities, harm to individuals or property, damage to our reputation, loss of business, regulatory actions, and potential liability, any of which could have a material adverse effect on our financial position, results of operations and/or cash flows.

Risks Related to Our Intellectual Property

Our patents and proprietary rights may not be enforceable.

We rely on a combination of patent and trademark law, license agreements, internal procedures, and nondisclosure agreements to protect our intellectual property. These may be invalidated, circumvented, or challenged. In addition, the laws of some foreign countries in which our products may be produced or sold may not protect our intellectual property rights to the same extent as the laws of the United States. Our failure to protect our patent and proprietary information could adversely affect us.

Rights we have to trademarks, patents and pending patent applications may be challenged.

We have a portfolio of intellectual property that includes common law and state rights, as well of federally and internationally recognized trademark and patent rights. In addition, we take active precautions to protect our trade secret rights through various contractual means. However, we recognize that third parties may challenge these rights, including through unauthorized use or misappropriation or theft, or by legal challenge in administrative or challenge in state or district court. Such challenges include the risks of long and costly litigation, as well as the potential loss of property rights and the assessment of damages against a losing party.

Risks relating to Intellectual Property.

Because U.S. patent applications are maintained in secret until patents are issued, and publications of discoveries in the scientific or patent literature tend to lag actual discoveries by several months, we may not be the first creator of inventions covered by issued patents or pending patent applications or the first to file patent applications for such inventions. Moreover, other parties may independently develop similar technologies, duplicate our technologies or, if patents are issued to us or rights licensed by us, design around the patented aspects of any technologies we developed or licensed. We may have to participate in interference proceedings declared by the U.S. Patent and Trademark Office to determine the priority of inventions, which could result in substantial costs. Litigation may also be necessary to enforce any patents held by or issued to us or to determine the scope and validity of others' proprietary rights, which could result in substantial costs.

We may be unable to adequately prevent disclosure of trade secrets and other proprietary information.

To protect our proprietary and licensed technology and processes, we rely in part on confidentiality agreements with our corporate partners, employees, consultants, manufacturers, outside scientific collaborators and sponsored researchers and other advisors. These agreements may not effectively prevent disclosure of our confidential information and may not provide an adequate remedy in the event of unauthorized disclosure of confidential information. In addition, others may independently discover our trade secrets and proprietary information. Failure to obtain or maintain trade secret protection could adversely affect our competitive business position.

The rapid technological changes of our industry may adversely affect us if we do not keep pace with advancing technology.

The PVD market is characterized by rapidly advancing technology coupled with long and uncertain paths to large market acceptance. Our success depends on our ability to keep pace with advancing technology and processes and industry standards. We have focused our development efforts on sputtering targets. We intend to continue to develop innovative materials and integrate those advances to the thin film coatings industry and other potential industries. However, our development efforts may be rendered obsolete by research efforts and technological advances made by others or by the failure of anticipated markets to emerge, and materials other than those we currently use may prove more advantageous.

Risks Related to Our Common Stock

Our Articles of Incorporation authorize us to issue additional shares of stock.

The Company is authorized to issue up to 15,000,000 shares of common stock, which may be approved by our Board of Directors for such consideration, as they may consider sufficient without seeking shareholder approval. As of December 31, 2022, we had 4,519,524 shares outstanding and 34,361 shares underlying options that are currently exercisable resulting in 10,446,115 shares of common stock available for issue. The issuance of additional shares of common stock in the future may reduce the proportionate ownership and voting power of current shareholders.

Our Articles of Incorporation authorize us to issue up to 260,000 shares of preferred stock. The issuance of preferred stock in the future could create additional securities which would have dividend and liquidation preferences prior to the outstanding shares of common stock. These provisions could also impede a non-negotiated change in control. The Board of Directors voted in November 2021 to authorize full redemption of 24,152 shares of the Company's Convertible Preferred Stock, Series B ("Series B") effective December 31, 2021. This involved cash payments of \$248,766 (\$10.30 per Series B share, which included a 3% premium to the stated value of \$10 per share), plus unpaid annual dividends of \$265,672 (\$11.00 per Series B share).

We have not paid dividends on our common stock in the past and do not expect to do so in the foreseeable future.

We have never declared or paid cash dividends on our shares of common stock and do not expect to do so in the foreseeable future. We intend to use future earnings for the growth of our business. As a result, investors must rely on sales of the common stock after price appreciation, which may not occur, as the best way to realize future gains on their investments.

Provisions in our Articles of Incorporation and Code of Regulations provide for indemnification of officers and directors which could require us to divert funds away from our business and operations.

Our Articles of Incorporation and Code of Regulations provide for the indemnification of our officers and directors. We may be required to advance costs incurred by an officer or director to pay judgments, fines and expenses incurred by an officer or director, including reasonable attorneys' fees, as a result of actions or proceedings in which our officers and directors are involved by reason being or having been an officer or director of our company. Funds paid in satisfaction of judgments, fines, and expenses may be funds we need for operation and growth of our business.

Takeover defense provisions in Ohio law and our corporate governance documents may delay or prevent takeover attempts preventing our shareholders from realizing a premium on their stock.

Various provisions of Ohio corporation laws as well as our corporate governance documents may inhibit changes in control not approved by our Board of Directors and may have the effect of depriving our investors of an opportunity to receive a premium over the prevailing market price of our common stock in the event of an attempted hostile takeover. In addition, the existence of these provisions may adversely affect the market price of our common stock. These provisions include:

- A requirement that a special meeting of the shareholders must be called by our Board of Directors, Chairperson, the President, or the holders of shares with voting powers of at least fifty percent (50%).
- Advanced notice requirements for shareholder proposals and nominations.
- The availability of "blank check preferred stock."

Our Board of Directors can use these and other provisions to prevent, delay or discourage a change in control of the company or a change in our management. Any such delay or prevention of a change in control of management could deter potential acquirers or prevent the completion of a takeover transaction to which our shareholders could receive a substantial premium over the current market price of our common stock, which may in turn limit the price investors might be willing to pay for our common stock.

The market for our common stock is limited, and as such our shareholders may have difficulty reselling their shares when desired or at attractive market prices.

Our stock price, trading volume, and market listing may make it more difficult for our shareholders to resell shares when desired or at attractive prices. In 2001, our stock began trading on The Over-the-Counter Bulletin Board, now known as the OTC Markets. Our common stock trades in low volumes and at low prices. Some investors view low-priced stocks as unduly speculative and therefore not appropriate candidates for investment. Many institutional investors have internal policies prohibiting the purchase or maintenance of positions in low-priced stocks. This has the effect of limiting the pool of potential purchasers of our common stock at present price levels. Shareholders may find greater percentage spreads between bid and asked prices, and more difficulty in completing transactions and higher transaction costs when buying or selling our common stock than they would if our stock were listed on a major stock exchange.

Our common stock has been subject to the Securities and Exchange Commission's "penny stock" regulations, which may limit the liquidity of common stock held by our shareholders.

Our common stock currently trades on the OTC Markets' OTCQB market under the symbol "SCIA". Based on a trading price below \$5 per share, our common stock is considered a "penny stock" for purposes of federal securities laws, and therefore has been subject to regulations, which affected the ability of broker-dealers to sell our securities. Broker-dealers who recommend a "penny stock" to persons (other than established customers and accredited investors) must make a special written suitability determination and receive the purchaser's written agreement to a transaction prior to sale.

If penny stock regulations apply to our common stock, it may be difficult to trade the stock because compliance with the regulations can delay and/or preclude certain trading transactions. Broker-dealers may be discouraged from effecting transactions in common stock because of the sales practice and disclosure requirements for penny stock. This could adversely affect the liquidity and/or price of our common stock and impede the sale of the common stock in the secondary market.

Risks Related to Government Regulation

We are subject to anti-corruption laws in the jurisdictions in which we may operate, including anti-corruption laws of China and the Federal Corrupt Practices Act (FCPA). Our failure to comply with these laws could result in penalties which could harm our reputation and have a material adverse effect on our business, results of operations and financial condition.

We are subject to the FCPA, which generally prohibits companies and their intermediaries from making improper payments to foreign officials for the purpose of obtaining or keeping business and/or other benefits, along with various other anticorruption laws. Although we continue to monitor policies and procedures designed to ensure that we, our employees, distributors and other intermediaries comply with the FCPA and other anti-corruption laws to which we are subject, there is no assurance that such policies or procedures will work effectively all of the time or protect us against liability under the FCPA or other laws for actions taken by our employees, distributors and other intermediaries with respect to our business or any businesses that we may acquire. If we are not in compliance with the FCPA and other laws governing the conduct of business with government entities (including local laws), we may be subject to criminal and civil penalties and other remedial measures, which could have an adverse impact on our business, financial condition, results of operations and liquidity. Any investigation of any potential violations of the FCPA or other anticorruption laws by U.S. or foreign authorities could have an adverse impact on our business, financial condition, and results of operations.

Environmental compliance costs and liabilities associated with our facility may have a material adverse effect on our business, financial condition, results of operations and prospects.

We are subject to various federal, state, and local environmental and health and safety laws and regulations with respect to our operations. These laws and regulations address various matters, including asbestos, fuel oil management, wastewater discharges, air emissions, and hazardous wastes. The costs of complying with these laws and regulations and the penalties for non-compliance can be substantial. For example, with respect to leased property, we may be held liable for costs relating to the investigation and cleanup of our leased property from which there has been a release or threatened release of a regulated material as well as other properties affected by the release. In addition to these costs, which are typically not limited by law or regulation and could exceed the property's value, we could be liable for certain other costs, including, without limitation, governmental fines, and injuries to persons, property, or natural resources. Further, some environmental laws create a lien on the contaminated site in favor of the government for damages and the costs it incurs in connection with the contamination. While we are not aware of any potential environmental problems, no assurances are made that such problems and costs associated with them will not arise in the future. If any of our properties were found to violate environmental laws, we may be required to expend significant amounts of time and money to rehabilitate the property, and we may be subject to significant liability. Any environmental compliance costs and liabilities incurred may have a material adverse effect on our business, financial condition, results of operations and growth prospects.

The increasing costs of being a public company may strain our resources and impact our business, financial condition, and results of operations.

As a public company, we are subject to reporting requirements of the Securities Exchange Act of 1934, as amended or the Exchange Act, the Sarbanes-Oxley Act of 2002, or the Sarbanes Oxley Act and the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act. The Exchange Act requires that we file annual, quarterly, and current reports with respect to our business and financial condition. The Sarbanes-Oxley Act requires that we maintain effective disclosure controls and procedures and internal controls for financial reporting. We are required to document and test our internal control procedures to satisfy the requirements of Section 404(b) of the Sarbanes-Oxley Act, which requires annual management assessments of the effectiveness of our internal controls over financial reporting. The Dodd-Frank Act requires us to audit our supply chain and report conflict minerals usage.

These requirements may place a strain on our systems and resources in the future and may require us to hire additional accounting and financial staff with the appropriate public company experience and technical accounting knowledge. In addition, the failure to maintain such internal controls could result in us being unable to provide timely and reliable financial information which could potentially subject us to sanctions or investigations by the Securities and Exchange Commission or events could have an adverse effect on our business, financial condition, or results of operations. Although we have taken steps to maintain our internal control structure as required by the Exchange Act and the Sarbanes-Oxley Act, we cannot provide any assurances that control deficiencies will not occur in the future.

Regulation from the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) could adversely affect our business or financial results.

Changes in regulatory requirements, such as the reporting requirements relating to conflict minerals originating in the Democratic Republic of Congo or adjoining countries included in the Dodd-Frank Act, or evolving interpretations of existing regulatory requirements, may result in increased compliance cost, capital expenditures and other financial obligations that could adversely affect our business or financial results. We conducted an analysis of our products and found that the above SEC defined “conflict minerals”, which are tantalum, tin, tungsten, and gold (3TG), can be found in our products. Therefore, the products that we manufacture are subject to the reporting obligations of Rule 13p-1.

Despite having conducted a good faith reasonable country of origin inquiry, we concluded that our supply chain remains “DRC conflict undeterminable”. We have reached this conclusion because we have been unable to determine the origin of the 3TG used. We will continue to work with our suppliers. Should the regulations or our analysis change, it could impact the sourcing of materials that we use to manufacture our products.

If significant tariffs or other restrictions are placed on imports or any related countermeasures are taken by other countries, our revenue and results of operations may be materially harmed.

Import tariffs and/or other mandates imposed by sovereign governments could potentially lead to a trade war with other foreign governments and could significantly increase the prices on raw materials that are critical to our business. We could be forced to increase prices to our customers or, if unable to do so, result in lowering our gross margin on products sold.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

Not applicable.

ITEM 2. PROPERTIES.

Our office and manufacturing facilities are located at 2839 Charter Street, Columbus, Ohio, where we occupy approximately 32,000 square feet. We moved our operations into this facility in 2004. The lease on the property expires on November 30, 2024.

We are current on all operating lease liabilities.

ITEM 3. LEGAL PROCEEDINGS.

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Market for Common Stock

Our common stock currently trades on the OTC Markets' OTCQB market under the symbol "SCIA".

Based on its trading price, our common stock is considered a "penny stock" for purposes of federal securities laws, and therefore has been subject to certain regulations. See "Risk Factors" for specific disclosures concerning the market for the Company's common stock.

Holders of Record

As of December 31, 2022, there were approximately 220 registered holders of record of our common stock and 4,519,524 shares issued and outstanding.

Dividends

We have never paid cash dividends on our common stock and do not expect to pay any dividends on our common stock in the foreseeable future. We intend to use our future earnings for the growth of the business.

The Board of Directors voted in November 2021 to authorize full redemption of 24,152 shares of the Company's Convertible Preferred Stock, Series B ("Series B") effective December 31, 2021. This involved cash payments of \$248,766 (\$10.30 per share, which included a 3% premium to the stated value of \$10 per share), plus unpaid annual dividends of \$265,672 (\$11.00 per share).

Equity Compensation Plan Information

The following table sets forth additional information as of December 31, 2022, concerning shares of our common stock that may be issued upon the exercise of options and rights under our existing equity compensation plans and arrangements approved by our shareholders which include our 2011 Stock Option Plan and 2006 Stock Option Plan. The information includes the number of shares covered by and the weighted average exercise price of, outstanding options and other rights, and the number of shares remaining available for future grants (excluding the shares to be issued upon exercise of outstanding options and other rights).

	Number of Securities to be issued upon exercise of outstanding options and rights (a)	Weighted-average exercise price of outstanding options and rights (b)	Number of securities remaining available for issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans	41,304	\$ 1.05	215,285

ITEM 6. RESERVED.

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

Executive Summary

For the year ended December 31, 2022, we had total revenue of \$23,467,030 compared to \$13,448,021 for the year ended December 31, 2021. Higher pricing, primarily attributable to raw material costs, higher volume and product mix were key factors that contributed to the increase.

Gross profit was \$4,786,955 for 2022 compared to \$3,529,255 for 2021. The increase was attributable to higher revenue as well as favorable product mix and improved manufacturing efficiency. The year ended December 31, 2021 included a reduction of costs of approximately \$323,000 related to the Employee Retention Credit ("ERC") enacted in 2020.

Operating expenses were \$2,306,737 and \$1,751,349 for 2022, and 2021, respectively. The year ended December 31, 2021 included a reduction of expenses of approximately \$238,000 related to the ERC.

Income from operations was \$2,480,218 and \$1,777,906 for 2022 and 2021, respectively

Consistent with our growth strategy, we have identified niche markets that can benefit from our expertise in custom powder solutions, such as near-infrared doped phosphors and short-wave infrared applications. These applications enable extended life of phosphors for specific nighttime identification needs of defense personnel and first responders.

New initiatives are also being pursued that utilize our vacuum hot press, cold isostatic press, and kilns for increased production and development projects, including diffusion bonding. We recently manufactured and sold conductive metal oxides for direct current sputtering of Tungsten Oxide and Molybdenum Oxide materials. We continue to invest in developing new products for all our markets including specialty bonding processes for Aerospace customers. Those products involve research and development expense to accelerate time to market.

Several issues continue to affect national and global market conditions. First, inflation remains at historically high levels, impacting labor, raw material costs and transportation expenses. We have generally been able to pass on these increases to customers but are unable to predict how future or sustained inflationary pressure may impact our results. Second, supply chain disruptions are adversely impacting customers in certain markets. Thus far, we have not experienced material adverse effects regarding product shipments; however, timely deliveries and sourcing of certain materials is of increased concern. Third, published articles and corporate announcements continue to address the global semiconductor chip shortage, which is anticipated to continue into 2023. This shortage is affecting some of our customers which could impact the Company's revenue, volume, and profitability. Fourth, there are increased political uncertainties affecting global markets. Although we currently have no customers or vendors in Russia or Ukraine, we continue to monitor the situation as some raw material comes from Russia for the PVD industry. We continue to actively monitor these developments, including ongoing contact with our suppliers and customers, including identifying additional suppliers and adapting to our customers' specific circumstances and forecasts.

In March 2020, the World Health Organization declared the coronavirus disease (COVID-19) a global pandemic and recommended containment and mitigation measures worldwide. Since then, most federal, state, and local executive orders have been lifted. Based on ongoing conversations with customers, we do not expect to experience any material impairments or changes in accounting judgements related to COVID-19. We continue to follow practical safety procedures as needed. During 2022, we resumed in-person meetings, participated onsite in industry trade shows, and continue to maintain regular contact, via phone and other electronic means, with all customers and suppliers.

RESULTS OF OPERATIONS

Year 2022 compared to Year 2021

Revenue

For the year ended December 31, 2022, we had total revenue of \$23,467,030, compared to \$13,448,021 for the year ended December 31, 2021. This was an increase of \$10,019,009. Higher raw material pricing was the most significant factor for the increase in revenue. In addition, higher volume and product mix contributed to the increase.

Gross profit

Gross profit was \$4,786,955 for 2022 compared to \$3,529,255 for 2021. The increase was attributable to higher revenue as well as improved manufacturing efficiency. The year ended December 31, 2021 included a reduction of costs of approximately \$323,000 related to the Employee Retention Credit ("ERC"). Gross profit as a percentage of revenue (gross margin) was 20.4% and 26.2% for 2022 and 2021, respectively. The lower gross margin in 2022 compared to a year ago was due to higher raw material costs and product mix during 2022 as well as the ERC recognized in 2021.

General and administrative expense

General and administrative expense for 2022 and 2021, was \$1,549,696 and \$1,280,579, respectively, an increase of 21.0%. During 2022 there was an increase in compensation of \$151,771, which included an increase in staff. Business liability insurance (due to higher revenue) increased \$48,892. The year 2021 also benefited from the ERC of approximately \$78,000.

Included in general and administrative expense was \$260,826 and \$270,609 for professional fees during 2022 and 2021, respectively. These expenses were primarily related to SEC compliance costs for legal, accounting and stockholder relations fees.

Research and development expense

Research and development expense for 2022 was \$375,728, compared to \$235,679 for 2021, an increase of 59.4%. The ERC of approximately \$89,000 was included in the twelve months ended December 31, 2021. Additional research supplies also contributed to the increase in expenses in 2022. Specialty materials are being researched for use in niche markets which include custom applications and additive manufacturing. Our development efforts utilize a disciplined innovation approach focused on accelerating time to market for these applications and involve ongoing research and development expense.

Marketing and sales expense

Marketing and sales expense was \$381,313, and \$235,091 during 2022 and 2021, respectively. This was an increase of \$146,222, or 62.2%. During 2022 there was an increase in compensation of \$45,632 which was partially offset by a reduction in outside consulting expenses of \$23,500. Travel expenses increased \$43,474 as we resumed in-person meetings with some customers and participated onsite in additional industry trade shows. The ERC of approximately \$71,000 reduced expenses in 2021.

Stock compensation expense

Included in total expenses were non-cash stock-based compensation costs of \$49,321 and \$47,903 for 2022 and 2021, respectively. The non-employee board members received compensation of 8,755 and 9,165 shares of common stock of the Company during 2022 and 2021, respectively. The stock had an aggregate value of \$29,967 and \$29,963 for the year ended December 31, 2022, and 2021, respectively, and was recorded as non-cash stock compensation expense in the financial statements. Beginning January 1, 2023, non-employee board members will receive their entire compensation in cash. Compensation expense for all stock-based awards is based on the grant date fair value and recognized over the required service (vesting) period. Unrecognized non-cash stock-based compensation expense was \$1,576 as of December 31, 2022, and will be recognized through April 2023.

Interest

Interest income was \$19,201 for the year ended December 31, 2022 and interest expense was \$32,140 for the year ended December 31, 2021. The improvement was due to our investment into marketable securities and the overall increase in interest rates during the second half of 2022 and the final payments of multiple finance leases during 2021.

Income taxes

Income tax expense was \$542,395 and \$392,242 for the twelve months ended December 31, 2022 and 2021, respectively. At December 31, 2021, the deferred tax asset was \$663,820. As of each reporting date, management considers new evidence, both positive and negative, that could affect its view of the future realization of deferred tax assets. Accordingly, management determined that no valuation allowance was necessary, and the deferred tax asset was \$151,164 at December 31, 2022.

Income applicable to common stock

Income applicable to common stock for 2022 and 2021 was \$1,957,024 and \$1,654,672, respectively. The increase was primarily the result of higher revenue and gross profit. Included in the year 2021 was the ERC which reduced overall expenses by approximately \$561,000 and the forgiveness of our Payroll Protection Plan loan of \$325,300.

Liquidity and Capital Resources

Cash

As of December 31, 2022, cash on hand was \$3,947,966 compared to \$4,140,942 at December 31, 2021. We purchased marketable securities of \$1,989,265 and production equipment of \$536,313 during 2022 which slightly reduced our year-end cash balance.

Working capital

At December 31, 2022, working capital was \$5,211,625 compared to \$3,907,135 at December 31, 2021, an increase of \$1,304,490 or 33.4%. The increase was primarily due to the increase in inventory and investment in marketable securities noted above.

Cash from operations

Net cash provided by operating activities during 2022 was \$2,398,155 and \$2,610,548 during 2021. In addition to the net income generated, this included depreciation and amortization of \$519,031 and \$516,579, and noncash stock-based compensation costs of \$49,321 and \$47,903 for the twelve months ended December 31, 2022, and 2021, respectively. The decrease in prepaid expenses was related to inventory paid for in December 2021 and received in January 2022. Inventories and accounts payable increased due to orders received during the fourth quarter and throughout 2022. Customer orders remain strong, and deposits increased slightly as customers have monitored inventory more closely with continued emphasis on intra-quarter shipments.

Cash from investing activities

Cash of \$536,313 and \$706,242 was used in investing activities during the twelve months ended December 31, 2022, and 2021, respectively, for the acquisition of production equipment. This included a vacuum hot press that enables production of higher temperature materials with increased capacity. It was purchased and installed for approximately \$500,000. A deposit of \$220,075 was paid in the first quarter of 2021 for this vacuum hot press and the remaining amount was paid in cash during the third quarter of 2022. As previously mentioned, we purchased marketable securities of \$1,989,265 during 2022.

Cash from financing activities

Cash of \$96,702 and \$160,416 was used in financing activities for principal payments to third parties for finance lease obligations during 2022 and 2021, respectively. The decrease was due to final payments of multiple finance leases during 2021. On December 31, 2021, we redeemed all 24,152 shares of our Convertible Preferred Stock, Series B. The redemption included cash payments of \$248,766 plus unpaid annual dividends of \$265,672. An annual dividend payment of \$24,152 was previously made to owners of this stock during the second quarter of 2021.

Debt outstanding

Total debt outstanding decreased to \$146,516 at December 31, 2022, from \$243,218 at December 31, 2021, a decrease of 40%. As previously mentioned, cash of \$96,702 was used for principal payments for finance lease obligations during 2022.

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make judgments, assumptions and estimates that affect the amounts reported in the Financial Statements and accompanying notes. Note 2 to the Financial Statements in the Annual Report on Form 10-K for the year ended December 31, 2022, describes the significant accounting policies and methods used in the preparation of the Financial Statements. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventory allowances, property and equipment depreciable lives, patents and license useful lives, revenue recognition, income tax expense, deferred tax assets and liabilities, realization of deferred tax assets, stock-based compensation and assessing changes in which impairment of certain long-lived assets may occur. Actual results could differ from these estimates. The following critical accounting policies are impacted significantly by judgments, assumptions and estimates used in the preparation of the Financial Statements. The allowance for doubtful accounts is based on our assessment of the expected collectability of specific customer accounts and the aging of the accounts receivable. If there is a deterioration of a major customer's credit worthiness or actual defaults are higher than our expected losses, our estimates of the recoverability of amounts due us could be adversely affected. Inventory purchases and commitments are based upon future demand forecasts. If there is a sudden and significant decrease in demand for our products or there is a higher risk of inventory obsolescence because of rapidly changing technology and customer requirements, we may be required to increase our inventory allowances and our gross profit could be adversely affected. The tax valuation allowance is based on our consideration of new evidence, both positive and negative, that could affect our view of the future realization of deferred tax assets. If we were to determine we would not be able to realize all or part of the deferred tax asset in the future, an adjustment to the deferred tax asset would be necessary which would reduce our net income for that period. Depreciable and useful lives estimated for property and equipment, licenses and patents are based on initial expectations of the period of time these assets and intangibles will provide benefit. Changes in circumstances related to a change in our business, change in technology or other factors could result in these assets becoming impaired, which could adversely affect the value of these assets.

Inflation

While there was not a significant impact from inflation on our operations during the past three fiscal years, we experienced increased costs during 2022 that are expected to continue into 2023.

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

Not applicable

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Our balance sheets as of December 31, 2022, and 2021, and the related statements of operations, shareholders' equity and cash flows for the years ended December 31, 2022, and 2021, together with the Report of Independent Registered Public Accounting Firm thereon appear beginning on Page F-1.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

Not applicable.

ITEM 9A. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and implemented, can only provide reasonable assurance of achieving the desired control objectives. Management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, to allow timely discussions regarding required disclosure.

Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective. Disclosure controls and procedures are defined by Rules 13a-15(e) and 15d-15(e) of the Exchange Act as controls and other procedures that are designed to ensure that information required to be disclosed by us in reports filed with the SEC under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms.

Inherent Limitations Over Internal Controls

Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of assets that could have a material effect on the financial statements.

Management is responsible for the consistency, integrity, and presentation of information. We fulfill our responsibility by maintaining systems of internal control designed to provide reasonable assurance that assets are safeguarded, and transactions are executed in accordance with established procedures. The concept of reasonable assurance is based upon recognition that the cost of the controls should not exceed the benefit derived. We believe our systems of internal control provide this reasonable assurance.

The Board of Directors exercises its oversight role with respect to our systems of internal control primarily through its Audit Committee, which is comprised of independent directors. The Committee oversees our financial reporting, quarterly reviews, and audits to assess whether their quality, integrity, and objectivity are sufficient to protect shareholders' investments.

Management's Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the criteria established in the Internal Control – Integrated Framework (2013 Framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). We performed a review of our related procedures and controls and strengthened cross approval of various functions, including financial reporting and disclosure review controls by the Chief Financial Officer, to include the Chief Executive Officer and Audit Committee Chairperson where appropriate. We continue to report to the Audit Committee and the Board of Directors at least monthly (and more often as necessary). This reporting includes balance sheets, statements of operations, statements of cash flows, and other detail supporting these statements. Based on this evaluation, management has concluded that our internal control over financial reporting was effective as of December 31, 2022.

This annual report does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. Our report was not subject to attestation by our registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permits us to provide only management's report in this annual report.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rules 13a-13(f) and 15d-15(f) under the Exchange Act) that occurred during the fourth quarter of the year ended December 31, 2022, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

ITEM 9B. OTHER INFORMATION.

None.

ITEM 9C. DISCLOSURE REGARDING FOREIGN JURISDICTIONS THAT PREVENT INSPECTIONS.

Not applicable.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.

The information required by this item is included under the captions, "**Election of Directors**," "**Executive Officers**" and "**Section 16(a) Beneficial Ownership Reporting Compliance**" in our proxy statement relating to our 2023 Annual Meeting of Shareholders scheduled to be held on June 8, 2023, and is incorporated herein by reference.

We have a Business Conduct Policy applicable to all employees of the Company. Additionally, the Chief Executive Officer ("CEO") and all senior financial officers, including the principal financial officer, the principal accounting officer or controller, or any person performing a similar function (collectively, the "Senior Financial Officers") are bound by the provisions of our code of ethics relating to ethical conduct, conflicts of interest, and compliance with the law. The code of ethics is posted on our website at <http://www.sciengineeredmaterials.com/corporate-governance>.

We intend to satisfy the disclosure requirement under Item 10 of Form 8-K regarding any amendment to, waiver of, any provision of this code of ethics by posting such information on our website at the address and location specified above.

ITEM 11. EXECUTIVE COMPENSATION.

The information required by this item is included under the caption "**Executive Compensation**" in our proxy statement relating to our 2023 Annual Meeting of Shareholders scheduled to be held on June 8, 2023, and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

The information required by this item is included under the captions “**Ownership of Common Stock by Directors and Executive Officers**” and “**Ownership of Common Stock by Principal Shareholders**” in our proxy statement relating to our 2023 Annual Meeting of Shareholders scheduled to be held on June 8, 2023, and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.

The information required by this item is included under the caption “**Certain Relationships and Related Transactions, and Director Independence**” in our proxy statement relating to our 2023 Annual Meeting of Shareholders scheduled to be held on June 8, 2023, and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

The information required by this item is included under the caption “**Fees of the Registered Independent Public Accounting Firm for the years ended December 31, 2022, and 2021**” in our proxy statement relating to our 2023 Annual Meeting of Shareholders scheduled to be held on June 8, 2023, and is incorporated herein by reference.

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

<u>Exhibit Number</u>	<u>Exhibit Description</u>
3(a)	Certificate of Second Amended and Restated Articles of Incorporation of Superconductive Components, Inc. (Incorporated by reference to Exhibit 3(a) to the Company's initial Form 10-SB, filed on September 28, 2000).
3(b)	Restated Code of Regulations of Superconductive Components, Inc. (Incorporated by reference to Exhibit 3(b) to the Company's initial Form 10-SB, filed on September 28, 2000)
3(c)	Amendment to Articles of Incorporation recording the change of the corporate name to SCI Engineered Materials, Inc. (Incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-QSB filed November 7, 2007).
4(a)	SCI Engineered Materials, Inc. 2011 Stock Incentive Plan (Incorporated by reference to the Company's Definitive Proxy Statement for the 2011 Annual Meeting of Shareholders held on June 10, 2011, filed April 28, 2011).
4(b)	Superconductive Components, Inc. 2006 Stock Incentive Plan (Incorporated by reference to Appendix A to the Company's Definitive Proxy Statement for the 2006 Annual Meeting of Shareholders held on June 9, 2006, filed May 1, 2006).
4(c)	Form of Incentive Stock Option Agreement under the Superconductive Components, Inc. 2006 Stock Incentive Plan (Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated June 19, 2006, filed June 23, 2006).
4(d)*	Description of Securities of the Company.
14(a)	SCI Engineered Materials Code of Ethics for the Chief Executive Officer and Chief Financial Officer (Incorporated by reference to the Company's Current Report via the Company's website at www.sciengineeredmaterials.com).
23.1*	Consent of Independent Registered Public Accounting Firm.
24*	Power of Attorney.
31.1*	Rule 13a-14(a) Certification of Principal Executive Officer.
31.2*	Rule 13a-14(a) Certification of Principal Financial Officer.
32.1*	Section 1350 Certification of Principal Executive Officer.
32.2*	Section 1350 Certification of Principal Financial Officer.
99.1*	Press Release dated February 3, 2023, entitled "SCI Engineered Materials, Inc., Reports 2022 Fourth Quarter and Full-Year Results".
101	The Company's Annual Report on Form 10-K for the year ended December 31, 2022, formatted in iXBRL (Inline eXtensible Business Reporting Language): (i) Balance Sheets at December 31, 2022 and December 31, 2021 (ii) Statements of Operations for the years ended December 31 2022 and 2021, (iii) Statement of Changes in Equity for the years ended December 31, 2022 and December 2021, (iv) Statements of Cash Flows for the years ended December 31, 2022 and 2021, and (v) Notes to Financial Statements.
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101).

* Filed herewith

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Date: February 3, 2023

SCI ENGINEERED MATERIALS, INC.

By: /s/ Jeremiah R. Young

Jeremiah R. Young, Director, and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on the 3rd day of February 2023.

<i>Signature</i>	<i>Title</i>
<u>/s/ Jeremiah R. Young</u> Jeremiah R. Young	Director and Chief Executive Officer (principal executive officer)
<u>/s/ Gerald S. Blaskie</u> Gerald S. Blaskie	Vice President and Chief Financial Officer (principal financial and accounting officer)
<u>Laura F. Shunk*</u> Laura F. Shunk	Chairperson of the Board of Directors
<u>Edward W. Ungar*</u> Edward W. Ungar	Director
<u>John P. Gilliam*</u> John P. Gilliam	Director
<u>Emily Lu*</u> Emily Lu	Director
<u>Charles Wickersham*</u> Charles Wickersham	Director

*By: /s/ Jeremiah R. Young

Jeremiah R. Young, Attorney-in-Fact

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To the Board of Directors and Shareholders
SCI Engineered Materials, Inc.

Report of Independent Registered Public Accounting Firm

Opinion on the Financial Statements

We have audited the accompanying balance sheets of SCI Engineered Materials, Inc. (the “Company”) as of December 31, 2022 and 2021, the related statements of operations, shareholders’ equity, and cash flows for each of the years then ended, and related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2022 and 2021, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2022, in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting 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.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matter

The critical audit matter communicated below is a matter arising from the current period audit of the financial statements that was communicated or required to be communicated to the audit committee and that: (1) relates to accounts or disclosures that are material to the financial statements and (2) involved our especially challenging, subjective, or complex judgments. The communication of the critical audit matter does not alter in any way our opinion on the financial statements, taken as a whole, and we are not, by communicating the critical audit matter below, providing separate opinions on the critical audit matter or on the accounts or disclosures to which it relates.

Realizability of Deferred Tax Assets

Description of the Matter

As described further in Note 10 to the financial statements, the Company assesses the realizability of deferred income tax assets, which represent the tax benefits of future tax deductions, based on available positive and negative evidence and by considering the adequacy of future taxable income from all sources, including prudent and feasible tax planning strategies. The Company assesses the need for a valuation allowance by evaluating both positive and negative evidence that may exist. We identified the realizability of deferred tax assets and the assessment of the need for a valuation allowance as a critical audit matter.

The principal consideration for our determination that the realizability of deferred tax assets is a critical audit matter is that the forecast of future taxable income is an accounting estimate subject to a high level of estimation uncertainty. There is inherent uncertainty and

subjectivity related to management's judgments and assumptions regarding the Company's future taxable income, which are complex in nature and require significant auditor judgment.

How We Addressed the Matter in Our Audit

We obtained an understanding, evaluated the design and operating effectiveness of controls over the Company's process to assess the realizability of the deferred tax assets and measurement of the valuation allowances, including controls over management's review of the significant assumptions described above.

To test the realizability of the deferred tax assets, our audit procedures included, among others, evaluating the methodologies used, the significant assumptions for each type of evidence discussed above, and testing the completeness and accuracy of the underlying data used by the Company in its analysis. We involved income tax specialists and evaluated the nature of each of the deferred tax assets, including their expiration dates and their projected utilization when compared to projections of future taxable income. Additionally, we assessed the reasonableness of the methods, assumptions, and judgments used by management to assess available positive and negative evidence and determine whether a valuation allowance was necessary. Next, we considered management's ability to accurately estimate projected future taxable income by comparing actual results to management's historical estimates and evaluating whether there have been any changes that would affect management's ability to accurately estimate future taxable income and performed sensitivity analyses of the significant assumptions to evaluate the changes in realizability of deferred tax assets that would result from changes in the assumptions. Lastly, we reviewed the Company's income tax disclosures related to the matters described above.

GBQ Partners LLC

We have served as the Company's auditor since 2014.

Columbus, Ohio

February 3, 2023

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SCI ENGINEERED MATERIALS, INC.

BALANCE SHEETS

DECEMBER 31, 2022 AND 2021

ASSETS

	<u>December 31,</u> <u>2022</u>	<u>December 31,</u> <u>2021</u>
Current Assets		
Cash	\$ 3,947,966	\$ 4,140,942
Investments - marketable securities, short term	989,265	—
Accounts receivable		
Trade, less allowance for doubtful accounts of \$15,000	842,647	425,327
Tax - Employee Retention Credit	40,539	105,000
Other	12,653	1,250
Inventories, net	2,177,917	1,073,218
Prepaid expenses	136,134	678,357
Total current assets	<u>8,147,121</u>	<u>6,424,094</u>
Property and Equipment, at cost		
Machinery and equipment	8,584,871	7,949,746
Furniture and fixtures	142,471	132,365
Leasehold improvements	607,156	596,867
Construction in progress	28,708	287,510
	<u>9,363,206</u>	<u>8,966,488</u>
Less accumulated depreciation and amortization	<u>(7,101,573)</u>	<u>(6,809,850)</u>
	<u>2,261,633</u>	<u>2,156,638</u>
Other Assets		
Investment - marketable securities, long term	1,000,000	—
Right of use asset, net	185,072	274,298
Deferred tax asset	151,164	663,820
Other assets	85,138	89,552
Total other assets	<u>1,421,374</u>	<u>1,027,670</u>
TOTAL ASSETS	<u>\$ 11,830,128</u>	<u>\$ 9,608,402</u>

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

SCI ENGINEERED MATERIALS, INC.

BALANCE SHEETS (continued)

DECEMBER 31, 2022 AND 2021

LIABILITIES AND SHAREHOLDERS' EQUITY

	December 31, 2022	December 31, 2021
Current Liabilities		
Finance lease obligations, current portion	\$ 97,367	\$ 96,702
Operating lease obligations, current portion	105,789	97,292
Accounts payable	514,512	250,383
Customer deposits	1,825,595	1,724,556
Accrued compensation	270,168	225,190
Accrued expenses and other	122,065	122,836
Total current liabilities	2,935,496	2,516,959
 Finance lease obligations, net of current portion	 49,149	 146,516
Operating lease obligations, net of current portion	99,834	205,623
Total liabilities	3,084,479	2,869,098
 Shareholders' Equity		
Common stock, no par value, authorized 15,000,000 shares; 4,519,524 and 4,506,269 shares issued and outstanding, respectively	10,618,435	10,573,843
Additional paid-in capital	2,231,807	2,227,078
Accumulated deficit	(4,104,593)	(6,061,617)
Total shareholders' equity	8,745,649	6,739,304
 TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	 \$ 11,830,128	 \$ 9,608,402

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

SCI ENGINEERED MATERIALS, INC.
STATEMENTS OF OPERATIONS
YEARS ENDED DECEMBER 31, 2022 AND 2021

	<u>2022</u>	<u>2021</u>
Revenue	\$ 23,467,030	\$ 13,448,021
Cost of revenue	<u>18,680,075</u>	<u>9,918,766</u>
Gross profit	4,786,955	3,529,255
General and administrative expense	1,549,696	1,280,579
Research and development expense	375,728	235,679
Marketing and sales expense	<u>381,313</u>	<u>235,091</u>
Income from operations	2,480,218	1,777,906
Gain on extinguishment of debt	—	325,300
Interest (income) expense	<u>(19,201)</u>	<u>32,140</u>
Income before provision for income taxes	2,499,419	2,071,066
Income tax expense	<u>542,395</u>	<u>392,242</u>
Net income	1,957,024	1,678,824
Dividends on preferred stock	—	<u>24,152</u>
INCOME APPLICABLE TO COMMON STOCK	<u>\$ 1,957,024</u>	<u>\$ 1,654,672</u>
Earnings per share - basic and diluted (Note 8)		
Income per common share		
Basic	\$ 0.43	\$ 0.37
Diluted	<u>\$ 0.43</u>	<u>\$ 0.37</u>
Weighted average shares outstanding		
Basic	4,515,002	4,495,678
Diluted	<u>4,542,891</u>	<u>4,523,690</u>

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

SCI ENGINEERED MATERIALS, INC.
STATEMENTS OF SHAREHOLDERS' EQUITY
YEARS ENDED DECEMBER 31, 2022 AND 2021

	<u>Convertible Preferred Stock, Series B</u>	<u>Common Stock</u>	<u>Additional Paid-In Capital</u>	<u>Accumulated Deficit</u>	<u>Total</u>
Balance 12/31/2020	\$ 514,438	\$ 10,530,669	\$ 2,246,501	\$ (7,740,441)	\$ 5,551,167
Accretion of cumulative dividends	24,152	—	(24,152)	—	—
Stock based compensation expense (Note 2J)	—	—	4,729	—	4,729
Payment of dividend redemption (Note 8)	(248,766)	—	—	—	(248,766)
Payment of cumulative dividends (Note 8)	(289,824)	—	—	—	(289,824)
Common stock issued (Note 8)	—	43,174	—	—	43,174
Net income	—	—	—	1,678,824	1,678,824
Balance 12/31/2021	\$ —	\$ 10,573,843	\$ 2,227,078	\$ (6,061,617)	\$ 6,739,304
Stock based compensation expense (Note 2J)	—	—	4,729	—	4,729
Common stock issued (Note 8)	—	44,592	—	—	44,592
Net income	—	—	—	1,957,024	1,957,024
Balance 12/31/2022	\$ —	\$ 10,618,435	\$ 2,231,807	\$ (4,104,593)	\$ 8,745,649

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

SCI ENGINEERED MATERIALS, INC.
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2022 AND 2021

	2022	2021
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 1,957,024	\$ 1,678,824
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and accretion	425,391	429,066
Amortization of right of use asset	89,226	83,099
Amortization of patents	4,414	4,414
Stock based compensation	49,321	47,903
Gain on disposal of equipment	(18,321)	(2,522)
Deferred tax asset	512,656	355,497
Gain on extinguishment of debt	—	(325,300)
Inventory reserve	(14,987)	1,200
Changes in operating assets and liabilities:		
Accounts receivable	(364,262)	(72,107)
Inventories	(1,089,711)	105,941
Prepaid expenses	542,223	(547,023)
Other assets	—	2,658
Accounts payable	264,129	103,099
Operating lease obligations	(97,292)	(88,918)
Accrued expenses and customer deposits	138,344	834,717
Net cash provided by operating activities	<u>2,398,155</u>	<u>2,610,548</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds on sale of equipment	31,149	18,091
Purchases of marketable securities	(1,989,265)	—
Purchases of property and equipment	(536,313)	(706,242)
Net cash used in investing activities	<u>(2,494,429)</u>	<u>(688,151)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments of dividend redemption on preferred stock	—	(248,766)
Payments of cumulative dividends on preferred stock	—	(289,824)
Principal payments on finance lease obligations and notes payable	(96,702)	(160,416)
Net cash used in financing activities	<u>(96,702)</u>	<u>(699,006)</u>
NET (DECREASE) INCREASE IN CASH	<u>\$ (192,976)</u>	<u>\$ 1,223,391</u>
CASH - Beginning of year	<u>4,140,942</u>	<u>2,917,551</u>
CASH - End of period	<u>\$ 3,947,966</u>	<u>\$ 4,140,942</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the year for:		
Interest	\$ 8,600	\$ 12,210
Income taxes	24,935	36,745
SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Increase in asset retirement obligation	6,900	6,900

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

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 1. Business Organization and Purpose

SCI Engineered Materials, Inc. ("SCI", "we" or the "Company"), an Ohio corporation, was incorporated in 1987. The Company operates in one segment as a global supplier and manufacturer of advanced materials for Physical Vapor Deposition ("PVD") thin film applications. The Company is focused on markets within the PVD industry including Aerospace, Automotive, Defense, Glass, Optical Coatings, and Solar. Substantially, all revenues are generated from customers with multi-national operations. The Company develops innovative customized solutions enabling commercial success through collaboration with end users and Original Equipment Manufacturers.

Note 2. Summary of Significant Accounting Policies

A. Cash - The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash.

B. Investments in marketable securities – The Company's investments in marketable securities consist of corporate and government bonds and have been classified as held-to-maturity. The Company has the intent and ability to hold to maturity and the securities are reported at amortized cost. The Company considers those investments which will mature in the next twelve months, including interest receivable on long-term bonds, as current assets. The remaining investments are considered non-current assets which the Company intends to hold longer than twelve months. The Company periodically evaluates our investments for impairment.

C. Fair Value of Financial Instruments - The estimated fair value of amounts reported in the financial statements have been determined using available market information and valuation methodologies, as applicable (see Note 11).

D. Concentrations of Credit Risk - The Company's cash balances, which are at times more than federally insured levels, are maintained at a large regional bank, and are continually monitored to minimize the risk of loss. The Company grants credit to most customers, who are varied in terms of size, geographic location, and financial strength. Customer balances are continually monitored to minimize the risk of loss.

The Company's two largest customers accounted for 73% and 15% of total revenue in 2022. These two customers represented 59% of the accounts receivable trade balance at December 31, 2022. The Company expects to collect all outstanding accounts receivable as of December 31, 2022, from these customers.

The Company's two largest customers accounted for 63% and 21% of total revenue in 2021. These two customers represented 43% of the accounts receivable trade balance at December 31, 2021. The Company subsequently collected all outstanding accounts receivable as of December 31, 2021, from these customers.

E. Accounts Receivable - The Company extends unsecured credit to customers under normal trade agreements which require payment within 30-60 days. The Company does not charge interest on delinquent trade accounts receivable. Unless specified by the customer, payments are applied to the oldest unpaid invoice. Accounts receivable are presented at the amount billed.

Management estimates an allowance for doubtful accounts, which was \$15,000 as of December 31, 2022, and 2021. This estimate is based upon management's assessment of the expected collectability of specific customer accounts and the aging of the accounts receivable. Specific accounts are charged directly to the reserve or bad debt expense when management obtains evidence of a customer's

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 2. Summary of Significant Accounting Policies (continued)

insolvency or otherwise determines that the account is uncollectible. There was no bad debt expense during 2022 and 2021.

F. Inventories - Inventories are stated at the lower of cost or net realizable value on an acquired or internally produced lot basis, and consist of raw materials, work-in-process, and finished goods. Cost includes material, labor, freight and applied overhead. Inventory reserves are established for obsolete inventory, lower of cost or net realizable value, and excess inventory quantities based on management's estimate of net realizable value. The Company had an inventory reserve of \$10,431 and \$25,418 at December 31, 2022, and 2021, respectively.

G. Property and Equipment - Property and equipment are carried at cost. Depreciation is provided using the straight-line method based on the estimated useful lives of the assets. Useful lives range from three years on computer equipment to sixteen years on certain equipment. Leasehold improvements are amortized over the shorter of the estimated useful life or the term of the lease. Depreciation expense totaled \$425,391 and \$429,066 for the years ended December 31, 2022, and 2021, respectively. Expenditures for renewals and betterments are capitalized and expenditures for repairs and maintenance are charged to operations as incurred.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the fair value is less than the carrying amount of the asset, a loss is recognized for the difference. During 2022, various assets totaling \$83,596 with a net book value of \$7,201 were considered impaired. During 2021, various assets totaling \$62,166 with a net book value of \$15,569 were considered impaired. This impairment is offset against gain on disposal of equipment in the Statement of Operations.

H. Intangible Assets - The Company reviews intangible assets for impairment and performs detailed testing whenever impairment indicators are present. If necessary, an impairment loss is recorded for the excess of carrying value over fair value. There were no intangible assets considered impaired during 2022 or 2021.

Costs incurred to secure patents have been capitalized and amortized over the life of the patents. Cost and accumulated amortization of the patents at December 31, 2022, was \$85,516 and \$17,596 respectively, and cost and accumulated amortization of the patents at December 31, 2021, was \$85,516 and \$13,182, respectively. Amortization expense related to patents was \$4,414 for the years ended December 31, 2022, and 2021. Amortization expense is expected to be at least \$4,414 for each of the next five years.

I. Revenue Recognition - The Company enters into contracts with its customers that generally represent purchase orders specifying general terms and conditions, order quantities and per unit product prices. The Company has determined that each unit of product purchased represents a separate performance obligation. The Company satisfies its performance obligations and recognizes revenue at a point in time when control of a unit of product is transferred to the customer. Revenue is measured as the amount of consideration the Company expects to receive in exchange for transferring products. For most product sales, transfer of control occurs when the products are shipped from the Company's manufacturing facility to the customer. The cost of delivering products to the Company's customers is recorded as a component of cost of products sold. Those costs may include the amounts paid to a third party to deliver the products. Any freight costs billed to and paid by a customer are included in revenue.

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 2. Summary of Significant Accounting Policies (continued)

The Company considers collectability of amounts due under a contract to be probable upon inception of a sale based on an evaluation of the credit worthiness of each customer. The Company sells its products typically under agreements with payment terms of 30-60 days. The Company does not typically include extended payment terms or significant financing components in contracts with customers. The majority of the Company's contracts have an obligation to transfer products within one year. Thus, the Company elects to use the practical expedient where incremental cost of obtaining a contract, such as commissions, is expensed when incurred because the amortization period for those costs is one year or less. The Company treats shipping and handling activities that occur after control of the product transfers as fulfillment activities, and therefore, does not account for shipping and handling costs as a separate performance obligation. Customer deposits are funds received in advance from customers and are recognized as revenue when the Company has transferred control of product to the customer. Product revenues are recognized upon shipment of goods as the customer has assumed the significant risks and rewards of ownership and the Company is entitled to payment at this point. Service revenues are recognized upon completion as the customer cannot realize the benefit of the service until fully completed.

During 2022 and 2021, revenue from the PVD industry exceeded 99% of total revenue. The balance of the revenue was from the solar and thin film battery markets. The top two customers represented 88% and 84% of total revenue during 2022 and 2021, respectively. International shipments resulted in 1% and 2% of total revenue for 2022 and 2021, respectively.

J. Stock Based Compensation - Compensation cost for all stock-based awards is based on the grant date fair value and is recognized over the required service (vesting) period. Non cash stock-based compensation expense was \$49,321 and \$47,903 for the years ended December 31, 2022, and 2021, respectively. Non cash stock-based compensation expense includes \$29,968 and \$29,963 for stock grants awarded to the non-employee board members during 2022 and 2021. Unrecognized compensation expense was \$1,576 as of December 31, 2022, and will be recognized through April 2023. There was no tax benefit recorded for this compensation cost as the expense primarily relates to incentive stock options that do not qualify for a tax deduction until, and only if, a qualifying disposition occurs.

K. Research and Development - Research and development costs are expensed as incurred. Research and development expense for the years ended December 31, 2022 and 2021, was \$375,728 and \$235,679, respectively. Consistent with our growth strategy, we have identified niche markets that can benefit from our expertise in custom powder solutions, such as near-infrared doped phosphors and short-wave infrared applications. These applications enable extended life of phosphors for specific nighttime identification needs of defense personnel and first responders.

New initiatives are also being pursued that utilize our vacuum hot presses, cold isostatic press, and kilns for increased production and development projects, including diffusion bonding. We recently manufactured and sold conductive metal oxides for direct current sputtering of Tungsten Oxide and Molybdenum Oxide materials. We continue to invest in developing new products for all our markets including specialty bonding processes for Aerospace customers. Those products continue to require research and development expense to accelerate time to market.

L. Income Taxes – Income taxes are accounted for under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, we determine deferred tax assets and liabilities on the basis of the differences between the financial statement and tax bases of assets and liabilities by using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 2. Summary of Significant Accounting Policies (continued)

We recognize deferred tax assets to the extent that we believe that these assets are more likely than not to be realized. In making such a determination, we consider all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax-planning strategies, and results of recent operations. If we determine that we would not be able to realize our deferred tax assets in the future, we would make an adjustment to the deferred tax asset valuation allowance, which would increase the provision for income taxes.

M. Use of Estimates - The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventory allowances, property and equipment depreciable lives, patents and licenses useful lives, revenue recognition, tax valuation allowance, stock-based compensation and assessing changes in which impairment of certain long-lived assets may occur. Actual results could differ from those estimates.

N. Recent Accounting Pronouncements –

In June 2016, the FASB issued ASU No. 2016-13 “Credit Losses - Measurement of Credit Losses on Financial Instruments.” ASU No. 2016-13 significantly changes how entities will measure credit losses for most financial assets, including accounts and notes receivables, by replacing today’s “incurred loss” approach with an “expected loss” model under which allowances will be recognized based on expected rather than incurred losses. ASU No. 2016-13 will become effective for the Company in the first quarter of 2023. The Company is evaluating the impact that the adoption of this update will have on its financial statements; however, it is not expected to be material

O. Employee Retention Credit (“ERC”) - The Company qualified for federal government assistance through ERC provisions of the Consolidated Appropriations Act of 2021 during 2021 in the amount of \$255,507 for the first quarter of 2021, \$151,701 for the second quarter of 2021, and \$153,713 for the third quarter of 2021. The purpose of the ERC was to encourage employers to keep employees on the payroll, even if they are not working during the covered period because of the coronavirus outbreak. This credit was recorded in the Statement of Operations as an offset to payroll costs in their respective expense lines. A balance of \$40,539 and \$105,000 appears as a tax receivable on the balance sheets at December 31, 2022, and 2021, respectively.

Note 3. Investments

As of December 31, 2022, the Company held investments in corporate and government bonds that are required to be measured for disclosure purposes at fair value on a recurring basis. The bonds are considered held-to-maturity and are recorded at amortized cost on the balance sheet. These investments are considered level 2 as detailed in the table below. The Company considers investments which will mature in the next twelve months and interest receivable on the long-term bonds as current assets. The remaining investments are considered non-current assets including the investment in marketable securities which the Company intends to hold longer than twelve months. The fair value of these investments was estimated using recently executed transactions and market price quotations. The amortized cost and the fair value of these investments, and the related gross unrealized gains and losses, were as follows:

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 3. Investments (continued)

As of December 31, 2022	Level	Cost	Unrealized gains/(losses)	Fair value
Bonds	2	\$ 1,989,265	\$ 741	\$ 1,990,006

At December 31, 2022, the length of time until maturity of the bonds currently owned ranged from 5 months to 23 months.

Note 4. Inventories

Inventories consist of the following at December 31:

	December 31, 2022	December 31, 2021
Raw materials	\$ 1,375,669	\$ 440,759
Work-in-process	528,631	549,369
Finished goods	284,048	108,508
	2,188,348	1,098,636
Inventory reserve	(10,431)	(25,418)
	<u>\$ 2,177,917</u>	<u>\$ 1,073,218</u>

Note 5. Notes Payable

On April 17, 2020, the Company entered into an unsecured promissory note under the Paycheck Protection Program (the "PPP"), with a principal amount of \$325,300. Under the terms of the CARES Act, PPP loan recipients were eligible to apply for, and be granted, forgiveness for all or a portion of loans granted. Such forgiveness was subject to limitations and ongoing rulemaking by the SBA, based on the use of loan proceeds for payroll costs and mortgage interest, rent or utility costs and the maintenance of employee and compensation levels. The Company applied for forgiveness of the entire amount of the loan during the fourth quarter of 2020, and the SBA approved the Forgiveness Application in full during the first quarter of 2021. This amount is included in the Statement of Operations as gain on extinguishment of debt in 2021.

The Company commenced a line of credit with Fifth Third Bank for \$1 million during August of 2021 and renewed in August 2022. The line of credit bears interest equal to the rate of interest per annum established by Fifth Third Bank as its Prime Rate. This line of credit has a maturity date of August 29, 2023. No amounts were drawn on this line of credit during 2021 or 2022.

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 6. Operating Lease Obligations

The Company entered into an operating lease with a third party on March 18, 2014 for its headquarters in Columbus, Ohio. The terms of the lease include monthly payments ranging from \$9,400 to \$9,700 with an expiration date of November 30, 2024. The Company has the option to extend the lease period for an additional five years beyond the expiration date. There are no restrictions or covenants associated with the lease. The lease costs were approximately \$112,600 and \$110,400 during the years ended December 31, 2022 and 2021, respectively.

The following is a maturity analysis, by year, of the annual undiscounted cash outflows of the operating lease liabilities as of December 31, 2022:

2023	\$ 114,857
2024	102,550
Total minimum lease payments	217,407
Less debt discount	11,784
Total operating lease obligations	<u>\$ 205,623</u>
Operating cash outflows from operating leases	\$97,292
Weighted average remaining lease term – operating leases	1.9 years
Weighted average discount rate – operating leases	5.5 %

Note 7. Finance Leases

The Company also leases certain equipment under finance leases. Future minimum lease payments, by year, with the present value of such payments, as of December 31, 2022, are shown in the following table.

2023	\$ 101,675
2024	49,859
Total minimum lease payments	151,534
Less amount representing interest	5,018
Present value of minimum lease payments	146,516
Less current portion	97,367
Finance lease obligations, net of current portion	<u>\$ 49,149</u>

The equipment under finance lease at December 31 is included in the accompanying balance sheets as follows:

	December 31, 2022	Dec. 31, 2021
Machinery and equipment	\$ 385,923	\$ 385,923
Less accumulated depreciation and amortization	104,376	65,783
Net book value	<u>\$ 281,547</u>	<u>\$ 320,140</u>

These assets are amortized over a period of ten years using the straight-line method and amortization is included in depreciation expense.

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 7. Finance Leases (continued)

The finance leases are structured such that ownership of the leased asset reverts to the Company at the end of the lease term. Accordingly, leased assets are depreciated using the Company's normal depreciation methods and lives. Ownership of certain assets was transferred to the Company in accordance with the terms of the leases and these assets have been excluded from the leased asset disclosure above.

Note 8. Common and Preferred Stock

Common Stock

The non-employee board members received compensation of 8,755 and 9,165 shares of common stock of the Company during 2022 and 2021, respectively. The stock had an aggregate value of \$29,967 and \$29,963 for the year ended December 31, 2022, and 2021, respectively, and was recorded as non-cash stock compensation expense in the financial statements.

Employees received compensation of 4,500 and 4,804 aggregate shares of common stock of the Company during 2022 and 2021, respectively, which had an aggregate value of \$14,625 and \$13,211, respectively, and was recorded as noncash stock-based compensation expense in the financial statements. In addition, during 2021, a total of 34,733 stock options were exercised by management.

Preferred Stock

Shares of preferred stock authorized and outstanding at December 31, 2022 and 2021, were as follows:

	2022 Shares Authorized	2022 Shares Outstanding	2021 Shares Authorized	2021 Shares Outstanding
Cumulative Preferred Stock	10,000	—	10,000	—
Voting Preferred Stock	125,000	—	125,000	—
Cumulative Non-Voting Preferred Stock (a)	125,000	—	125,000	—

(a) Includes 700 shares of Series A Preferred Stock and 100,000 shares of Convertible Series B Preferred Stock authorized for issuance.

In January 1996, the Company completed an offering of 24,152 shares of \$10 stated value 1995 Series B 10% cumulative non-voting convertible preferred stock (a total of 70,000 shares were offered and 24,152 were sold). The shares were convertible to common shares at the rate of \$5.00 per share. A dividend payment of \$24,152 was made to preferred shareholders of record during the second quarter of 2021. The Board of Directors voted in November 2021 to authorize full redemption of 24,152 shares of the Company's Convertible Preferred Stock, Series B ("Series B") effective December 31, 2021. This involved cash payments of \$248,766 (\$10.30 per share, which included a 3% premium to the stated value of \$10 per share), plus unpaid annual dividends of \$265,672 (\$11.00 per share).

Earnings Per Share

Basic income per share is calculated as income available to common shareholders divided by the weighted average of common shares outstanding. Diluted earnings per share is calculated as diluted income available to common shareholders divided by the diluted weighted average number of common shares outstanding. Diluted weighted average number of common shares gives effect to all dilutive

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 8. Common and Preferred Stock (continued)

potential common shares outstanding during the period using the treasury stock method and convertible preferred stock using the if-converted method. Diluted earnings per share exclude all diluted potential shares if their effect is anti-dilutive.

Following is a summary of employee and director outstanding stock options outstanding and preferred stock, Series B at December 31.

	2022	2021
Options	41,304	41,304

The following is provided to reconcile the earnings per share calculations:

	Year ended December 31,	
	2022	2021
Income applicable to common stock	\$ 1,957,024	\$ 1,654,672
Weighted average common shares outstanding - basic	4,515,002	4,495,678
Effect of dilution - stock options	27,889	28,012
Weighted average shares outstanding - diluted	4,542,891	4,523,690

Note 9. Stock Option Plans

On June 10, 2011, shareholders approved the SCI Engineered Materials, Inc. 2011 Stock Incentive Plan (the "2011 Plan"). The Company adopted the 2011 Plan as incentive to key employees, directors, and consultants under which options to purchase up to 250,000 shares of the Company's common stock may be granted, subject to the execution of stock option agreements. Incentive stock options may be granted to key employees of the Company and non-statutory options may be granted to directors who are not employees and to consultants and advisors who render services to the Company. Options may be exercised for periods up to 10 years from the date of grant at prices not less than 100% of fair market value on the date of grant. As of December 31, 2022, there were 21,061 stock options outstanding from the 2011 Plan which expire in May 2028.

On June 9, 2006, shareholders approved the Superconductive Components, Inc. 2006 Stock Incentive Plan (the "2006 Plan"). The Company adopted the 2006 Plan as incentive to key employees, directors, and consultants under which options to purchase up to 600,000 shares of the Company's common stock may be granted, subject to the execution of stock option agreements. Incentive stock options may be granted to key employees of the Company and non-statutory options may be granted to directors who are not employees and to consultants and advisors who render services to the Company. Options may be exercised for periods up to 10 years from the date of grant at prices not less than 100% of fair market value on the date of grant. The 2006 Plan expired in 2016 and no additional stock options may be granted. As of December 31, 2022, there were 20,243 stock options outstanding from the 2006 Plan which expire in November 2024.

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 9. Stock Option Plans (continued)

The cumulative status at December 31, 2022 and 2021 of options granted and outstanding, as well as options which became exercisable in connection with the Stock Option Plans is summarized as follows:

Employee Stock Options

	Stock Options	Weighted Average Exercise Price
Outstanding at January 1, 2021	76,037	\$ 1.03
Exercised	(34,733)	1.00
Outstanding at December 31, 2021	41,304	\$ 1.05
Outstanding at December 31, 2022	41,304	\$ 1.05
Options exercisable at December 31, 2021	27,418	\$ 0.95
Options exercisable at December 31, 2022	34,361	\$ 1.01

Information related to the weighted average fair value of nonvested stock options for the year ended December 31, 2022, is as follows:

	Stock Options	Weighted Average Exercise Price
<u>Employee Stock Options</u>		
Nonvested options at January 1, 2022	20,829	\$ 1.25
Vested	(13,886)	1.25
Nonvested options at December 31, 2022	6,943	\$ 1.25

Exercise prices for options outstanding ranged from \$0.84 to \$1.25 and the weighted average option price was \$1.05 at December 31, 2022, and 2021, respectively. The weighted average remaining contractual life was 3.6 years and 4.6 years at December 31, 2022, and 2021, respectively.

Note 10. Income Taxes

Deferred tax assets and liabilities result from temporary differences in the recognition of income and expense for tax and financial reporting purposes. Significant components of the Company's deferred tax assets and liabilities are as follows at December 31.

	2022	2021
Deferred tax assets (liabilities)		
NOL carryforwards	\$ 8,917	\$ 434,566
General business credits carryforwards	388,776	389,741
Stock based compensation	155,707	149,389
Allowance for doubtful accounts	3,162	3,162
Reserve for obsolete inventories	2,199	5,358
Reserve for asset retirement	18,797	17,342
Property and equipment	(426,394)	(335,738)
Total	<u>\$ 151,164</u>	<u>\$ 663,820</u>

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 10. Income Taxes (continued)

A valuation allowance of \$0 has been recorded against the realizability of the net deferred tax asset of \$151,164 at December 31, 2022, and \$663,820 at December 31, 2021.

As of each reporting date, management considers new evidence, both positive and negative, that could affect its view of the future realization of deferred tax assets. As of December 31, 2022, management determined that there is sufficient positive evidence to conclude that it is more likely than not that deferred taxes of \$151,164 are realizable in part because we achieved six consecutive years of pretax income, expect profits to continue for the foreseeable future and implemented new efficiencies in the Company's manufacturing process. Accordingly, we determined that no valuation allowance was necessary at December 31, 2022.

The Company had net operating loss carryforwards available for federal and state tax purposes of approximately \$42,000 and \$2,100,000 at December 31, 2022, and 2021, respectively, which expire in varying amounts through 2042. The deferred tax asset of \$151,164 is expected to be realized within the next three years.

For the years ended December 31, 2022, and 2021, a reconciliation of the statutory rate and effective rate for the provisions for income taxes consists of the following:

	Percentage	
	2022	2021
Federal statutory rate	21.0 %	21.0 %
State/city tax	1.2	1.8
Non-deductible expense	0.2	0.2
PPP tax exempt income	—	(3.4)
Valuation allowance	(0.7)	(0.4)
Effective rate	21.7 %	19.2 %

Components of the income tax provision are as follows:

	2022	2021
Current	\$ 29,739	\$ 36,745
Deferred:		
NOL utilization/expiration	425,649	351,585
General business credits	965	(8,563)
Other temporary differences	86,042	12,475
Total	\$ 542,395	\$ 392,242

The Company follows guidance issued by the Financial Accounting Standards Board ("FASB ASC 740") with respect to accounting for uncertainty in income taxes. A tax position is recognized as a benefit only if it is "more-likely-than-not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than fifty percent likely of being realized on examination. For tax positions not meeting the "more-likely-than-not" test, no tax benefit is recorded.

The Company has no unrecognized tax benefits under guidance related to tax uncertainties. The Company does not anticipate the unrecognized tax benefits will significantly change in the next twelve months. Any tax penalties or interest expense will be recognized in income tax expense. No interest and penalties related to unrecognized tax benefits were accrued at December 31, 2022, and 2021.

SCI ENGINEERED MATERIALS, INC.
NOTES TO FINANCIAL STATEMENTS

Note 10. Income Taxes (continued)

The Company files income tax returns in the U.S. federal jurisdiction and various state and local jurisdictions. The Company is open to federal and state tax audits until the applicable statute of limitations expire. There are currently no federal or state income tax examinations underway for the Company. The tax years 2019 through 2022 remain open to examination by the major taxing jurisdictions in which the Company operates.

Note 11. Fair Value of Financial Instruments

The fair value of financial instrument represents the price that would be received to sell an asset or paid to transfer a liability (an exit price), and not the price that would be paid to acquire an asset or received to assume a liability (an entry price). Significant differences can arise between the fair value and carrying amount of financial instruments that are recognized at historical cost amounts.

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

- The fair values of cash and cash equivalents, trade receivables, accounts payable, short-term notes payable and finance lease obligations and current maturities of long-term notes payable and finance lease obligations: Amounts are reported at cost, approximate fair value based on the short-term nature and high credit quality of these financial instruments.
- Long-term note payable and finance lease obligations: Amounts reported in the balance sheet approximate fair value as the interest rates on the obligations range from 4.2% to 4.8%, which approximates current fair market rates.

Note 12. Asset Retirement Obligation

Included in machinery and equipment is various production equipment, which per the Company's building lease is required to be removed upon termination of the related lease. Included in accrued expenses in the accompanying balance sheet is the asset retirement obligation that represents the expected present value of the liability to remove this equipment. There are no assets that are legally restricted for purposes of settling this asset retirement obligation.

Following is a reconciliation of the aggregate retirement liability associated with the Company's obligation to dismantle and remove the machinery and equipment associated with its lease:

Balance at January 1, 2021	\$ 75,368
Increase in present value of the obligation (accretion expense in the corresponding amount charged against earnings)	6,900
Balance at December 31, 2021	\$ 82,268
Increase in present value of the obligation (accretion expense in the corresponding amount charged against earnings)	6,900
Balance at December 31, 2022	\$ 89,168

Description of the Company's Common Stock Registered
Under Section 12 of the Exchange Act of 1934

The following summary of SCI Engineered Materials, Inc.'s common stock is based on and qualified by the Company's Restated Code of Regulations ("Regulations") and Second Amended Articles of Incorporation (the "Amended Articles of Incorporation").

The Company's Amended Articles of Incorporation authorize the issuance of 15,000,000 shares of Common Stock, 10,000 shares of Cumulative Preferred Stock, 125,000 shares of Voting Preferred Stock, and 125,000 shares of Non-Voting Preferred Stock, all of which are without par value. There are no shares of Cumulative Preferred Stock and Voting Preferred Stock currently outstanding.

The holders of Common Stock, Cumulative Preferred Stock and Voting Preferred Stock are entitled to one vote per share on each matter submitted to a vote of shareholders. The holders of Non-Voting Preferred Stock are not entitled to vote. The Company's Board of Directors (the "Board") is not classified, and each member is elected annually. The Company's Regulations provide for candidates receiving the greatest number of votes to be elected.

The holders of Cumulative Preferred Stock, Voting Preferred Stock and Non-Voting Preferred Stock have the right to receive dividends prior to the payment of dividends on the Common Stock. The Board has the power to determine certain terms relative to any Preferred Stock to be issued, such as the power to establish different series and to set dividend rates, the dates of payment of dividends, the cumulative dividend rights and dates, redemption rights and prices, sinking fund requirements, restrictions on the issuance of such shares or any series thereof, preference, if any, in the event of liquidation. Also, the Board may fix such other express terms as may be permitted or required by law. In the event of any liquidation or dissolution, the holders of the Common Stock are entitled to receive as a class, pro rata, the residue of the assets after payment of the liquidation price to the holders of Preferred Stock.

In January 1996, the Company completed an offering of 24,152 shares of \$10 stated value 1995 Series B 10% cumulative non-voting convertible preferred stock (a total of 70,000 shares were offered and 24,152 were sold). The shares were convertible to common shares at the rate of \$5.00 per share. A dividend payment of \$24,152 was made to preferred shareholders of record during the second quarter of 2021. The Board of Directors voted in November 2021 to authorize full redemption of 24,152 shares of the Company's Convertible Preferred Stock, Series B ("Series B") effective December 31, 2021. This involved cash payments of \$248,766 (\$10.30 per share, which included a 3% premium to the stated value of \$10 per share), plus unpaid annual dividends of \$265,672 (\$11.00 per share).

The common stock is traded on OTC Markets' OTCQB market under the trading symbol "SCIA".

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statements No.333-97583, No. 333-67212 and No. 333-136694 on Forms S-8 of SCI Engineered Materials, Inc. of our report dated February 3, 2023, relating to the financial statements, appearing in this Annual Report on Form 10-K.

GBQ Partners LLC

Columbus, Ohio
February 3, 2023

POWER OF ATTORNEY

Each of the undersigned officers and/or directors of SCI Engineered Materials, Inc., an Ohio corporation (the "Company"), hereby appoints Jeremiah R. Young and Michael A. Smith as his or her true and lawful attorneys-in-fact, or any of them individually with power to act without the other, as his or her true and lawful attorney-in-fact, in his or her name and on his or her behalf, and in any and all capacities stated below, to sign and to cause to be filed with the Securities and Exchange Commission the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2022, and any and all amendments thereto, hereby granting unto said attorneys, and to each of them, full power and authority to do and perform in the name and on behalf of the undersigned, in any and all such capacities, every act and thing whatsoever necessary to be done in and about the premises as fully as each of the undersigned could or might do in person, hereby granting to each such attorney full power of substitution and revocation, and hereby ratifying all that any such attorney or his substitute may do by virtue hereof.

IN WITNESS WHEREOF, the undersigned have executed this Power of Attorney in counterparts, if necessary, effective as of February 3, 2023.

*Signature**Title*

/s/ Jeremiah R. Young
Jeremiah R. Young

President and Chief Executive Officer
(principal executive officer)

/s/ Gerald S. Blaskie
Gerald S. Blaskie

Vice President and Chief Financial Officer
(principal financial and accounting officer)

/s/ Laura F. Shunk
Laura F. Shunk

Chairperson of the Board of Directors

/s/ John P. Gilliam
John P. Gilliam

Director

/s/ Emily Lu
Emily Lu

Director

/s/ Edward W. Ungar
Edward W. Ungar

Director

/s/ Charles Wickersham
Charles Wickersham

Director

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Jeremiah R. Young, certify that:

1. I have reviewed this annual report on Form 10-K of SCI Engineered Materials, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, which involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 3, 2023

/s/ Jeremiah R. Young

Jeremiah R. Young

President and Chief Executive Officer (Principal Executive Officer)

**CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Gerald S. Blaskie certify that:

1. I have reviewed this annual report on Form 10-K of SCI Engineered Materials, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, which involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 3, 2023

/s/ Gerald S. Blaskie

Gerald S. Blaskie

Vice President and Chief Financial Officer

(Principal Financial and Accounting Officer)

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of SCI Engineered Materials, Inc. (the "Company") on Form 10-K for the period ending December 31, 2022, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jeremiah R. Young, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Jeremiah R. Young

Jeremiah R. Young
President and Chief Executive Officer of
SCI Engineered Materials, Inc.
February 3, 2023

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of SCI Engineered Materials, Inc. (the "Company") on Form 10-K for the period ending December 31, 2022, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gerald S. Blaskie, Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Gerald S. Blaskie

Gerald S. Blaskie

Vice President and Chief Financial Officer of
SCI Engineered Materials, Inc.

February 3, 2023