U.S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(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, 2017

or

☐ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the Transition Period From to .

Commission file number 000-25727

IKONICS CORPORATION

(Exact name of registrant as specified in its charter)

Minnesota (State or other jurisdiction of incorporation or organization)	**41-0730027** (I.R.S. employer identification no.)
4832 Grand Avenue **Duluth, Minnesota** (Address of principal executive offices)	**55807** (Zip code)

(218) 628-2217
Issuer's telephone number

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). 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 (Do not check if a smaller reporting company) ☐	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. ☐

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: Common Stock, $.10 par value - 2,019,003 shares outstanding as of May 1, 2017.

IKONICS Corporation

QUARTERLY REPORT ON FORM 10-Q

PART I - FINANCIAL INFORMATION

ITEM 1. Condensed Financial Statements

IKONICS CORPORATION

CONDENSED BALANCE SHEETS

	March 31, 2017 (unaudited)	December 31, 2016
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 608,340	$ 1,048,713
Short-term investments	3,338,000	3,246,000
Trade receivables, less allowance of $60,000 in 2017 and $54,000 in 2016	1,930,959	2,336,501
Inventories	2,232,534	1,986,172
Prepaid expenses and other assets	391,835	361,905
Income taxes receivable	280,540	66,181
Total current assets	8,782,208	9,045,472
PROPERTY, PLANT, AND EQUIPMENT, at cost:		
Land and building	9,201,846	9,189,743
Machinery and equipment	4,909,952	4,884,814
Office equipment	1,590,032	1,566,856
Vehicles	272,144	272,144
	15,973,974	15,913,557
Less accumulated depreciation	(7,213,464)	(7,001,162)
	8,760,510	8,912,395
INTANGIBLE ASSETS, less accumulated amortization of $155,552 in 2017 and $149,072 in 2016	339,329	338,127
	$ 17,882,047	$ 18,295,994
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current portion of long-term debt, net	$ 128,182	$ 127,303
Accounts payable	842,140	730,386
Accrued compensation	242,469	388,600
Other accrued liabilities	92,743	67,088
Total current liabilities	1,305,534	1,313,377
LONG-TERM LIABILITIES		
Long-term debt, less current portion, net	3,044,789	3,077,457
Deferred income taxes	446,000	446,000
Total long-term liabilities	3,490,789	3,523,457
Total liabilities	4,796,323	4,836,834
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Preferred stock, par value $.10 per share; authorized 250,000 shares; none issued	—	—
Common stock, par value $.10 per share; authorized 4,750,000 shares; issued and outstanding 2,018,753 shares in 2017 and 2016	201,875	201,875
Additional paid-in-capital	2,737,467	2,732,006
Retained earnings	10,146,382	10,525,279
Total stockholders' equity	13,085,724	13,459,160
	$ 17,882,047	$ 18,295,994

See notes to condensed financial statements.

IKONICS CORPORATION
CONDENSED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
NET SALES	$ 3,628,992	$ 4,013,210
COST OF GOODS SOLD	2,538,764	2,716,536
GROSS PROFIT	1,090,228	1,296,674
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	1,510,614	1,439,116
RESEARCH AND DEVELOPMENT EXPENSES	165,770	177,864
LOSS FROM OPERATIONS	(586,156)	(320,306)
INTEREST EXPENSE	(20,817)	—
OTHER	5,153	114
LOSS BEFORE INCOME TAXES	(601,820)	(320,192)
INCOME TAX BENEFIT	(222,923)	(127,380)
NET LOSS	$ (378,897)	$ (192,812)
LOSS PER COMMON SHARE:		
Basic	$ (0.19)	$ (0.10)
Diluted	$ (0.19)	$ (0.10)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING		
Basic	2,018,753	2,018,335
Diluted	2,018,753	2,018,335

See notes to condensed financial statements.

IKONICS CORPORATION
CONDENSED STATEMENTS OF CASH FLOWS (Unaudited)

	Three Months Ended March 31, 2017	Three Months Ended March 31, 2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (378,897)	$ (192,812)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	212,302	162,751
Amortization	9,574	6,047
Stock based compensation	5,461	5,248
Net loss on sale and disposal of property, plant and equipment	—	8,001
Changes in working capital components:		
Trade receivables	405,542	(56,062)
Inventories	(246,362)	(134,229)
Prepaid expenses and other assets	(29,930)	(96,474)
Income tax receivable	(214,359)	(139,119)
Accounts payable	111,754	170,805
Accrued expenses	(120,476)	110,076
Net cash used in operating activities	(245,391)	(155,768)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property, plant, equipment and construction in progress	(60,417)	(1,017,857)
Proceeds from sale of equipment	—	1,000
Purchases of intangibles	(7,682)	(14,242)
Purchases of short-term investments	(1,225,000)	—
Proceeds on sale of short-term investments	1,133,000	—
Net cash used in investing activities	(160,099)	(1,031,099)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on long-term debt	(34,883)	—
Proceeds from exercise of stock options	—	3,765
Net cash provided by (used in) financing activities	(34,883)	3,765
NET DECREASE IN CASH AND CASH EQUIVALENTS	(440,373)	(1,183,102)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	1,048,713	2,248,466
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 608,340	$ 1,065,364
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Construction in progress included in accounts payable	$ —	$ 96,166
Cash paid for interest	$ 17,786	$ —
Cash received (paid) for income taxes, net	$ 8,564	$ (11,740)

See notes to condensed financial statements.

1. Basis of Presentation

The condensed balance sheet of IKONICS Corporation (the "Company") as of March 31, 2017, and the related condensed statements of operations for the three months ended March 31, 2017 and 2016, and cash flows for the three months ended March 31, 2017 and 2016, have been prepared without being audited.

In the opinion of management, these statements reflect all adjustments (consisting of only normal recurring adjustments) necessary to present fairly the financial position of IKONICS Corporation as of March 31, 2017, and the results of operations and cash flows for all periods presented.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. Therefore, these statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

The results of operations for interim periods are not necessarily indicative of results that will be realized for the full fiscal year.

2. Short-Term Investments

The Company's $3.3 million of short-term investments at March 31, 2017 is comprised of 14 fully insured certificates of deposit with original maturities ranging from nine to twelve months and interest rates ranging from 0.60% to 0.95%

3. Inventories

The major components of inventories are as follows:

	Mar 31, 2017	Dec 31, 2016
Raw materials	$ 1,555,975	$ 1,438,471
Work-in-progress	374,598	355,208
Finished goods	1,442,853	1,319,856
Reduction to LIFO cost	(1,140,892)	(1,127,363)
Total Inventories	$ 2,232,534	$ 1,986,172

4. Earnings Per Common Share (EPS)

Basic EPS is calculated using net loss divided by the weighted average of common shares outstanding. Diluted EPS is calculated similarly to Basic EPS except that the weighted average number of common shares outstanding is increased to include the number of additional common shares that would have been outstanding if the potential dilutive common shares, such as those shares subject to options, had been issued. The options disclosed in Note 5 have been excluded from the computation because of their antidilutive effect.

Shares used in the calculation of diluted EPS are summarized below:

	Three Months Ended	
	Mar 31, 2017	Mar 31, 2016
Weighted average common shares outstanding	2,018,753	2,018,335
Dilutive effect of stock options	—	—
Weighted average common and common equivalent shares outstanding	2,018,753	2,018,335

If the Company was in a net income position for the first three months of 2017, 250 options with a weighted average exercise price of $7.54 would have been included as part of the weighted average common and common equivalent shares outstanding as the options would have been dilutive, while 15,918 options with a weighted average exercise price of $14.51 would have remained excluded as the options were anti-dilutive.

If the Company was in a net income position for the first three months of 2016, 250 options with a weighted average exercise price of $7.54 would have been included as part of the weighted average common and common equivalent shares outstanding as the options would have been dilutive while 11,418 options with a weighted average exercise price of $15.99 would have remained excluded as the options were anti-dilutive.

5. Stock-Based Compensation

The Company maintains a stock incentive plan which authorizes the issuance of up to 442,750 shares of common stock. Of those shares, 16,168 were subject to outstanding options and 104,239 were reserved for future grants at March 31, 2017. The plan provides for granting eligible participants stock options or other stock awards, as described by the plan, at option prices ranging from 85% to 110% of fair market value at the date of grant. Options granted expire up to seven years after the date of grant. Such options generally become exercisable over a one- to three-year period.

The Company charged compensation cost of approximately $5,000 against income for the three months ended March 31, 2017 and 2016. As of March 31, 2017, there was approximately $27,000 of unrecognized compensation cost related to unvested share-based compensation awards granted. That cost is expected to be recognized over the next three years.

The Company receives a tax deduction for certain stock option exercises during the period in which the options are exercised, generally for the excess of the market price at the time the stock options are exercised over the exercise price of the options, which increases additional paid in capital and reduces income taxes payable.

Proceeds from the exercise of 500 stock options were approximately $4,000 for the three months ended March 31, 2016. No stock options were exercised during the three months ended March 31, 2017, and there were no options granted for the three months ended March 31, 2017 or 2016.

Stock option activity during the three months ended March 31, 2017 was as follows:

	Shares	Weighted Average Exercise Price
Outstanding at January 1, 2017	16,168	$ 14.40
Outstanding at March 31, 2017	16,168	$ 14.40
Exercisable at March 31, 2017	8,084	$ 15.49

The aggregate intrinsic value of all options outstanding and exercisable at March 31, 2017 was approximately $1,000.

6. Segment Information

The Company's reportable segments are strategic business units that offer different products and have varied customer bases. There are five reportable segments: Domestic, Export, IKONICS Imaging, Digital Texturing (DTX) and Advanced Material Solutions (AMS). Domestic sells screen printing film, emulsions, and inkjet receptive film to distributors located in the United States and Canada. IKONICS Imaging sells photo resistant film, art supplies, glass, metal medium and related abrasive etching equipment to end user customers located in the United States and Canada. AMS provides sound deadening and weight reduction technology to the aerospace industry along with products and services for etched composites, ceramics, glass and silicon wafers. DTX includes products and customers related to patented and proprietary inkjet technology used for mold texturing and prototyping. Export sells primarily the same products as Domestic and the IKONICS Imaging products not related to AMS or DTX. The accounting policies applied to determine the segment information are the same as those described in the Company's Annual Report on Form 10-K for the year ended December 31, 2016.

Management evaluates the performance of each segment based on the components of divisional income. Assets and liabilities are not allocated to segments, except for trade receivables which are allocated based on the previous segmentation. Financial information with respect to the reportable segments follows:

For the three months ended March 31, 2017:

	IKONICS						
	Domestic	Export	IKONICS Imaging	DTX	AMS	Unalloc.	Total
Net sales	$ 1,303,569	$ 1,055,005	$ 989,986	$ 115,231	$ 165,201	$ —	$ 3,628,992
Cost of goods sold	826,741	839,364	523,580	35,482	313,597	—	2,538,764
Gross profit (loss)	476,828	215,641	466,406	79,749	(148,396)	—	1,090,228
Selling, general and administrative*	351,422	196,117	283,859	34,635	96,795	547,786	1,510,614
Research and development*	—	—	—	—	—	165,770	165,770
Income (loss) from operations	$ 125,406	$ 19,524	$ 182,547	$ 45,114	$ (245,191)	$ (713,556)	$ (586,156)

For the three months ended March 31, 2016:

	IKONICS						
	Domestic	Export	IKONICS Imaging	DTX	AMS	Unalloc.	Total
Net sales	$ 1,353,728	$ 1,243,185	$ 1,117,698	$ 76,880	$ 221,719	$ —	$ 4,013,210
Cost of goods sold	846,399	962,489	539,782	35,424	332,442	—	2,716,536
Gross profit (loss)	507,329	280,696	577,916	41,456	(110,723)	—	1,296,674
Selling, general and administrative*	359,397	143,031	251,371	34,743	103,903	546,671	1,439,116
Research and development*	—	—	—	—	—	177,864	177,864
Income (loss) from operations	$ 147,932	$ 137,665	$ 326,545	$ 6,713	$ (214,626)	$ (724,535)	$ (320,306)

* The Company does not allocate all selling, general and administrative expenses or any research and development expenses to its operating segments for internal reporting.

Trade receivables by segment as of March 31, 2017 and December 31, 2016 were as follows:

	Mar 31, 2017	Dec 31, 2016
Domestic	$ 877,154	$ 1,206,866
Export	527,327	551,803
IKONICS Imaging	286,048	363,602
DTX	87,569	52,935
AMS	192,097	177,374
Unallocated	(39,236)	(16,079)
Total	$ 1,930,959	$ 2,336,501

7. Income Taxes

The Company reports a liability for unrecognized tax benefits taken or expected to be taken when they are uncertain. As of March 31, 2017 and 2016, there was no liability for unrecognized tax benefits.

The Company is subject to taxation in the United States and various states. The material jurisdictions that are subject to examination by tax authorities primarily include Minnesota and the United States, in each case for tax years 2014, 2015, and 2016.

IKONICS CORPORATION

The information presented below in Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended. Statements that are not historical or current facts, including statements about beliefs and expectations, are forward-looking statements. These forward-looking statements include statements relating to our future plans and objectives and results. Such statements are subject to risks and uncertainties, including those discussed elsewhere in this report and under the heading "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2016, as updated in our subsequent reports filed with the SEC, which could cause actual results to differ materially from those projected. Because actual results may differ, readers are cautioned not to place undue reliance on these forward-looking statements.

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

The following management's discussion and analysis focuses on those factors that had a material effect on the Company's financial results of operations during the first quarter of 2017 and for the same period of 2016. It should be read in connection with the Company's condensed unaudited financial statements and notes thereto included in this Form 10-Q.

Critical Accounting Estimates

The Company prepares its financial statements in conformity with accounting principles generally accepted in the United States of America. Therefore, the Company is required to make certain estimates, judgments and assumptions that the Company believes are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. The accounting estimates, which IKONICS believes are the most critical to aid in fully understanding and evaluating its reported financial results, include the following:

Trade Receivables. The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer's current credit worthiness, as determined by review of the current credit information. The Company continuously monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that have been identified. While such credit losses have historically been within expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same collection history that has occurred in the past. The general payment terms are net 30-45 days for domestic customers and net 30-90 days for foreign customers. A small percentage of the trade receivables balance is denominated in a foreign currency with no concentration in any given country. At the end of each reporting period, the Company analyzes the receivable balance for customers paying in a foreign currency. These balances are adjusted to each quarter or year-end spot rate in accordance with FASB ASC 830, *Foreign Currency Matters.* The Company also maintains a provision for any customer related returns based upon historical experience of actual returns and any specifically identified product issues, refunds or credits.

Inventories. Inventories are valued at the lower of cost or market value using the last in, first out (LIFO) method. The Company monitors its inventory for obsolescence and records reductions from cost when required.

Income Taxes. Deferred taxes are provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. Deferred tax assets and liabilities are presented as long-term on a net basis. The Company follows the accounting standard on accounting for uncertainty in income taxes, which addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. Under this guidance, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50 percent likelihood of being realized upon ultimate settlement. The guidance on accounting for uncertainty in income taxes also addresses derecognition, classification, interest and penalties on income taxes, and accounting in interim periods.

Revenue Recognition. The Company recognizes revenue on sales of products when title passes, which can occur at the time of shipment or when the goods arrive at the customer location depending on the agreement with the customer. The Company sells its products to both distributors and end-users. Sales to distributors and end-users are recorded based upon the criteria governed by the sales, delivery, and payment terms stated on the invoices from the Company to the purchaser. In addition to transfer of title / risk of loss, all revenue is recorded in accordance with the criteria outlined within Staff Accounting Bulletin 104 and FASB ASC 605 *Revenue Recognition*:

(a) persuasive evidence of an arrangement (principally in the form of customer sales orders and the Company's sales invoices);

(b) delivery and performance (evidenced by proof of delivery, e.g. the shipment of film and substrates with bill of lading used for proof of delivery for FOB shipping point terms, and the carrier booking confirmation report used for FOB destination terms). Once the finished product is shipped and physically delivered under the terms of the invoice and sales order, the Company has no additional performance or service obligations to complete;

(c) a fixed or determinable sales price (the Company's pricing is established and is not based on variable terms, as evidenced in either the Company's invoices or the limited number of distribution agreements; the Company rarely grants extended payment terms and has no history of concessions); and

(d) a reasonable likelihood of payment (the Company's terms are standard, and the Company does not have a substantial history of customer defaults or non-payment).

Sales are reported on a net basis by deducting credits, estimated normal returns and discounts. The Company's return policy does not vary by geography. The customer has no rotation or price protection rights and the Company is not under a warranty obligation. Freight billed to customers is included in sales. Shipping costs are included in cost of goods sold.

Results of Operations

Quarter Ended March 31, 2017 Compared to Quarter Ended March 31, 2016

Sales. The Company's 2017 first quarter sales of $3.6 million were 9.6% lower than the 2016 first quarter sales of $4.0 million. Export 2017 first quarter sales decreased by $188,000, or 15.1%, compared to the same period last year as the Company realized lower sales in Asia, Europe and the Middle East. Part of this decrease is timing related, and the Company expects to recover a portion of the first quarter sales shortfall in the second quarter of 2017. IKONICS Imaging sales also decreased by 11.4% for the period from $1.1 million in 2016 to $990,000 in 2017 as 2016 benefitted from a large initial order by a newly acquired customer. AMS realized a drop in sales from $222,000 in first quarter of 2016 to $165,000 in 2017. AMS's largest customer has temporarily curtailed orders due to an overstocking in the supply chain. The Company expects this slowdown to continue well into the second quarter of 2017. Lower equipment and film sales resulted in 3.7% decrease in first quarter Domestic sales as sales decreased from $1.4 million in 2016 to $1.3 million in 2017. Partially offsetting these sales decreases was an increase in DTX sales of 49.9%, or $38,000, in the first quarter of 2017 versus the same period in 2016 due to an increase in orders from DTX's largest customer.

Gross Profit. Gross profit was $1.1 million, or 30.0% of sales, in the first quarter of 2017 compared to $1.3 million, or 32.3% of sales, for the same period in 2016. IKONICS Imaging gross margin for 2017 was unfavorably impacted by lower sales volumes, and a decrease in high margin film sales as its first quarter gross margin percentage decreased from 51.7% in 2016 to 47.1% in 2017. Lower sales volumes negatively affected both the Export and AMS gross margins in the first quarter of 2017 compared to same period in 2016 while a decrease in Domestic high-margin film sales resulted in Domestic's gross margin decreasing from 37.5% in first quarter of 2016 to 36.6% in 2017. The DTX gross margin which improved to 69.2% in the first quarter of 2017 from 53.9% in first quarter of 2016 benefitted from an increase in high-margin film sales.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were $1.5 million, or 41.6% of sales, in the first quarter of 2017 compared to $1.4 million, or 35.9% of sales, for the same period in 2016. The first quarter 2017 increase in selling, general and administrative expense is related to higher trade show and promotional expenses along with increased international sales consulting expenses.

Research and Development Expenses. Research and development expenses during the first quarter of 2017 were $166,000, or 4.6% of sales, versus $178,000, or 4.4%, of sales for the same period in 2016. The decrease is related to lower supplies, compliance and production trial expenses.

Income Taxes. For the first three months of 2017, the Company realized an income tax benefit of $223,000, or an effective rate of 37.0%, compared to income tax benefit of $127,000, or an effective rate of 39.8%, for the same period in 2016. The decrease in the effective tax rate for 2017 over 2016 is primarily due to higher pre-tax loss for the current year and the impact of non-deductible items. In 2017, the unfavorable non-deductible items decreased the effective tax rate due to estimated pre-tax losses. The income tax provision for the 2017 and 2016 periods differ from expected tax benefit due to unfavorable non-deductible items offset by the generation of research and development tax credits.

Liquidity and Capital Resources

Outside of the building expansion, for which $3.4 million in financing was obtained during 2016, the Company has financed its operations principally with funds generated from operations. These funds have been sufficient to cover the Company's normal operating expenditures, annual capital requirements, and research and development expenditures.

Cash and cash equivalents were $608,000 and $1.0 million at March 31, 2017 and December 31, 2016, respectively. Operating activities used $245,000 in cash during the first three months of 2017 compared to $156,000 of cash used in operating activities during the same period in 2016. Cash used in operating activities is primarily the result of net loss adjusted for non-cash depreciation, amortization, loss on sale and disposal of property, and certain changes in working capital components discussed in the following paragraph.

During the first three months of 2017, the decrease in sales for the first quarter resulted in a $406,000 decrease in trade receivables. The Company believes that the quality of its receivables is high and that strong internal controls are in place to maintain proper collections. Inventories increased by $246,000 due to higher raw material and finished good levels. Prepaid expenses and other assets increased by $30,000, reflecting insurance premiums paid in advance. Accounts payable increased by $112,000 due to the timing of vendor payments. Accrued expenses decreased by $120,000, reflecting the timing of compensation payments while income taxes receivable increased by $214,000 due to the timing of estimated tax payments compared to the calculated 2017 tax liability.

During the first three months of 2016, the increase in sales for the first quarter along with the timing of collections resulted in a $56,000 increase in trade receivables. The Company believes that the quality of its receivables is high and that strong internal controls are in place to maintain proper collections. Inventories increased by $134,000 due to higher raw material levels. Prepaid expenses and other assets increased by $96,000, reflecting insurance premiums paid in advance. Accounts payable increased by $171,000 due to the timing of payments related to construction accounts payable and the timing of vendor payments. Accrued expenses increased by $110,000, reflecting the timing of compensation payments while income taxes receivable increased by $139,000 due to the timing of estimated tax payments compared to the calculated 2016 tax liability.

During the first three months of 2017, cash used in investing activities was $160,000. The Company purchased five certificates of deposits totaling $1.2 million. Five certificates of deposits totaling $1.1 million matured during the first three months of 2017. The Company's purchases of property and equipment of $60,000 were mainly for improvements to production and process capabilities. Also, during the first three months of 2017, the Company incurred $8,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process

During the first three months of 2016, cash used in investing activities was $1,031,000. The Company's purchases of property and equipment totaled $1,018,000. Total building expansion expenditures were $864,000, but $82,000 of the expenditures were included as part of construction payable and not as cash used in investing activities. Similarly, expenditures on the new ERP system in the first quarter of 2016 were $81,000 of which $14,000 was included as part of construction payable and not as cash used in investing activities. The remaining capital expenditures were mainly for upgrades to improve AMS production and process capabilities. Also, during the first three months of 2016, the Company incurred $14,000 in patent application costs that the Company records as an asset and amortizes upon successful completion of the application process. In addition, the Company sold a piece of equipment for $1,000.

Related to the Company's loan, the Company made principal payments of $35,000 during the first three months of 2017. During the first three months of 2016, the Company received $4,000 from financing activities from the issuance of 500 shares of common stock due to the exercise of stock options. There were no exercises of stock options during the first three months of 2017.

A bank line of credit exists providing for borrowings of up to $2,050,000 and expires on May 31, 2017. The line of credit is collateralized by the Company's assets and bears interest at 1.8 percentage points over the 30-day LIBOR rate. The Company did not utilize this line of credit during the first three months of 2017 or 2016 and there were no borrowings outstanding as of March 31, 2017 and December 31, 2016. There are no financial covenants related to the line of credit, and the Company expects to obtain a similar line of credit when the current line of credit expires.

The Company believes that current financial resources, its line of credit, cash generated from operations and secured through debt financing, and short-term investments, along with the Company's capacity for additional debt and/or equity financing will be sufficient to fund current and anticipated business operations. The Company also believes that it is unlikely that a decrease in demand for the Company's products would impair the Company's ability to fund operations given its excess cash and available line of credit.

Capital Expenditures

Through the first three months of 2017, the Company incurred $60,000 of capital expenditures mainly for improvements to production and process capabilities.

The Company expects additional capital expenditures in 2017 of approximately $530,000 mainly for AMS process improvements, enhancements to emulsion and film production and replacement automobiles for sales personnel. Currently, the Company expects to fund its capital expenditures with existing cash and cash generated from operating activities.

International Activity

The Company markets its products to numerous countries in North America, Europe, Latin America, Asia and other parts of the world. Foreign sales were approximately 29% of total sales during the first three months of 2017 compared to 31% of sales for the first three months of 2016. Export sales volume for the first three months of 2017 were down compared to the same period in 2016 due to a decrease in sales in Asia, Europe and the Middle East. Part of this decrease is timing related and the Company anticipates sales increasing in the second quarter of 2017. The fluctuations of certain foreign currencies have not significantly impacted the Company's operations, as the Company's foreign sales are not concentrated in any one region of the world, although a strong U.S. dollar does make the Company's products less competitive internationally. The Company believes its vulnerability to uncertainties due to foreign currency fluctuations and general economic conditions in foreign countries is not significant.

The Company's foreign transactions are primarily negotiated, invoiced and paid in U.S. dollars, while a portion is transacted in Euros. IKONICS has not implemented an economic hedging strategy to reduce the risk of foreign currency translation or transaction exposures, as management does not believe this to be a significant risk based on the scope and geographic diversity of the Company's foreign operations as of March 31, 2017. Furthermore, the impact of foreign exchange on the Company's balance sheet and operating results was not material in either 2017 or 2016.

Future Outlook

IKONICS has spent an average of approximately 4.0% of annual sales in research and development and has made capital expenditures related to new products and programs. The Company plans to maintain its efforts in these areas to expedite internal product development as well as to form technological alliances with outside entities to commercialize new product opportunities.

The Company continues to make progress on its AMS business initiative. Although AMS is experiencing a short-term drop in sales due to a temporary inventory overstocking by a major customer, the Company anticipates growth over the long term. The Company has two long-term agreements in place for its technology with major aerospace companies and is negotiating a third. In anticipation of this growing business, the Company increased its AMS capacity with a 27,300 square foot expansion at its Morgan Park site in 2016.

The Company is also continuing to pursue DTX-related business initiatives and anticipates the sale of two DTX printers in the second quarter of 2017. In addition to making efforts towards growing the inkjet technology business, the Company offers a range of products for creating texture surfaces and has introduced a fluid for use in prototyping. The Company is currently working on production improvements to enhance its customer offerings. The Company has been awarded European, Japanese, and United States patents on its DTX technologies. The Company has also modified its DTX technology to enter into the market for prototyping.

Both the Domestic and IKONICS Imaging units remain profitable in mature markets. Although these business units require aggressive strategies to grow market share, both are developing new products and business relationships that we believe will contribute to growth. In addition to its traditional emphasis on domestic markets, the Company will continue efforts to grow its business internationally by attempting to develop new markets and expanding market share where it has already established a presence. However, the strong U.S. dollar has made this challenging.

Other future activities undertaken to expand the Company's business may include acquisitions, building improvements, equipment additions, new product development and marketing opportunities.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, *Revenue from Contracts with Customers.* ASU 2014-09 supersedes the revenue recognition requirements in *Revenue Recognition (Topic 605*), and requires entities to recognize revenue in a way that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers: Deferral of the Effective Date,* which defers the adoption of ASU 2014-09 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. The standard permits two methods of adoption: retrospectively to each prior reporting period presented (full retrospective method), or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application (the cumulative catch-up transition method). The standard also requires expanded disclosures relating to the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. Additionally, qualitative and quantitative disclosures are required about customer contracts, significant judgments and changes in judgments, and assets recognized from the costs to obtain or fulfill a contract. While the Company is still in the process of evaluating the effect of adoption on its financial statements and is currently assessing its contracts with customers, the Company anticipates that it will expand its financial statement disclosures in order to comply with the new standard. The Company has established a timeline and process to evaluate the impact, transition and disclosure requirements of the ASU and believes the timeline is sufficient to allow the Company to effectively implement the new standard. The Company has not yet concluded on a transition method upon adoption, but plans to select a transition method by the fourth quarter of 2017.

During February 2016, the FASB issued ASU No. 2016-02, *Leases.* ASU No. 2016-02 was issued to increase transparency and comparability among organizations by recognizing all lease transactions (with terms in excess of 12 months) on the balance sheet as a lease liability and a right-of-use asset (as defined). ASU No. 2016-02 is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with earlier application permitted. Upon adoption, the lessee will apply the new standard retrospectively to all periods presented or retrospectively using a cumulative effect adjustment in the year of adoption. The Company is currently assessing the effect that ASU No. 2016-02 will have on its financial statements.

Off Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

ITEM 3. Quantitative and Qualitative Disclosures about Market Risk

Not applicable

ITEM 4. Controls and Procedures

As of the end of the period covered by this report, the Company conducted an evaluation, under the supervision and with the participation of the principal executive officer and principal financial officer, of the Company's disclosure control and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")). Based on this evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

There was no change in the Company's internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) and Rule 15d-15(d) of the Exchange Act that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

None

ITEM 1A. Risk Factors

Not applicable

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

Not applicable

ITEM 3. Defaults upon Senior Securities

Not applicable

ITEM 4. Mine Safety Disclosures

Not applicable

ITEM 5. Other Information

None

ITEM 6. Exhibits

The following exhibits are filed as part of this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2017:

Exhibit	Description
3.1	Restated Articles of Incorporation of Company, as amended.[1]
3.2	By-Laws of the Company, as amended.[2]
31.1	Rule 13a-14(a)/15d-14(a) Certifications of CEO
31.2	Rule 13a-14(a)/15d-14(a) Certifications of CFO
32	Section 1350 Certifications
101	Interactive Data Files Pursuant to Rule 405 of Regulation S-T

Copies of Exhibits will be furnished upon request and payment of the Company's reasonable expenses in furnishing the Exhibits.

(1) Incorporated by reference to the like numbered Exhibit to the Company's Registration Statement on Form 10-SB filed with the Commission on April 7, 1999 (File No. 000-25727).

(2) Incorporated by reference to the like numbered Exhibit to the Company's Current Report on Form 8-K filed with the Commission on February 22, 2007 (File No. 000-25727).

IKONICS CORPORATION

SIGNATURES

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

IKONICS CORPORATION

DATE: May 10, 2017	By:	/s/ Jon Gerlach
		Jon Gerlach, Chief Financial Officer, and Vice President of Finance

INDEX TO EXHIBITS

Exhibit	Description	Page
3.1	Restated Articles of Incorporation of Company, as amended	Incorporated by reference
3.2	By-Laws of the Company, as amended.	Incorporated by reference
31.1	Rule 13a-14(a)/15d-14(a) Certifications of CEO.	Filed Electronically
31.2	Rule 13a-14(a)/15d-14(a) Certifications of CFO.	Filed Electronically
32	Section 1350 Certifications.	Filed Electronically
101	Interactive Data Files Pursuant to Rule 405 of Regulation S-T	Filed Electronically

EXHIBIT 31.1

RULE 13a-14(a)/15d-14(a) CERTIFICATIONS OF CEO

I, William C. Ulland, certify that:

1. I have reviewed this quarterly report on Form 10-Q of IKONICS Corporation;

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 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-15f and 15d-15(f)) for the registrant and we 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 (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) 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.

5. The registrant’s other certifying officer 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, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 10, 2017

/s/ William C. Ulland
William C. Ulland
Chairman, Chief Executive Officer
and President

EXHIBIT 31.2

RULE 13a-14(a)/15d-14(a)/CERTIFICATIONS OF CFO

I, Jon Gerlach, certify that:

1. I have reviewed this quarterly report on Form 10-Q of IKONICS Corporation;

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 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-15f and 15d-15(f)) for the registrant and we 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 (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) 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.

5. The registrant's other certifying officer 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, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 10, 2017

/s/ Jon Gerlach
Jon Gerlach
Chief Financial Officer
and Vice President of Finance

EXHIBIT 32

SECTION 1350 CERTIFICATIONS

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, each of the undersigned certifies that this periodic report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in this periodic report fairly presents, in all material respects, the financial condition and results of operations of IKONICS Corporation.

Date: May 10, 2017

/s/ William C. Ulland
William C. Ulland
Chairman, Chief Executive Officer
and President

Date: May 10, 2017

/s/ Jon Gerlach
Jon Gerlach
Chief Financial Officer
and Vice President of Finance