

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

BION ENVIRONMENTAL TECHNOLOGIES INC
Form 10QSB
May 01, 2003

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-QSB

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2003

OR

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

Commission file number 001-19333

Bion Environmental Technologies, Inc.

(Exact name of registrant as specified in its charter)

Colorado

84-1176672

(State or other jurisdiction of
incorporation or organization)

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

18 East 50th Street 10th Floor N.Y., N.Y.

10022

(Address of principal executive offices)

(Zip Code)

(212) 758-6622

(Registrant's telephone number, including area code)

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

As of April 30, 2003 the issuer had outstanding 5,276,802 shares of common stock. This includes 1,900,000 shares held by a majority-owned subsidiary of the registrant and 91,439 shares of common stock held in trust.

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

BION ENVIRONMENTAL TECHNOLOGIES, INC.

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

QUARTERLY REPORT ON FORM 10-QSB

TABLE OF CONTENTS

PART I	3
Item 1. Financial Statements	3
Unaudited consolidated balance sheet as of March 31, 2003	4
Unaudited consolidated statements of operations for the three and nine months ended March 31, 2003 and 2002	5
Unaudited consolidated statements of cash flows for the nine months ended March 31, 2003 and 2002	6
Notes to unaudited consolidated financial statements	7
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	15
Item 3. Controls and Procedures	22
PART II	22
Item 1. Legal Proceedings	22
Item 5. Other Information	23
Item 6. Exhibits and Reports on Form 8-K	23
Signatures	24
Certifications	25

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Item 1. Financial Statements

This Form 10-QSB has not been reviewed by BDO Seidman, LLP, our independent certified public accountants, as required by Item 310(b) of Regulation S-B. BDO Seidman, LLP has not performed the review because they have not yet reviewed the impact on the Company's accounts and operations of the various items disclosed in our Report on Form 8-K dated February 7, 2003. We are not aware of any dispute with BDO Seidman, LLP as to any accounting matters. In addition, we owe approximately \$125,000 to BDO Seidman, LLP, which must be paid or otherwise resolved in order to eliminate independence issues prior to any review or audit of our financial statements.

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Unaudited Consolidated Balance Sheet
As of March 31, 2003

ASSETS

Current assets:

Cash and cash equivalents	\$ 3,218
Accounts receivable, net of allowance for doubtful accounts of \$2,000	4,540
Inventory	98,608
Prepaid expenses and other current assets	50,804
Total current assets	157,170

Property and equipment, net	190,605
Claims receivable	1,339,154
Other assets	157,000

Total assets	\$ 1,843,929
	=====

LIABILITIES AND STOCKHOLDERS' DEFICIT

Current liabilities:

Accounts payable	\$ 795,353
Accrued expenses	129,102
Advances from affiliates	284,500
Capital lease obligation	1,020

Total current liabilities	1,209,975

Deferred compensation	549,185

Total liabilities	1,759,160

Minority interest 401,232

Commitments and contingencies

Stockholders' Deficit:

Preferred Stock, \$.01 par value, 10,000 shares authorized, -0- shares issued and outstanding	-
Common stock, no par value, 100,000,000 shares authorized, 4,184,791 shares issued and 4,093,352 outstanding (this does not include 1,095,730 shares held by Centerpoint which will be distributed to Bion and subsequently cancelled)	-
Additional paid in capital	59,402,577
Accumulated deficit	(58,898,563)
Treasury stock, at cost, 91,439 shares of common stock	(820,477)

Total stockholders' deficit	(316,463)

Total liabilities and stockholders' deficit	\$ 1,843,929
	=====

See notes to consolidated financial statements

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

4

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Unaudited Consolidated Statements of Operations

	Three Months Ended March 31,		Nine M M
	2003	2002	2003
Revenue:			
Soil sales	\$ -	\$ 21,245	\$ 109,26
Cost of soil	191,022	160,418	578,13
Gross loss	(191,022)	(139,173)	(468,87
Expenses:			
General and administrative (excluding non-cash charges for services and compensation of \$37,494 and \$4,252,599 for the three months ended March 31, 2003 and 2002, respectively and \$29,571 and \$4,753,229 for the nine months ended March 31, 2003 and 2002, respectively)	440,467	673,086	1,804,66
Research and development	180,964	219,062	516,15
Non-cash charges for services and compensation	37,494	4,252,599	29,57
	658,925	5,144,747	2,350,39
Operating loss	(849,947)	(5,283,920)	(2,819,26
Other income and (expense):			
Interest expense (including non-cash interest charges of \$0 and \$1,421,048 for the three months ended March 31, 2003 and 2002, respectively and \$2,250 and \$2,539,766 for the nine months ended March 31, 2003 and 2002, respectively)	(110)	(6,082,428)	(2,54
Interest income	1,031	11,928	8,82
Other income, net	67,425	4,496	46,81
	68,346	(6,066,004)	53,08
Net loss before minority interest	(781,601)	(11,349,924)	(2,766,17
Minority interest	43,850	39,631	39,86

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Net loss and comprehensive loss	\$ (737,751)	\$ (11,310,293)	\$ (2,726,318)
	=====	=====	=====
Basic and diluted loss per common share:			
Net loss per common share	\$ (0.18)	\$ (3.06)	\$ (0.66)
	=====	=====	=====
Weighted-average number of common shares outstanding, basic and diluted loss	4,093,352	3,702,218	4,109,469
	=====	=====	=====

See notes to consolidated financial statements

5

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Unaudited Consolidated Statements of Cash Flows

	Nine Months End March 31,	
	----- 2003 -----	----- 2002 -----
Cash flows from operating activities:		
Net loss	\$ (2,726,318)	\$ (1,000,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Minority interest in net loss of subsidiary	(39,861)	
Depreciation and amortization	62,114	
Beneficial conversion feature amortized to interest expense	-	
Gain on disposal of assets	(24,272)	
Amortization of debt discount	-	
Amounts owed to Trust	487,500	
Reduction in value of Trust	(459,287)	
Interest expense for amounts owed to Trust	2,250	
Reduction of note receivable for consulting services	-	
Compensation charge from variable options	-	
Non-cash charges for equity instruments issued for compensation and services	(891)	
Changes in:		
Accounts receivable	12,755	
Note receivable	(3,008)	
Inventory	(30,968)	
Prepaid expenses and other current assets	97,195	
Deposits and other	56,399	
Accounts payable	471,416	
Accrued expenses	73,950	
	-----	-----
Net cash used in operating activities	(2,021,026)	(1,000,000)
Cash flows from investing activities:		

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Proceeds from sale of assets	44,554	
Purchases of property and equipment	(116,152)	
Business acquisition, net of cash acquired	-	

Net cash used in investing activities	(71,598)	

Cash flows from financing activities:		
Proceeds from advances from affiliates	284,500	
Proceeds from stock issuance	-	
Payments of capital lease obligations	(2,229)	
Payments of loan	-	
Proceeds from the exercise of stock options	-	
Issuance of notes payable, related parties	-	

Net cash provided by financing activities	282,271	

Net (decrease) increase in cash and cash equivalents	(1,810,353)	

Cash and cash equivalents, beginning of period	1,813,571	

Cash and cash equivalents, end of period	\$ 3,218	\$
	=====	=====
Supplemental disclosure of cash flow information:		
Cash paid for interest during the period	\$ 110	\$
	=====	=====
Supplemental disclosure of non-cash financing activities:		
Issuance of stock for convertible bridge note	\$ -	\$

See notes to consolidated financial statements

6

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Bion Environmental Technologies, Inc. (the "Company", "Bion", "we", "us" or "our") have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information. In the opinion of management, such statements include all adjustments (consisting only of normal recurring adjustments) necessary for the fair presentation of the Company's financial position, results of operations and cash flows at the dates and for the periods indicated. Pursuant to the requirements of the Securities and Exchange Commission applicable to Quarterly Reports on Form 10-QSB, the accompanying financial statements do not include all the disclosures required by GAAP for annual financial statements. While the Company believes that the disclosures presented are adequate to make the information not misleading, these interim consolidated financial statements should be read in conjunction with the audited financial statements and related notes included in the Company's Annual Report on Form 10-KSB/A for the year ended June 30, 2002. Operating results for the periods indicated are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2003.

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Certain fiscal year 2002 items have been reclassified to conform to their fiscal year 2003 presentation.

2. ORGANIZATION AND NATURE OF BUSINESS

Bion Environmental Technologies, Inc. ("Bion" or the "Company") was incorporated in 1987 in the State of Colorado.

Bion is an environmental service company focused on the needs of confined animal feeding operations (CAFOs). Bion is engaged in two main areas of activity: waste stream remediation and organic soil and fertilizer production. Bion's waste remediation service business provides CAFOs (primarily in the swine and dairy industries) with treatment for the animal waste outputs. In this regard, Bion treats their entire waste stream in a manner which cleans and reduces the waste stream thereby mitigating pollution of the air, water (both ground and surface) and soil, while creating value-added organic soil and fertilizer products. Bion's soil and fertilizer products are being used for a variety of applications including school athletic fields, golf courses and home and garden applications.

The Company's Nutrient Management System (NMS) is a patented biological and engineering process that treats water, nutrient and air pollution associated with animal waste. The system also provides a use for the waste materials and solids by biologically converting them into environmentally friendly, time-release organic-based solids that are the basis of Bion's organic soil and fertilizer business segment. Bion's BionSoil(R) and Bion Fertilizer product lines contain a unique mix of organic nutrients, bacteria and other microbes that extensive testing has shown produces superior plant growth with reduced leaching of nutrients when compared to traditional chemical fertilizers.

7

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

2. ORGANIZATION AND NATURE OF BUSINESS (CONTINUED)

The unaudited consolidated financial statements have been prepared assuming the Company will continue as a going concern. The Company incurred losses totaling \$2,726,318 during the nine months ended March 31, 2003 and has a history of losses which has resulted in an accumulated deficit of \$58,898,563 at March 31, 2003.

During the year ended June 30, 2002, through the Company's transactions with Centerpoint Corporation and OAM S.p.A., the Company obtained \$4,800,000 in cash. The Company is currently engaged in seeking additional financing to satisfy its current operating requirements.

There can be no assurance that sufficient funds required during the immediate future or thereafter will be generated from operations or that funds will be available from external sources such as debt or equity financings or other potential sources. THE LACK OF ADDITIONAL CAPITAL RESULTING FROM THE INABILITY TO GENERATE CASH FLOW FROM OPERATIONS OR TO RAISE CAPITAL FROM EXTERNAL

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

SOURCES HAVE ALREADY FORCED THE COMPANY TO SUBSTANTIALLY CURTAIL OPERATIONS, CAUSED US TO REDUCE STAFF TO SIX EMPLOYEES, AND MAY CAUSE THE COMPANY TO CEASE OPERATIONS AND WOULD, THEREFORE, HAVE A MATERIAL ADVERSE EFFECT ON ITS BUSINESS. Further, there can be no assurance that any such required funds, if available, will be available on attractive terms or that they will not have a significantly dilutive effect on the Company's existing shareholders.

We have a stockholders' deficit of \$316,463, an accumulated deficit of \$58,898,563, limited current revenues, substantial current operating losses and negative working capital. Our operations are not currently profitable; therefore, readers are further cautioned that our continued existence is uncertain if we are not successful in obtaining outside funding in an amount sufficient for us to meet our operating expenses at our current level. Management is currently engaged in seeking additional capital to fund operations until Bion system and BionSoil(R) sales are sufficient to fund operations.

THERE IS SUBSTANTIAL DOUBT ABOUT THE COMPANY'S ABILITY TO CONTINUE AS A GOING CONCERN. The accompanying consolidated financial statements do not include any adjustments relating to the recoverability or classification of asset carrying amounts or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

In connection with their report on our Consolidated Financial Statements as of and for the year ended June 30, 2002, BDO Seidman, LLP, our independent certified public accountants, expressed substantial doubt about our ability to continue as a going concern because of recurring net losses and negative cash flow from operations.

3. SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation:

The consolidated financial statements include the accounts of the Company and its wholly- and majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

8

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

3. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Loss per share of common stock:

Basic earnings per share includes no dilution and is computed by dividing income or loss available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of an entity, similar to fully diluted earnings per share. In loss periods, dilutive common equivalent shares are excluded, as the effect would be anti-dilutive. Therefore, basic and diluted earnings per share are the same for all periods presented. For the periods ended March 31, 2003, 143,211 stock options and 1,393,303 warrants having a weighted-average exercise price of \$10.48 and \$7.66, respectively, were excluded in the net loss per share calculation since the effect of inclusion would be anti-dilutive and for the periods ended March 31, 2002, 214,480 stock options and 1,393,303 warrants

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

having a weighted-average exercise price of \$13.27 and \$7.66, respectively, were excluded in the net loss per share calculation since the effect of inclusion would be anti-dilutive.

Patents:

Patents are recorded at costs of \$54,946 less accumulated amortization of \$28,849 for a net amount of \$27,713, which is included in other assets. Amortization is calculated on a straight-line basis over a period of the estimated economic life or legal life of 17 years. Amortization expense for the nine and three month periods ended March 31, 2003 and 2002 was \$2,424 and \$808, respectively.

4. ADVANCES FROM AFFILIATES

As of March 31, 2003, Bright Capital LLC ("Brightcap"), an entity owned and controlled by Dominic Bassani, a consultant whose services were provided to us as part of our management agreement with D2CO, LLC ("D2"), advanced us \$219,500 so that we could pay operating expenses that are critical to our operations, primarily consisting of salaries paid to retain critical personnel, which now consists of six employees. Mr. David Mitchell has advanced us \$65,000, for total advances from affiliates of \$284,500. Subsequent to March 31, 2003, through April 25, 2003, Brightcap advanced the Company an additional \$54,000.

On March 28, 2003, we executed a promissory note in favor of Brightcap. The note is in the initial principal sum of \$42,500 plus the \$27,000 that Brightcap has loaned since then and any additional amounts that it may loan to us in the future. The \$42,500 sum represents amounts that had already been loaned to us by Brightcap which enabled us to pay certain of our ongoing operating expenses. The note bears interest on the unpaid principal at the simple rate of six percent (6%) per annum. All principal and accrued interest becomes payable on March 28, 2004. This promissory note is included in advances from affiliates.

9

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

4. ADVANCES FROM AFFILIATES (CONTINUED)

Repayment of amounts due under the note is secured by a lien on all of our tangible assets, including without limitation, all of our computers, office furniture, file cabinets, equipment and inventory. None of our intangible assets, including our patents, intellectual property or trade secrets, is pledged as collateral for the note.

5. DEFERRED COMPENSATION

On June 30, 2001, Bion and D2CO, LLC ("D2") agreed that the payments owed to D2 under an existing management agreement be paid to a Rabbi Trust for the benefit of D2. On July 31, 2001, Bion and Sam Spitz (the "Trustee") entered into the Trust Under Deferred Compensation Plan for D2Co, LLC (the "Trust").

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Under the Trust agreement, the Company shall contribute assets to the Trust. Such assets are subject to claims of the Company's creditors in the event of the Company's insolvency, at such times as specified in the management agreement with D2. D2 shall have no preferred claim on, or any beneficial ownership interest in, any assets of the Trust. Any rights created under the management agreement with D2 and the Trust shall be unsecured contractual rights of D2 against the Company. Payments of all amounts in the Trust are to be made to D2 on January 2, 2011, as stated in the Trust agreement.

The Company accounts for the Trust under the provisions of Emerging Issues Task Force ("EITF") 97-14 "Accounting for Deferred Compensation Arrangement Where Amounts are Earned and Held in a Rabbi Trust and Invested" which requires the Company to consolidate into its financial statements the net assets of the Trust. The value of the Company's common stock held by the Trust is classified in shareholders' equity and is accounted for in a manner similar to treasury stock. The deferred compensation obligation has been classified as a liability and is adjusted, with the corresponding charge or credit to compensation expense, to reflect changes in fair value of the common stock held by the Trust. As of March 31, 2003, \$489,750 is owed to the Trust, including interest of \$2,250, and the Trust holds 91,439 shares of common stock of the Company having a fair value of \$59,435, for a total of \$549,185 in deferred compensation.

The management agreement between us and D2 was terminated effective as of March 25, 2003. The voting and shareholder agreements to which D2 was a party were also terminated as of that same date. The Trust Under Deferred Compensation Plan for D2CO, LLC (the "Trust") will remain in existence until mutually agreed otherwise and, unless otherwise agreed in writing, the "payable" balance of \$487,500 currently owed by us to the Trust will be converted into shares of our Common Stock upon the earlier to occur of (a) a \$5 million or greater equity financing(s) by us, in which case the amount payable will be converted into shares of our common stock at the equity price of the financing (or, in the event that the \$5 million in equity financing is obtained in a series of more than one financing, the price of the equity financing which pushed the aggregate total of the financings above \$5 million), or (b) March 31, 2005, at the then current market price of our common stock.

10

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

6. STOCKHOLDERS' EQUITY

Reverse stock split:

Effective July 8, 2002, the Company completed a one-for-ten reverse stock split of its outstanding shares of common stock. The accompanying unaudited consolidated financial statements have been retroactively adjusted to reflect the reverse stock split.

Warrants:

As of March 31, 2003, the Company had the following common stock warrants outstanding:

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

	Number of Shares -----	Exercise Price -----	Expiration Date -----
Class D2C-W	2,455	\$ 25.00	June 30, 2004
Class J-1	3,000	\$ 20.00	December 31, 2004
Class J-1A	119,850	\$ 6.00	December 31, 2004
Class J-1AA	17,596	\$ 7.50	December 31, 2004
Class J-1B	30,047	\$ 6.00	December 31, 2005
Class J-1C	45,770	\$ 6.00	December 31, 2005
Class J-1D	30,832	\$ 15.00	December 31, 2004
Class J-2	6,500	\$ 15.00	December 31, 2004
Class SV	1,037,343	\$ 7.50	February 16, 2006
Class O	100,000	\$ 9.00	January 15, 2006

	1,393,393		
	=====		

Stock options:

As of March 31, 2003, the Company had 143,211 stock options outstanding, having a weighted exercise price of \$10.54. As a result of the termination of employees during the quarter, a significant number of options will expire in May 2003, if not exercised.

7. COMMITMENTS AND CONTINGENCIES

Operating leases:

We amended our New York City office lease effective March 1, 2003. Under this amendment the expiration date was changed to December 31, 2003, from the previous expiration date of December 31, 2010. The amendment calls for the drawdown of the letter of credit provided to the landlord for the full amount of \$120,561 to be used to pay arrearages and future rent. In addition, two of our new subtenants, Mitchell & Co. and Zizza & Co., which are controlled by David Mitchell and Salvatore Zizza, respectively, are former officers and directors of Bion, and have personally guaranteed the lease with the landlord.

11

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

7. COMMITMENTS AND CONTINGENCIES (CONTINUED)

In addition we have entered into agreements with Mitchell & Co. and Zizza & Co. whereby they will pay the remaining rental payments and hold Bion harmless in case of default. As a result of these agreements, we will not incur additional cash outflows in connection with this lease and have no further commitment as to rental payments. Accordingly, the \$120,561 letter of credit has been expensed and the balance due for rents has been eliminated.

We vacated our Buffalo and North Carolina locations. Employees remaining from those locations are working out of their homes.

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Litigation:

On July 22, 2002, Thomas Keith Barefoot ("Barefoot"), doing business as Quin Deca Farm ("Quin Deca"), an unaffiliated party, filed a complaint against the Company in the Superior Court of the County of Harnett in the State of North Carolina regarding the Company's first generation Bion NMS System on Quin Deca Farm and the harvesting of BionSoil(R). The complaint includes breach of contract claims asserting that the Company abandoned the NMS system on Quin Deca Farm and the failure of the Company to harvest BionSoil(R). The second claim is for fraud regarding misrepresentation of the state of the technology of the first generation NMS. The third claim is for unfair and deceptive trade practices for misrepresentation of the state of the technology of the NMS System. The fourth claim is for negligent misrepresentation made by Bion in connection with the work it performed and its suitability for the intended purpose. The fifth claim is for equity/specific performance in that Bion left Quin Deca with an economically and technically deficient waste management system that cannot continue to be used without adequate and alternative methods of waste removal. Quin Deca is seeking \$830,000 in damages plus punitive damages and to have its damages trebled, reasonable attorney fees and principles of equity requiring Bion to install its second generation Bion NMS system. We have filed an answer and counterclaims. Additionally, we have filed a pending motion to remove the action to Federal court. The Company does not believe that the claim has merit and, assuming that we have the funds to properly defend this action, that the ultimate resolution of this litigation will have a material adverse effect on the Company, its operations or its financial condition.

On May 6, 2002, Arab Commerce Bank Ltd. ("ACB"), an unaffiliated party, filed a complaint against the Company in the Supreme Court of the State of New York regarding \$100,000 of the Company's convertible bridge notes ("Notes") that were issued to ACB in March of 2000. The complaint includes breach of contract claim asserting that the Company owes ACB \$265,400 plus interest or \$121,028 including interest based on ACB's interpretation of the terms of the Notes and subsequent amendments. Effective June 30, 2001, the Company issued ACB 5,034 shares of common stock on conversion in full payment of the Notes based on the Company's interpretation of the Notes, as amended. The Company has filed an answer to the complaint denying the allegations. Assuming that we have the funds to properly defend this action, the Company does not believe that the ultimate resolution of this litigation will have a material adverse effect on the Company, its operations or its financial condition.

12

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

7. COMMITMENTS AND CONTINGENCIES (CONTINUED)

We have been delinquent in paying our creditors due to our poor financial condition. As a result, various creditors have threatened litigation, although none have commenced litigation as of the date of the filing of this report.

Commitments:

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

As of March 31, 2003, we have commitments to purchase approximately \$82,000 in equipment related to our research and development project at DeVries Dairy. The Company may not be able to meet these commitments.

8. RELATED PARTY TRANSACTIONS

The Company issued to D2 11,953 and 35,374 shares of common stock for management fees during the three and nine months ended March 31, 2002, respectively. The management fees were valued at \$125,000 and \$400,000 during the three and nine months ended March 31, 2002, respectively.

The Company and D2 orally agreed during January 2002, that in the event the average price per common share is below \$7.50 for any quarter in which consulting fees are to be paid to the Trust, Bion will issue a convertible note in lieu of the stock payment. The agreement was to remain in place during the "Adjustment Period" noted in the Centerpoint and OAM Agreements. Subsequently, D2 agreed to forgo the convertible notes and the amounts remain owed to the Trust. The amounts owed to the trust are recorded as part of deferred compensation.

On July 1, 2002, D2 returned to the Company 2,874 shares of the Company's common stock that was issued as part of the consulting fee to D2 paid to the Trust Under Deferred Compensation Plan for D2Co, LLC (the "Trust") for the Benefit of D2. The shares were subsequently cancelled.

On September 30, 2002, the Company issued a convertible note for the D2 management fee to be paid to the Trust for the three months ended September 30, 2002. The convertible note was issued for the amount of the management fee of \$150,000 and pays interest at 6% per annum, payable in cash or in shares of the Company's common stock. The convertible note is convertible into shares of common stock in whole or in part at the time of the Company's next equity financing, at the price of the next equity financing. As mentioned above, D2 elected to forgo the convertible note and the amount remains owed to the Trust and is recorded as deferred compensation.

On December 31, 2002, the Company issued a convertible note for the D2 management fee to be paid to the Trust for the three months ended December 31, 2002. The convertible note was issued for the amount of the management fee of \$150,000 and pays interest at 6% per annum, payable in cash or in shares of the Company's common stock. The convertible note is convertible into shares of common stock in whole or in part at the time of the Company's next equity financing, at the price of the next equity financing. As mentioned above, D2 elected to forgo the convertible note and the amount remains owed to the Trust and is recorded as deferred compensation.

13

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statements

8. RELATED PARTY TRANSACTIONS

On March 31, 2003, the Company accrued \$187,500 for amounts owed to the Trust for the quarter ended March 31, 2003.

Also, see note 4, "Advances from Affiliates."

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Agreement with Centerpoint Corporation:

Effective February 12, 2003, in order to eliminate an impediment to a possible future financing, we entered into an agreement with Centerpoint Corporation, our majority -owned subsidiary, to immediately cancel Section 2.4

"Post-Closing Adjustment" and Section 1.2(b) "Failure to Register or Lapse of Effectiveness" from the January 2002 Subscription Agreement between us and Centerpoint. Our management believes that it is in the best interests of all of the shareholders of both companies that these obstacles to a possible future financing be removed. As majority stockholder, we have a fiduciary obligation to act in the best interests of the Centerpoint minority stockholders.

As consideration to Centerpoint for canceling the sections noted above, we will forgive all amounts due from Centerpoint, totaling approximately \$450,000 (this amount has been eliminated in consolidation) and we will return to Centerpoint, for cancellation, warrants to purchase one million shares of Centerpoint's common stock. In addition, Bion will use its best efforts to assist Centerpoint in distributing shares of Bion's common stock to its shareholders; provide the services of its management, personnel and staff and provide office space until 30 days after the distribution of the Bion common stock and; advance to Centerpoint sums reasonably needed for the distribution of the shares and a shareholder's meeting.

9. SUBSEQUENT EVENTS

On April 24, 2003, Hollandbrook Group, LLC, an entity affiliated with Mr. Howard Chase, a former director of the Company, returned to the Company 350 shares for terminating a consulting arrangement.

On April 24, 2003, Stanley F. Freedman, our legal counsel, prepaid a secured promissory note issued on August 9, 2001. The balance of the note on that date was \$58,977 and was prepaid by Mr. Freedman transferring to the Company 3,469 shares of our common stock previously held by him. The promissory note was repaid according to its terms, whereby for the purpose of paying amounts due under the promissory note, the shares of common stock are deemed to have a value of \$17.00 per share.

In a letter dated April 28, 2003, Mr. Lawrence R. Danziger resigned as Chief Financial Officer of the Company, effective April 30, 2003. We are not aware of any dispute with Mr. Danziger. Mr. Mark A. Smith, our President, has accepted the position of Interim Chief Financial Officer as of April 30, 2003.

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

Statements made in this Form 10-QSB that are not historical or current facts are "forward-looking statements" within the meaning of section 27A of the Securities Act of 1933, as amended (the "Securities Act") and section 21E of the Securities Exchange Act of 1934, as amended. These statements often can be identified by the use of terms such as "may," "will," "expect," "believe," "anticipate," "estimate," or "continue" or the negative thereof. Bion intends that such forward-looking statements be subject to the safe

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

harbors for such statements. We wish to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. Any forward-looking statements represent management's best judgment as to what may occur in the future. However, forward-looking statements are subject to risks, uncertainties and important factors beyond our control that could cause actual results and events to differ materially from historical results of operations and events and those presently anticipated or projected.

These factors include adverse economic conditions, entry of new and stronger competitors, inadequate capital, unexpected costs, failure to gain product approval in the United States or foreign countries and failure to capitalize upon access to new markets. Additional risks and uncertainties that may affect forward-looking statements about Bion's business and prospects include the possibility that a competitor will develop a more comprehensive or less expensive environmental solution, delays in market awareness of Bion and our systems and soil, or possible delays in Bion's marketing strategies, each of which could have an immediate and material adverse effect by placing us behind our competitors. Bion disclaims any obligation subsequently to revise any forward-looking statements to reflect events or circumstances after the date of such statements or to reflect the occurrence of anticipated or unanticipated events.

The following discussion should be read in conjunction with our consolidated financial statements and accompanying notes.

Lack of Review by Independent Certified Public Accountants

This Form 10-QSB has not been reviewed by BDO Seidman, LLP, our independent certified public accountants, as required by Item 310(b) of Regulation S-B. BDO Seidman, LLP has not performed the review because they have not yet reviewed the impact on the Company's accounts and operations of the various items disclosed in our Report on Form 8-K dated February 7, 2003. We are not aware of any dispute with BDO Seidman, LLP as to any accounting matters. In addition, we owe approximately \$125,000 to BDO Seidman, LLP, which must be paid or otherwise resolved in order to eliminate independence issues prior to any review or audit of our financial statements.

Overview

Bion Environmental Technologies, Inc. provides waste management solutions to the agricultural industry, focusing on livestock waste from confined animal feeding operations ("CAFOs"), such as large dairy and hog farms. We are currently engaged in two main areas of activity:

- * waste stream remediation and reduction of atmospheric emissions and
- * organic soil and fertilizer production.

Our waste remediation and reduction of atmospheric emissions service business provides CAFOs (primarily in the swine and dairy industries) with treatment for the animal waste outputs. In this regard, we microbiologically treat their entire waste stream, reducing air emissions and nutrient discharges, while creating value-added organic soil and fertilizer products. Bion's soil and fertilizer products are being used for a variety of topdressing applications including school athletic fields, golf courses and home and garden applications. Our Nutrient Management System (NMS) is a

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

patented biological and engineering process that treats water, nutrient and air pollution associated with animal waste. The system also provides a use for the waste materials and solids by biologically converting them into environmentally friendly, time-release organic-based solids that are the basis of our organic soil and fertilizer business segment. Our BionSoil(R) and Bion Fertilizer product lines contain a unique mix of organic nutrients, bacteria and other microbes that extensive testing has shown produces superior plant growth with reduced leaching of nutrients when compared to traditional chemical fertilizers.

We have been conducting business since 1989. Our original systems were wastewater treatment systems for dairy farms and food processing plants. The basic design was modified in late 1994 to create a NMS that produces organic soil products as a by-product of remediation of the waste stream when installed on large dairies or swine farms. Through June 2000, we sold and subsequently installed, in the aggregate, 32 of these first generation systems in 7 states, of which 19 are still in operation through December 2002. Of these 19 systems, 12 are first generation Bion NMS soil production system installations and 7 are waste only systems. Since June 30, 2000 we have not installed any new NMS systems since our concentration has been on research and the development of our second generation system.

We also have an ongoing research program related to our BionSoil(R) and Bion Fertilizer product lines. This research and development includes work related to harvest and processing, blending of specialty product mixes for specific market segments and tests of the effectiveness of BionSoil(R) and Bion Fertilizer blends in a number of plants in a variety of growing environments.

As the development program described above moved forward during the 2001 and 2002 fiscal years, our focus shifted from sales of first generation systems to pre-marketing the system capabilities and the economics of our second generation NMS. We have recently initiated marketing Bion's second generation system. We anticipate that we will begin leasing our first second generation system in the summer of 2003 and receive approximately \$22,000 a month in lease revenue.

The nutrient management capabilities of this new generation of systems will help break one of the major barriers facing those portions of the dairy and protein growing businesses in the U.S. which desire to expand. Our second generation system will allow businesses in these markets to meet ever stricter environmental standards for larger farms and raise more animals on less land while meeting or exceeding all requirements to protect the environment.

Critical Accounting Policies and Significant Use of Estimates in Financial Statements

The Securities and Exchange Commission ("SEC") recently issued disclosure guidance for "critical accounting policies." The SEC defines "critical accounting policies" as those that require application of management's most difficult, subjective or complex judgments, often as a

16

result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

The following list of critical accounting policies is not intended to be a comprehensive list of all of our accounting policies. Our significant accounting policies are more fully described in Note 3 to the consolidated

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

financial statements included in this Quarterly Report on Form 10-QSB and in Note 2 to the consolidated financial statements included in our Annual Report on Form 10-KSB/A. In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles with no need for management's judgment in their application. There are also areas in which management's judgment in selecting any available alternative would not produce a materially different result. We have identified the following to be critical accounting policies of the Company:

Revenue recognition: BionSoil(R) sales are recognized upon delivery of soil to customer and all risks and rewards of ownership pass to the customer.

Stock-based compensation: The Company accounts for its stock-based compensation arrangements with its employees in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and complies with the disclosure provisions of SFAS 123, "Accounting for Stock-Based Compensation." SFAS 123 established a fair-value-based method of accounting for stock-based compensation plans. Stock-based awards to non-employees are accounted for at fair value in accordance with the provisions of SFAS 123.

Income taxes: Deferred income taxes are determined by applying enacted statutory rates in effect at the balance sheet date to the differences between the tax bases of assets and liabilities and their reported amounts in the consolidated financial statements. A valuation allowance is provided based on the weight of available evidence, if it is considered more likely than not that some portion, or all, of the deferred tax assets will not be realized.

Claims receivable: Claims receivable are valued through an internal allocation made by Bion management based on its own evaluation of the relevant facts and circumstances and its review of a fairness opinion that was provided by an investment banking firm with regard to the transaction as a whole. The rights to 65% of these claims were ultimately assigned to OAM. The rights to 35% of the claims remained with Centerpoint and are included in the consolidated financial statements of the Company. This analysis requires the Company to make significant estimates, and changes in facts and circumstances could result in material changes in the valuation of the claims receivable.

Contingencies: Management is unable to make a reasonable estimate of the liabilities that may result from the final resolution of certain litigation matters disclosed. Further assessments of the potential liability will be made as additional information becomes available. Management currently does not believe that these proceedings will have a material adverse affect on the Company's consolidated financial position. It is possible, however, that results of operations could be materially affected by changes in management's assumptions relating to these proceedings or the actual final resolution of these proceedings.

Results of Operations - Comparison of Nine Months Ended March 31, 2003 with Nine Months Ended March 31, 2002

We recorded \$109,000 of soil sales during the nine months ended March 31, 2003 (the "2003 Nine Months"). This compares to soil sales of \$50,000 for

the nine months ended March 31, 2002 (the "2002 Nine Months"). In the 2003 Nine Months we began harvesting the solids from three of our first generation nutrient management systems. We did not harvest any solids from these systems in the 2002 Nine Months as we were focusing our efforts on the development of

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

our second generation system. The increase in solids allowed us to sell more soil during the 2003 Nine Months compared to the 2002 Nine Months. Cost of soil was \$578,000 for the 2003 Nine Months and \$403,000 for the 2002 Nine Months. The increase in cost of goods sold was principally due to an increase in sales. The decrease in the gross loss as a percentage of sales is principally the result of economies of scale.

General and administrative expenses decreased to \$1,805,000 for the 2003 Nine Months from \$1,886,000 for the 2002 Six Months. The decrease is primarily attributable to a decrease in salaries of \$112,000, a decrease in travel of \$45,000 a decrease in investor relation fees of \$68,000 and a decrease in equipment expenses of \$24,000. These decreased were partially offset by a an increase in legal fees of \$94,000 due to increased legal costs associated with structuring a future private placement and the preparation of agreements with California State University, Fresno, DeVries Dairy and Dairy Properties, LLC, an increase in tax and accounting fees of \$59,000 primarily due to expenses incurred to complete outstanding tax returns for Centerpoint and an increase in licensing fees of \$50,000 for the BioBalance patent.

Research and development costs decreased to \$516,000 for the 2003 Nine Months from \$616,000 for the 2002 Nine Months. This decrease is primarily the result of the construction during the 2002 Nine Months of the second generation prototype system built at Dreammaker Dairy. We did not incur construction costs on the prototype during the 2003 Nine Months.

Non-cash expenses for services and compensation decreased to \$30,000 for the 2003 Nine Months from \$4,753,000 for the 2002 Nine Months. During the 2003 Nine Months, non-cash charges for services and compensation consisted of \$488,000 in amounts owed as management fees to the Trust Under Deferred Compensation Plan for D2Co, LLC (the "Trust") and amortization for the value of options previously issued of \$31,000. These expenses were offset by income in the amount of \$459,000 from the reduction in the value of the Company's common stock previously issued to the Trust. In addition, we recognized income of \$30,000 for stock issued in error during the 2002 fiscal year. During the 2002 Nine Months, non-cash expenses for services and compensation were primarily attributable to charges of \$3,710,000 for the issuance of warrants as an inducement to convert debt, amortization of the value of options previously issued to various individuals of \$292,000, value of stock issued for management fees to D2 of \$400,000 and common stock issued to individuals with a value of \$278,000.

Interest expense decreased to \$3,000 for the 2003 Nine Months from \$8,623,000 for the 2002 Nine Months. Interest expense for the 2002 Nine Months included a charge for the beneficial conversion feature and interest of debt converted to common stock of \$5,844,000, amortization for debt discount of \$1,554,000 and interest expense of \$1,209,000 on notes payable that were subsequently converted into common stock.

Interest income decreased to \$9,000 for the 2003 Nine Months from \$23,000 for the 2002 Nine Months.

Other income decreased to \$47,000 for the 2003 Nine Months from \$73,000 for the 2002 Nine Months.

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

We recorded no soil sales during the three months ended March 31, 2003 (the "2003 Quarter"). This compares to soil sales of \$21,000 for the three months ended March 31, 2001 (the "2002 Quarter"). As a result of heavy rains and frequent snow falls, we were not able to ship any soil in the 2003 Quarter.

General and administrative expenses decreased to \$440,000 for the 2003 Quarter from \$673,000 for the 2002 Quarter. The decrease is primarily attributable to a decrease in salaries and related benefits of \$239,000, a decrease in travel of \$24,000, a decrease in accounting fees of \$42,000 and a decrease in legal fees of \$36,000. These decreases were primarily the result of a decrease in operations due to our current liquidity position. These decreases were partially offset by an increase in rent of \$81,000 primarily due to the forfeiture of our letter of credit as part of our renegotiation of our New York City lease.

Research and development decreased to \$181,000 for the 2003 Quarter from \$219,000 for the 2002 Quarter. The decrease was primarily the result of decreased activity as a result of our liquidity position.

Non-cash expenses for services and compensation decreased to \$37,000 for the 2003 Quarter from \$4,253,000 for the 2002 Quarter. During the 2003 Quarter, non-cash expenses for services and compensation were primarily attributable to charges of \$3,710,000 for the issuance of warrants as an inducement to convert debt, amortization of the value of options previously issued to various individuals of \$156,000, value of stock issued for management fees to D2 of \$150,000 and common stock issued to individuals with a value of \$201,000.

Interest expense decreased to \$0 for the 2003 Quarter from \$6,082,000 for the 2002 Quarter. The 2002 Quarter included a charge for the beneficial conversion feature and interest of debt converted to common stock of \$5,844,000, and interest expense of \$517,000 on notes payable that were subsequently converted into common stock.

Interest income decreased to \$1,000 for the 2003 Quarter from \$12,000 for the 2002 Quarter.

Other income increased to \$67,000 for the 2003 Quarter from \$4,000 for the 2002 Quarter. The 2003 Quarter included \$33,000 in gains from the sale of assets.

Seasonality

Bion's installation capability is restricted in cold weather climates to approximately eight months per year. However, when weather conditions limit construction activity in southern market areas, projects in northern markets can proceed, and when northern area weather is inappropriate, southern projects can proceed. BionSoil(R) harvests on the existing installed base is semi-annual and is timed for spring and fall, with harvested soils being available for sale shortly after harvesting. BionSoil(R) and Bion Fertilizer product sales are expected to exhibit a somewhat seasonal sales pattern with emphasis on spring, summer and fall sales.

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

Liquidity and Capital Resources

Our principal sources of liquidity, which consist of cash and cash equivalents, are \$3,000 as of March 31, 2003. We believe we will not generate sufficient operating cash flow to meet our needs and we are currently seeking external financing. THE LACK OF ADDITIONAL CAPITAL RESULTING FROM THE INABILITY TO GENERATE CASH FLOW FROM OPERATIONS OR TO RAISE CAPITAL FROM EXTERNAL SOURCES HAVE ALREADY FORCED THE COMPANY TO SUBSTANTIALLY CURTAIL OPERATIONS, CAUSED US TO REDUCE STAFF TO SIX EMPLOYEES, AND MAY CAUSE THE COMPANY TO CEASE OPERATIONS AND WOULD, THEREFORE, HAVE A MATERIAL ADVERSE EFFECT ON ITS BUSINESS. There can be no assurances that any financing will be available or that the terms will be acceptable to us, or that any financing will be consummated.

The level of funding required to accomplish our objectives is ultimately dependent on the success of our research and development efforts, which at this time is unknown. Currently, we estimate, that over the next six months, no less than approximately \$650,000 will be required for continued research and development efforts which includes construction of the system at Devries Dairy and the engineering for the system at the California Agricultural Technology Institute at California State University, Fresno. In addition, we would need additional funds for continued general and administration expenses and funds to satisfy our existing creditors.

Effective February 12, 2003, in order to eliminate an impediment to a possible future financing, we entered into an agreement with Centerpoint Corporation, our majority -owned subsidiary, to immediately cancel Section 2.4 "Post-Closing Adjustment" and Section 1.2(b) "Failure to Register or Lapse of Effectiveness" from the January 2002 Subscription Agreement between us and Centerpoint. Our management believes that it is in the best interests of all of the shareholders of both companies that these obstacles to a possible future financing be removed. As majority stockholder, we have a fiduciary obligation to act in the best interests of the Centerpoint minority stockholders.

As consideration to Centerpoint for canceling the sections noted above, if approved by the Board of Directors of Bion, we will forgive all amounts due from Centerpoint, totaling approximately \$450,000 (this amount has been eliminated in consolidation). In addition, we will return to Centerpoint, for cancellation, warrants to purchase one million shares of Centerpoint's common stock.

During the period from January 10, 2003 through April 11, 2003, Bright Capital LLC ("Brightcap"), an entity owned and controlled by Dominic Bassani, a consultant whose services were provided to us as part of our management agreement with D2CO, LLC ("D2"), advanced us \$249,500 so that we could pay operating expenses that are critical to our operations, primarily consisting of salaries paid to retain critical personnel, which now consists of six employees. Mr. David Mitchell has advanced us \$35,000. Also, as of April 25, 2003, we have accounts payable and accrued expenses of \$924,000.

We amended our New York City office lease effective March 1, 2003. Under this amendment the expiration date was changed to December 31, 2003, from the previous expiration date of December 31, 2010. The amendment calls for the drawdown of the letter of credit provided to the landlord for the full amount of \$120,561 to be used to pay arrearages and future rent. In addition, two of our new subtenants, Mitchell & Co. and Zizza & Co., which are controlled by David Mitchell and Salvatore Zizza, respectively, are former

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

officers and directors of Bion, and have personally guaranteed the lease with the landlord. In addition, we have entered into agreements with Mitchell & Co. and Zizza & Co. to make the remaining payments under the lease. We will not incur additional cash outflows in connection with this lease as a result of the drawdown of the letter of credit, the personal guarantees and the agreements with Mitchell & Co. and Zizza & Co.

We vacated our Buffalo and North Carolina locations. Employees remaining from those locations are working from their homes.

Going Concern

IN CONNECTION WITH THEIR REPORT ON OUR CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED JUNE 30, 2002, BDO SEIDMAN, LLP, OUR INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS, EXPRESSED SUBSTANTIAL DOUBT ABOUT OUR ABILITY TO CONTINUE AS A GOING CONCERN BECAUSE OF RECURRING NET LOSSES AND NEGATIVE CASH FLOW FROM OPERATIONS.

We have a stockholders' deficit of \$316,000, an accumulated deficit of \$58,899,000, limited current revenues and substantial current operating losses. Our operations are not currently profitable; therefore, readers are further cautioned that our continued existence is uncertain if we are not successful in obtaining outside funding in an amount sufficient for us to meet our operating expenses at our current level. Management is currently engaged in seeking additional capital or other financing arrangements to fund operations until Bion system and BionSoil(R) sales are sufficient to fund operations.

Consolidated Working Capital

Consolidated working capital is a negative \$1,053,000 at March 31, 2003 compared to a positive \$1,665,000 at June 30, 2002. This change is primarily the result of operating cash outflows of \$2,021,000 and purchases of property and equipment of \$116,000, and advances from affiliates of \$284,500 during the 2003 Nine Months.

Analysis of Cash Flows

Cash used in operating activities decreased to \$2,021,000 in the 2003 Nine Months from \$2,823,000 in the 2002 Nine Months. The decrease is primarily the result of an increase in accounts payable and accrued expenses of \$456,000 and amounts owed to affiliates of 284,500.

Cash used in investing activities increased to \$72,000 in the 2003 Nine Months compared to \$3,662,000 cash used in investing activities in the 2002 Nine Months. The 2002 Nine Months included a business acquisition of \$3,642,000, net of cash acquired. The increase is the result of property and equipment purchases relating to soil processing made in the 2003 Six Months.

Cash provided by financing activities decreased to \$282,000 in the 2003 Nine Months compared to \$8,067,000 of cash provided by financing activities in the 2002 Nine Months. The 2003 Nine Months includes \$284,500 in advances from affiliates. The 2002 Nine Months includes \$8,500,000 proceeds from stock issued to Centerpoint Corporation, \$120,000 from the exercise of stock options, \$355,000 in proceeds from the issuance of notes payable to related parties and payments of loan in the amount of \$898,000.

As of March 31, 2003, we have commitments to purchase approximately \$82,000 in equipment related to our research and development project at DeVries Dairy. The Company may not be able to meet these commitments.

Item 3. Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we have evaluated the effectiveness of the design and operation of our disclosure controls and procedures within 90 days of the filing date of this quarterly report, and, based on their evaluation, our principal executive officer and principal financial officer have concluded that these controls and procedures are effective. There were no significant changes in our internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

Disclosure controls and procedures are our controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in the reports that we file under the Exchange Act is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

PART II

Item 1. Legal Proceedings

On July 22, 2002, Thomas Keith Barefoot ("Barefoot"), doing business as Quin Deca Farm ("Quin Deca"), an unaffiliated party, filed a complaint against the Company in the Superior Court of the County of Harnett in the State of North Carolina regarding the Company's first generation Bion NMS System on Quin Deca Farm and the harvesting of BionSoil(R). The complaint includes breach of contract claims asserting that the Company abandoned the NMS system on Quin Deca Farm and the failure of the Company to harvest BionSoil(R). The second claim is for fraud regarding misrepresentation of the state of the technology of the first generation NMS. The third claim is for unfair and deceptive trade practices for misrepresentation of the state of the technology of the NMS System. The fourth claim is for negligent misrepresentation made by Bion in connection with the work it performed and its suitability for the intended purpose. The fifth claim is for equity/specific performance in that Bion left Quin Deca with an economically and technically deficient waste management system that cannot continue to be used without adequate and alternative methods of waste removal. Quin Deca is seeking \$830,000 in damages plus punitive damages and to have its damages trebled, reasonable attorney fees and principles of equity requiring Bion to install its second generation Bion NMS system. We have filed an answer and counterclaims. Additionally, we have filed a pending motion to remove the action to Federal court. The Company does not believe that the claim has merit and, assuming that we have the funds to properly defend this action, that the ultimate resolution of this litigation will have a material adverse effect on the Company, its operations or its financial condition.

On May 6, 2002, Arab Commerce Bank Ltd. ("ACB"), an unaffiliated party, filed a complaint against the Company in the Supreme Court of the State of New York regarding the \$100,000 of the Company's convertible bridge notes ("Notes") that were issued to ACB in March of 2000. The complaint includes

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

breach of contract claims asserting that the Company owes ACB \$265,400 plus interest or \$121,028 including interest based on its interpretation of the

22

terms of the Notes and subsequent amendments. Effective June 30, 2001, the Company issued ACB 5,034 shares of common stock on conversion in full payment of the Notes based on the Company's interpretation of the Notes, as amended. The Company has filed an answer to the complaint denying the allegations. Assuming that we have the funds to properly defend this action. The Company does not believe that the ultimate resolution of this litigation will have a material adverse effect on the Company, its operations or its financial condition.

We have been delinquent in paying our creditors due to our poor financial condition. As a result, various creditors have threatened litigation, although none have commenced litigation as of the date of the filing of this report.

Item 5. Other Information

The following additional change in our management has recently occurred:

In a letter dated April 28, 2003, Mr. Lawrence R. Danziger resigned as Chief Financial Officer of the Company, effective April 30, 2003. We are not aware of any dispute with Mr. Danziger. Mr. Mark A. Smith, our President, has accepted the position of Interim Chief Financial Officer as of April 30, 2003.

Item 6. Exhibits and Reports on Form 8-K

The following documents are filed as exhibits to this Form 10-QSB, including those exhibits incorporated in this Form 10-QSB by reference to a prior filing of Bion under the Securities Act or the Exchange Act as indicated in parenthesis:

Exhibit No.	Description
10.1	Promissory Note and Security Agreement between Bion Environmental Technologies, Inc. and Bright Capital, LLC (A)
10.2	First Amendment to Lease between Bion Environmental Technologies, Inc. and Pan Am Equities Corp. (A)
10.3	Agreement between Bion Environmental Technologies, Inc. and Bergen Cove (A)
10.4	Agreement between Bion Environmental Technologies, Inc. and David Mitchell dated April 7, 2003 (A)
10.5	Amendment to agreement between Bion Environmental Technologies, Inc. and Centerpoint Corporation (B)
10.6	Resignation letter of Lawrence Danziger as Chief Financial Officer (B)
99.1	Certification by Mark A. Smith pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
(B)

(A) Filed on April 15, 2003, as an exhibit to our Report on Form 8-K dated March 25, 2003.

(B) Filed herewith.

23

Reports on Form 8-K

We filed a Report on Form 8-K dated February 19, 2003 reporting information under Items 5 and 7 of that form concerning changes in management and disclosing a letter sent to investors.

We filed a Report on Form 8-K dated March 25, 2003 reporting information under Items 5 and 7 of that form concerning changes in management, a liquidity update, our loan with Bright Capital, LLC, and changes to our consulting agreement with D2Co, LLC.

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: May 1, 2003

BION ENVIRONMENTAL TECHNOLOGIES, INC.

by: /s/ Mark A. Smith

Mark A. Smith
Chief Executive Officer and
Interim Chief Financial Officer

CERTIFICATIONS PURSUANT TO RULE 13a-14 UNDER
THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED

I, Mark A. Smith, certify that:

1. I have reviewed this quarterly report on Form 10-QSB of Bion Environmental Technologies, Inc.;

2. Based on my knowledge, this quarterly 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 quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly 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 quarterly report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

a) designed such disclosure controls and procedures 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 quarterly report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

Edgar Filing: BION ENVIRONMENTAL TECHNOLOGIES INC - Form 10QSB

6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: May 1, 2003

/s/ Mark A. Smith

Name: Mark A. Smith
Title: Principal Executive Officer and
Interim Chief Financial Officer