SECTOR 10 INC
Form 10-Q
August 14, 2009

UNITED STATES SECURITIES

AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED **June 30, 2009**

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

SECTOR 10, Inc.

(Formerly SKRM Interactive, Inc.)

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

Delaware	**000-24370**	**33-0565710**

(State or other jurisdiction of incorporation)	*(Commission File No.)*	*(IRS Employer Identification No.)*

14553 South 790 West

Bluffdale, Utah 84065

(Address of principal executive offices, including zip code)

Issuer s telephone number, including area code: **(206) 853-4866**

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

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

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer ¨ Smaller reporting company þ

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

As of August 10, 2009 the issuer had 11,453,573 shares of common stock outstanding.

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

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FINANCIAL STATEMENTS

SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

CONSOLIDATED BALANCE SHEETS

		June 30, 2009 (Unaudited)		March 31, 2009 (Audited)
ASSETS				
Current assets:				
Cash	$	41	$	35,016
Accounts receivable		2,000		2,000
Inventory		18,409		18,409
Prepaid assets		4,167		37,291
Total current assets		24,617		92,716
Fixed Assets:				
Furniture		9,182		9,182
Computers		13,068		13,068
Total fixed asset cost		22,250		22,250
Less: accumulated depreciation		(6,823)		(5,710)
Net fixed assets		15,427		16,540
Other assets:				
Deposits				10,000
Network acquisition/development costs		1,147,995		1,147,995
Total other assets		1,147,995		1,157,995
Total assets	$	1,188,039	$	1,267,251
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities:				
Accounts payable and accrued liabilities	$	609,809	$	400,152
Deferred revenue		18,500		18,500
Note payable		451,000		451,000
Note payable officer / shareholder		21,831		38,754

Total current liabilities		1,101,140		908,406
Shareholders' equity:				
Preferred shares - $0.001 par value; 1,000,000 authorized, no shares issued or outstanding				
Common shares - $0.001 par value; 199,000,000 authorized; 11,393,573 and 10,143,530 shares issued and outstanding, respectively		11,394		10,144
Additional paid in-capital		1,156,508		1,009,008
Deficit accumulated during the development stage		(1,081,003)		(660,307)
Total shareholders' equity		86,899		358,845
Total liabilities and shareholders' equity	$	1,188,039	$	1,267,251

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

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SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

FOR THE THREE MONTHS ENDED JUNE 30, 2009 AND 2008 AND FOR THE PERIOD FROM INCEPTION,

SEPTEMBER 16, 2002 TO JUNE 30, 2009

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Inception to June 30, 2009
Sales	$	$	$ 18,500
Cost of Sales			18,032
Gross Profit			468
Expenses:			
General and administrative	412,337	240,132	1,563,562
Total expenses	412,337	240,132	1,563,562
Income (loss) from operations	(412,337)	(240,132)	(1,563,094)
Interest expense	(8,359)	(3,325)	(35,109)
Other income: debt restructuring		517,200	517,200
Net Income (loss)	$ (420,696)	$ 273,743	$ (1,081,003)
Weighted Average Shares Outstanding basic and diluted	10,636,384	8,669,480	
Basic and diluted income (loss) per share			
Continuing Operations	$ (0.04)	$ 0.03	
Net Loss	$ (0.04)	$ 0.03	

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

SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

UNAUDITED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (DEFICIT)

	Common Stock						
	Shares		Amount		Additional Paid-In Capital		Deficit Accumulated During the Development Stage
Balance at March 31, 2009	10,143,530	$	10,144	$	1,009,008	$	(660,307)
Issue shares on April 8, 2009 @$.30 per share to John Gargett for Director Fees (unaudited)	50,000		50				
Issue shares on April 22, 2009 to Layne Davis @$.20 per share for Product Design (unaudited)	27,500		28		5,472		
Issue shares on April 24, 2009 to QualityStocks, LLC @$.30 per share for Investor Relations (unaudited)	37,500		37		11,213		
Issue shares on April 24, 2009 to Illuminated Financial @$.20 per share for Investor Relations (unaudited)	25,000		25		4,975		
Authorize issue of shares on May 1, 2009 to officers @$.10 per share for prior year accrued services (unaudited)	900,000		900		89,100		
Authorize issue of shares on May 1, 2009 to directors @$.10 per share for current year board service (unaudited)	150,000		150		14,850		
Issue shares to John Gargett on May 8, 2009 @$.10 per share per employment contract (unaudited)	50,000		50		4,950		
Issue shares to Patrick Love on May 15, 2009 @$.20 per share per employment contract (unaudited)	10,000		10		1,990		

Issue Shares on May 19, 2009 as a result of Reverse stock split (unaudited)							
Net loss for the period (unaudited)							(420,696)
Balance at June 30, 2009 (unaudited)	11,393,573	$	11,394	$	1,156,508	$	(1,081,003)

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

SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Inception to June 30, 2009
Cash Flows from Operating Activities:			
Net income (loss)	$ (420,696)	$ 273,743	$ (1,081,003)
Adjustments to reconcile net loss to net cash used in operating activities:			
Stock for services	91,874	194,831	638,582
Depreciation	1,113	1,113	6,823
Gain on debt restructuring		(517,200)	(517,200)
Changes in			
Accounts receivable			(2,000)
Inventory			(18,409)
Deposits	10,000		
Accounts payable and accrued liabilities	310,060	37,121	790,826
Deferred revenue			18,500
Net cash used in operating activities	(7,649)	(10,392)	(163,881)
Cash Flows from Investing Activities:			
Fixed asset purchases			(22,250)
Network acquisition / development costs		(97,995)	(147,995)
Net cash used in investing activities		(97,995)	(170,245)
Cash Flows from Financing Activities:			
Bank overdraft		(692)	
Proceeds from general financing		200,000	451,000
Proceeds from Shareholder /Officers	19,974	32,808	902,795
Payments to Shareholder/Officers	(47,300)	(123,406)	(1,023,214)
Proceeds from issuance of common stock			3,586
Net cash provided (used) by financing activities	(27,326)	108,710	334,167
Net increase (decrease) in cash and cash equivalents	(34,975)	323	41
Beginning of the year cash balance	35,016		
Ending of the period cash balance	$ 41	$ 323	$ 41

Cash paid for interest	$	$	$
Cash paid for income taxes	$	$	$

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

SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - BASIS OF PRESENTATION

The accompanying unaudited consolidated condensed financial statements of Sector 10, Inc. (Sector 10 or the Company), have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and required by Rule 10-01 of Regulation S-X. They do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation, have been included in the accompanying unaudited consolidated financial statements. Operating results for the periods presented are not necessarily indicative of the results that may be expected for the full year.

Note 2 INVENTORY

The Company uses Dutro Company as an outsourced manufacturing company. The Dutro Company provides the Company with details regarding inventory on hand and related costs. The inventory on hand at March 31, 2009 was $18,409. Sales activity and related purchase orders were minimal for the fiscal year ended March 31, 2009 and no sales activity occurred in the quarterly period ended June 30, 2009. In accordance with the Manufacturing Agreement with Dutro Company, purchase orders will be negotiated for all sales activity. Dutro Company will provide reports to the Company regarding the status of all purchase order requested and the total finished goods inventory on hand. The Company relies on information provided by Dutro Company to record inventory on the Company books.

All inventory on hand is available for sale. As sales and related production activity increases the Company will with the assistance of the outsourced manufacturer periodically makes judgments and estimates regarding the future utility and carrying value of its inventory. The carrying value of inventory is periodically reviewed and impairments, if any, are recognized when the expected future benefit from the inventory is less than its carrying value. If applicable, the Company will establish inventory reserves for estimated obsolescence or unmarketable inventory which is equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. For the period ended June 30, 2009, the Company has no inventory reserve.

Note 3 NETWORK ACQUISITION/DEVELOPMENT COSTS

On May 19, 2008 Sector 10, Inc. (Sector 10 or Company) entered into an agreement with its major shareholder Sector 10 Holdings, Inc. (Holdings). Holdings currently owns over 50% of the outstanding shares of Sector 10, Inc. Holdings had developed a Server Network to maintain and administer products and services that had been developed within specifications to manage the SRU and MRU safety products.

The network has fully integrated capabilities for distribution services including the worldwide transmission of video and audio broadcasts, with content management services that archive data under a redundant system with various server clusters across the nation to service Sector10 s National and world-wide requirements. In addition to providing for the normal Sector 10 products such as the SRU and SRU- Media, the Network also has the capability to provide other services. The development costs include the licensed rights to proprietary software including the PLX-3D software which is used for the monitoring and tracking services provided with the SRU/MRU.

The network was transferred from Holdings to the Company at a cost of $1,000,000 which reflects the prior development costs incurred by Holdings prior to the transfer. As part of the agreement, the Company agreed to pay for development costs that were due in the month of transfer. This expense amounted to $97,995 in May 2008. An additional $50,000 was accrued for development expenses incurred prior to the year ended March 31, 2009. The transfer was reflected as Network acquisition /development costs and the Company issued 1,250,000 common shares that were valued at $.80 per share for total value of $1,000,000. The shares and related conversion price were adjusted to reflect the subsequent reverse stock split.

SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Note 3 NETWORK ACQUISITION/DEVELOPMENT COSTS (Continued)

The Network is treated as a Long Lived Asset which is reviewed regularly for impairment. In its review for impairment, the Company prepares estimates of future cash flows to assist in the determination of the asset s recoverability. If there is an issue regarding recoverability, an independent valuation will be obtained to determine any required adjustment for impairment The estimates used in determining for recoverability are updated by the Company on a regular basis to provide guidance for Management s quarterly and annual reporting. Based on the estimates prepared for the fiscal year end March 31, 2009, Management has determined that the Network Asset is recoverable and not subject to an adjustment for impairment.

The Network is not in service as of the period ended June 30, 2009. It is expected to be placed in service in the fiscal year ended March 31, 2010. Once, placed in service, the asset will be depreciated over its estimated useful life which is currently estimated to be 7 to 10 years. The Company has not completed its review of the final depreciable life for the Network asset.

The Company has determined that the performance of the administrator has been inadequate and the administration agreement was cancelled. The performance issues have resulted in various disagreements with the administrator. As part of the termination, the Company has requested the return of all servers and related software and other equipment for deployment in other secure facilities with a new administrator. The administrator has not provided the return of the equipment at this stage. In addition, the administrator is seeking payment of fees and has filed a claim for $58,732 of fees due. Although the fees at issue are attributable to services for the Company, the claim was not filed against the Company.

The Company disagrees with the total fees but has recorded the full amount in the financial statements. The Company has disputed this claim and considering legal options to provide the transfer the equipment to another administrator. The disputed fees include charges for consulting fees that are being challenged since the network is not in service. Removing the consulting fees included in the $58,732 and the consulting fees paid with the acquisition of the equipment, the Company has a credit balance of $4,000. The dispute is expected to be resolved before any significant sales activity begins. If needed, the Company will purchase additional servers as required to perform any required administration for new business in the next fiscal year. Any additional expenses needed to cover the IT administration during this dispute will be included as potential damages in any future legal considerations.

Note 4 DEPOSIT

The Company was approached by DPO Medical, Inc. with respect to the possible acquisition of a medical product that (if acquired) could produce immediate revenues to assist in providing the Company with cash flow during their growth period. In order to hold the rights during its due diligence review, the Company on September 15, 2008, placed a $25,000 refundable deposit with DPO Medical, Inc. The Company completed its due diligence review subsequent to the quarter ended September 30, 2008 and decided that it was not in the Company s best interest to pursue the acquisition of the medical product offered by DPO Medical. Accordingly, the Company has requested the full refund of the $25,000 deposit. The deposit has been recorded as an asset on the balance sheet for the period ended December 31, 2008. A total of $15,000 of the deposit was received in January 2009. The balance of $10,000 was still outstanding as of the year ended March 31, 2009. The final $10,000 deposit was received in May 2009.

SECTOR 10, INC.

(A DEVELOPMENT STAGE COMPANY)

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Note 5 DEBT CONVERSION

On May 8, 2008, Sector 10, Inc. (Sector 10) and Jeffrey Martin (Martin) agreed to convert all outstanding debt owed Martin to common shares of Sector 10, Inc. A brief description of the transaction and the related background is as follows.

Martin transferred 120,000 (adjusted for reverse stock split) SKRM Interactive, Inc. common shares (Martin Transfer) that were owned by Martin and/or related parties to various individuals in satisfaction of pre-acquisition debt. As a result of the Martin transfer, Sector 10 recorded $649,200 in liabilities due Martin on its books for the fiscal year end March 31, 2008.

Martin agreed to convert the debt into Sector 10 shares in an amount equal to the number of shares used by Martin in the Martin Transfer. Sector 10 agrees to issue 120,000 new shares (adjusted for reverse stock split) of Sector 10, Inc. in complete and total satisfaction of the $649,200 debt to Martin and in satisfaction of any other unrecorded debt that may exist between Martin and Sector 10.

The 120,000 shares were issued during the quarter ended June 30, 2008. The accounting for the debt conversion consisted of reclassification of the note payable of $649,200 to additional paid-in-capital ($131,880) and capital stock ($120). The value of the shares issued on May 8, 2008 was $132,000. The $517,200 difference between the value and the debt converted was treated as other income.

Note 6 NOTES PAYABLE