

DYNARESOURCE INC

Form 10-Q

November 14, 2017

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2017

OR

[] TRANSITION REPORT UNDER SECTION 13 OF 15(d) OF THE EXCHANGE ACT OF 1934

From the transition period _____ to _____.

Commission File Number 000-30371

DYNARESOURCE, INC.

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

Delaware

94-1589426

(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

222 W Las Colinas Blvd., Suite 744 East Tower, Irving, Texas 75039

(Address of principal executive offices)

(972) 868-9066

(Issuer's telephone number)

N/A

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days:

Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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:

Large Accelerated Filer ☐

Accelerated Filer ☐

Non-Accelerated Filer ☐ Smaller Reporting Company ☒

Indicate by a check mark whether the company is a shell company (as defined by Rule 12b-2 of the Exchange Act):

Yes ☐ No ☒

As of November 13, 2017, there were 17,722,825 shares of Common Stock of the issuer outstanding.

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CERTIFICATIONS

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EXHIBIT 31.2	CHIEF FINANCIAL OFFICER CERTIFICATION
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PART I**ITEM 1.****FINANCIAL STATEMENTS****DYNARESOURCE, INC.****Consolidated BALANCE SHEETS****SEPTEMBER 30, 2017 AND DECEMBER 31, 2016**

	Sept 30, 2017	Dec 31, 2016
ASSETS		
Current Assets:		
Cash and Cash Equivalents	\$3,548,315	\$2,197,005
Accounts Receivable	435,473	454,140
Inventories	1,065,785	561,238
Foreign Tax Receivable	1,136,090	1,083,364
Other Current Assets	121,095	73,871
Total Current Assets	6,306,758	4,369,618
Mining Equipment and Fixtures (Net of Accumulated Depreciation of \$950,380 and \$821,132	825,993	578,743
Mining Concessions (Net of Accumulated Amortization)	4,132,678	4,132,678
Investments in Affiliate	70,000	70,000
Other Assets	143,117	15,450
TOTAL ASSETS	\$11,478,546	\$9,166,489
LIABILITIES AND EQUITY		
Current Liabilities:		
Accounts Payable	\$1,665,721	\$851,197
Convertible Notes Payable	950,625	956,250
Due to Non-Controlling Interest	231,500	231,500
Accrued Expenses	998,372	1,367,510
Derivative Liabilities	2,649,027	5,106,090
Total Current Liabilities	6,495,245	8,512,547
Long-Term Liabilities:		
Accrued Expenses	265,028	—
TOTAL LIABILITIES	\$6,760,273	\$8,512,547
Preferred Stock, Series C, \$.0001 par value, 1,733,221 shares Authorized, 1,733,221 outstanding as of 2017 and 2016	\$4,333,053	\$4,333,053
Stockholders' Equity Deficit		

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Preferred Stock, Series A, \$.0001 par value, 1,000 shares		
Authorized, 1,000 and 1,000 issued and outstanding	\$ 1	\$ 1
Common Stock, \$.01 par value, 25,000,000 shares authorized, 17,722,825 and 16,722,825 shares outstanding as of 2017 and 2016	177,228	167,228
Preferred Rights	40,000	40,000
Additional Paid In Capital	57,573,783	55,083,783
Treasury Stock, 1,112,313 outstanding as of 2017 and 2016	(3,175,515) (3,175,515)
Accumulated Other Comprehensive Income	1,741,749	3,771,532
Accumulated Deficit	(50,515,213) (53,581,567)
Total DynaResource, Inc. Stockholders' Equity	5,842,033	2,305,462
Non-controlling Interest	(5,456,813) (5,984,573)
TOTAL (DEFICIT)	\$385,220	\$(3,679,111)
 TOTAL LIABILITIES AND EQUITY (DEFICIT)	 \$11,478,546	 \$9,166,489
The accompanying notes are an integral part of these consolidated financial statements.		

DYNARESOURCE, INC.**Consolidated Statements of Operations and Comprehensive Loss**

	Three Months	Three Months	Nine Months	Nine Months
	Sept 30, 2017	Sept 30, 2016	Sept 30, 2017	Sept 30, 2016
REVENUES	\$2,674,015	\$3,027,305	\$7,233,329	\$8,192,230
COSTS AND EXPENSES OF MINING OPERATIONS				
Production Costs Applicable to Sales	928,663	443,703	2,586,553	1,308,858
Mine Operating Costs	1,100,948	1,061,073	2,659,093	3,036,423
Property Holding Costs	135,681	153,286	398,751	370,986
General and Administrative	616,036	653,429	1,805,373	1,666,029
Depreciation and Amortization	36,781	29,496	129,248	77,626
Total Operating Expenses	2,818,109	2,340,987	7,579,018	6,459,922
NET OPERATING INCOME (LOSS)	(144,094)	686,318	(345,689)	1,732,308
OTHER INCOME (EXPENSE)				
Foreign Currency Gains (Losses)	195,042	(460,885)	890,491	(1,603,758)
Interest Expense	(27,533)	(29,883)	(89,203)	(89,649)
Gain (Loss) on Derivatives	753,626	(204,279)	2,457,063	—
Other Income	257	185	654	545
Total Other Income (Expense)	921,392	(694,862)	3,259,005	(1,692,862)
NET INCOME (LOSS) BEFORE TAXES	777,298	(8,544)	2,913,316	39,446
TAXES	—	—	—	—
NET INCOME (LOSS)	\$777,298	\$(8,544)	\$2,913,316	\$39,446
Cumulative Dividend for Series C Preferred	(42,737)	(40,000)	(128,211)	(120,000)
ATTRIBUTABLE TO NON-CONTROLLING INTERESTS	\$(49,397)	\$10,756	\$153,038	175,536
ATTRIBUTABLE TO COMMON SHAREHOLDERS	\$685,164	\$(37,788)	\$2,938,143	\$94,982
EARNINGS PER SHARE DATA				
ATTRIBUTABLE TO THE EQUITY HOLDERS OF DYNARESOURCE, INC:				
Basic Loss per Common Share	\$.04	\$(.00)	\$0.17	\$.01
Diluted Loss per Common Share	\$.00	(.00)	0.03	.01

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Weighted Average Shares Outstanding, Basic	17,124,999	16,722,825	16,858,356	16,722,825
Weighted Average Shares Outstanding, Diluted	18,725,897	16,722,825	18,977,097	16,722,825
OTHER COMPREHENSIVE INCOME (LOSS)				
NET INCOME (LOSS) PER ABOVE	\$777,298	\$(8,544)	\$2,913,316	\$39,446
Foreign Currency Exchange Gains (Losses)	2,571,845	(1,083,766)	2,313,973	(1,813,703)
TOTAL COMPREHENSIVE INCOME (LOSS)	\$3,349,143	\$(1,092,310)	\$5,227,289	\$(1,774,257)
ATTRIBUTABLE TO:				
EQUITY HOLDERS OF DYNARESOURCE, INC.	\$907,344	\$92,685	\$3,878,304	\$(269,442)
NON-CONTROLLING INTERESTS	\$2,441,799	\$(1,184,995)	\$1,348,985	\$(1,504,815)
TOTAL COMPREHENSIVE INCOME (LOSS)	3,349,143	(1,092,310)	5,227,289	(1,774,257)

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

DYNARESOURCE, INC.**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	September 30, 2017	September 30, 2016
	(Unaudited)	(Unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income (Loss)	\$2,913,316	\$39,446
Adjustments to reconcile net loss to cash provided by (used in) Operating activities		
Gain on Derivative Liabilities	(2,457,063)	—
Depreciation and Amortization	129,248	77,626
Change in Operating Assets and Liabilities:		
Accounts Receivable	77,451	(462,358)
Inventory	(411,736)	(500,133)
Other Current Assets	(47,224)	(189,863)
Receivables from Affiliate	(26,917)	(8,602)
Foreign Tax Receivable	91,222	(464,472)
Other Assets	(144,954)	(1,689)
Accounts Payable	1,157,521	22,669
Accrued Liabilities	(604,918)	466,132
CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES	675,946	(1,021,244)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Equipment	(327,786)	(127,997)
CASH FLOWS (USED IN) INVESTING ACTIVITIES	(327,786)	(127,997)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payment on Advances to Related Party	—	(150,000)
Payment of Dividends	—	(160,000)
Payment on Note Payable	(5,625)	—
Payment on Accrued LT	(155,856)	—
Proceeds on Sale of Common Stock	2,500,000	—
CASH FLOWS PROVIDED BY FINANCING ACTIVITIES	2,338,519	(310,000)
Effect of Foreign Exchange	(1,335,369)	1,890,284
NET DECREASE IN CASH	1,351,310	431,043
CASH AT BEGINNING OF PERIOD	2,197,005	1,922,599
CASH AT END OF PERIOD	\$3,548,315	\$2,353,642

SUPPLEMENTAL DISCLOSURES

Cash Paid for Interest	\$ 89,203	\$ 89,648
Cash Paid for Income Taxes	\$—	\$—

NON CASH TRANSACTIONS

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

DYNARESOURCE, INC.

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2017

NOTE 1 – NATURE OF ACTIVITIES AND SIGNIFICANT ACCOUNTING POLICIES

Nature of Activities, History and Organization

DynaResource, Inc. (The “Company”, “DynaResource”, or “DynaUSA”) was organized September 28, 1937, as a California corporation under the name of West Coast Mines, Inc. In 1998, the Company re-domiciled to Delaware and changed its name to DynaResource, Inc. The Company is in the business of acquiring, investing in, and developing precious metal properties, and in the test mining and pilot milling production of precious metals.

The interim consolidated financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) has been condensed or omitted pursuant to such rules and regulations, although the Company believes that the disclosures included are adequate to make the information presented not misleading.

In management’s opinion, the unaudited Consolidated Statements of Operations and Comprehensive Income for the nine months ended September 30, 2017 and 2016, the Consolidated Balance Sheets as at September 30, 2017 (unaudited) and December 31, 2016, and the unaudited Consolidated Statements of Cash Flows for the nine months ended September 30, 2017 and 2016, contained herein, reflect all adjustments, consisting solely of normal recurring items, which are necessary for the fair presentation of the Company’s financial position, results of operations and cash flows on a basis consistent with that of the Company’s prior audited annual consolidated financial statements. However, the results of operations for the interim periods may not be indicative of results to be expected for the full fiscal year. Therefore, these financial statements should be read in conjunction with the audited financial statements and notes thereto and summary of significant accounting policies included in the Company’s Form 10-K for the year ended December 31, 2016. Except as noted below, there have been no material changes in the footnotes from those accompanying the audited consolidated financial statements contained in the Company’s Form 10-K for the year ended December 31, 2016. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All inter-company accounts and transactions have been eliminated.

In the second quarter 2017, we identified certain property taxes amounting to \$541,245 from 2014, 2015, and \$169,232 for 2016, which were not expensed as required and an over accrual of \$150,000 for legal expenses at December 31, 2016. Based on Staff Accounting Bulletin No. 108 (“SAB 108”), we have determined that these amounts are immaterial to each of the time periods affected and, therefore, we are not required to amend our previously filed reports. However, if these adjustments were recorded in 2017, we believe the impact could be material to this year. Therefore, we plan to adjust our previously reported results for 2014, 2015, and 2016 for these immaterial amounts as required by SAB 108. Such previous periods will be restated upon the next filing of our quarterly and annual consolidated financial statements. The balance sheet as of December 31, 2016 has been adjusted to reflect the cumulative impact of such errors. As a result, Accounts payable has been increased by \$541,245, accrued expenses

increased by \$169,232 and retained earnings decreased by \$710,477. For additional information, see Footnote 14.

Reclassifications

Certain financial statement reclassifications have been made to prior period balances to reflect the current period's presentation format; such reclassifications had no impact on the Company's consolidated statements of operations or consolidated statements of cash flows and had no material impact on the Company's consolidated balance sheets.

Computation of Profit (Loss) per Share

Basic Income (Loss) per share is computed by dividing the period Income (Loss) available to common shareholders by the weighted average number of common shares outstanding. Diluted Profit (Loss) per share is computed by dividing the Income (Loss) available to common shareholders by the weighted average number of common shares outstanding plus additional common shares that would have been outstanding if dilutive potential common shares had been issued. For purposes of this calculation, convertible preferred stock, common stock dividends, warrants and options to acquire common stock, are all considered common stock equivalents in periods in which they have a dilutive effect and are excluded from this calculation in periods in which these are anti-dilutive or to the net loss. The securities for the three-month period ending September 30, 2017 and September 30, 2016 were deemed antidilutive.

The following table illustrates the computation of Profit (loss), for the three months and nine months ended September 30, 2016 and 2017:

	Three Months	Three Months	Nine Months	Nine Months
	Sept 30, 2017	Sept 30, 2016	Sept 30, 2017	Sept 30, 2016
Numerator				
Profit (Loss)	\$685,164	\$(37,788)	\$2,938,143	\$94,982
Preferred dividends accrued	42,737	—	128,211	—
Gain on Derivatives	(753,626)	—	(2,457,063)	—
Net Profit (Loss) applicable to common shareholders	\$(25,725)	\$(37,788)	\$609,291	\$94,982
Denominator for basic and dilutive loss per share:				
Weighted average common stock shares outstanding	17,124,999	16,722,825	16,858,356	16,722,825
Net effect of dilutive common stock equivalents	1,600,898	—	2,118,741	—
Weighted average shares outstanding – diluted	18,725,897	16,722,825	18,977,097	16,722,825
Income Profit (Loss) per share – basic	\$.04	\$(.00)	\$.17	\$.01
Income Profit (Loss) per share – diluted	\$.00	\$(.00)	\$.03	\$.01

NOTE 2 – INVENTORIES

The Company commenced underground test mining and pilot milling activities (“pilot production”) in the 2nd quarter of 2014. Rehabilitation of the San Pablo Mine and refurbishing of the Pilot Mill Facility and construction of the adjacent tailings pond continued through 2016, and expansion of these activities commenced in second quarter 2017.

Inventories are carried at the lower of cost or fair value and consist of mined tonnage, gravity-flotation concentrates, and gravity tailings (or, flotation feed material). Inventory balances of September 30, 2017 and December 31, 2016, respectively, were as follows:

	09/30/17	12/31/16
Mined Tonnage Stockpiled	\$674,382	\$445,082
Mill Tonnage Stockpiled	308,964	116,156
Finished Material	82,439	—
Total Inventories	\$1,065,785	\$561,238

NOTE 3 – PROPERTY

Property consists of the following at September 30, 2017 and December 31, 2016:

	09/30/17	12/31/16
Mining camp equipment	\$653,651	\$399,180
Transportation equipment	282,379	282,379
Machinery and equipment	587,280	470,741

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Office furniture and fixtures	78,709	75,829
Office equipment	174,314	171,746
Sub-total	1,776,373	1,399,875
Less: Accumulated depreciation	(950,380)	(821,132)
Total Property	\$ 825,993	\$ 578,743

The Company purchased equipment of \$327,786 and \$127,997 in the nine months ended September 30, 2017 and September 30, 2016, respectively.

Depreciation has been provided over each asset's estimated useful life. Depreciation expense was \$129,248 and \$77,626 for the nine months ended September 30, 2017 and 2016, respectively.

NOTE 4 – MINING CONCESSIONS

Mining properties consist of the following at September 30, 2017 and December 31, 2016:

	09/30/17	12/31/16
San Jose de Gracia ("SJG"):		
Total Mining Concessions	\$4,132,678	\$4,132,678

Depletion expense was \$nil and \$nil for the nine months ended September 30, 2017 and 2016 respectively, respectively.

NOTE 5 – INVESTMENT IN AFFILIATE/RECEIVABLES FROM AFFILIATE/OTHER ASSETS

Through December 31, 2016, the Company loaned a total of \$805,760 to DynaResource Nevada, Inc. ("DynaNevada"), a Nevada Corporation, which owns 100% of one operating subsidiary in México, DynaNevada de México, S.A. de C.V. ("DynaNevada de México"). The terms of the Note Receivable provided for a "Convertible Loan", repayable at 5% interest over a 3-year period, and convertible at the Company's option into common stock of DynaNevada at \$.25 / Share. DynaNevada is a related entity (affiliate), and through its subsidiary, DynaNevada de México has entered into an Option agreement with Grupo México (IMMSA) in México, for the exploration and development of approximately 3,000 hectares in the State of San Luis Potosi ("The Santa Gertrudis Property"). DynaNevada de México exercised the Option with IMMSA in March 2010, so that DynaNevada de México now owns 100% of the Santa Gertrudis Property. In June 2010, DynaNevada de México acquired an additional 6,000 hectares in the State of Sinaloa (the "San Juan Property"). As of September 30, 2017, and December 31, 2016 the investment was \$70,000.

NOTE 6 – CONVERTIBLE PROMISSORY NOTES

Notes Payable – Series I

In April and May 2013, the Company entered into note agreements with shareholders in the principal amount of \$1,495,000, of which \$340,000 was then converted to preferred shares within the same year, netting to proceeds of \$1,155,000 (the "Series I Notes"). The Series I Notes bear simple interest at twelve and a half percent (12.5%), accrued for twelve months, and with the accrued interest to be added to the principal, and then interest will be paid by the Company, quarterly in arrears. The holders of the Series I Notes (in aggregate) are also entitled to receive ten percent (10%) of the net profits received by the Company, on the first fifty thousand tons processed through the mill facilities at San Jose de Gracia. Such net profits (if any) are to be calculated after deducting "all expenses related to the production", and after a prior deduction of thirty-three percent (33%) from the net profits, to be deposited into a sinking fund cash reserve. To date, the Company has not produced any net profits as calculated in accordance with the Series I Notes.

The Notes originally matured on December 31, 2015. In April 2015, the Company received note extensions (allonges) from all Series I note holders to ensure that all Series I Notes were in good standing and also extended the maturity

date of the Series I Notes to December 31, 2016. At December 31, 2016, one of the Series I Notes remained outstanding for a total of \$5,801 and was paid in 2017, one of the Series I Notes was further extended to September 30, 2017, and the remaining Series I Notes were further extended to December 31, 2017. The balance of the Notes at September 30, 2017 was \$950,625.

The Company has the right to prepay the Series I Notes with a ten percent (10%) penalty.

The Series I Note holder retains the option, at any time prior to maturity or prepayment, to convert any unpaid principal and accrued interest into Common Stock at \$5.00 per share. If the Series I Note is converted into Common Stock, at the time of conversion, the holder would also receive warrants, in the same number as the number of common shares received upon conversion, to purchase additional common shares of the Company for \$7.50 per share, with such warrants expiring on December 31, 2018.

Notes Payable – Series II

In 2013 and 2014, the Company entered into additional note agreements of \$199,808 and \$250,000, respectively (the “Series II Notes”) with similar terms as the Series I Notes. The Series II Notes bear simple interest at twelve and a half percent (12.5%), accrued for twelve months, and with the accrued interest to be added to the principal, and then interest will be paid by the Company, quarterly in arrears. The holders of the Series II Notes (in aggregate) are also entitled to receive ten percent (10%) of the net profits received by the Company, on the second fifty thousand tons processed through the mill facilities at San Jose de Gracia. Such net profits (if any) are to be calculated after deducting “all expenses related to the production”¹, and after a prior deduction of thirty-three percent (33%) from the net profits, to be deposited into a sinking fund cash reserve. To date, the Company has not produced any net profits as calculated in accordance with the Series II Notes.

The Notes originally matured on December 31, 2015. In April 2015, the Company received allonges (note extensions) from all noteholders to ensure that all notes were in good standing and also confirmed the maturity of the Series II notes to be December 31, 2016. At December 31, 2016, the remaining Series II Notes were further extended to December 31, 2017.

The Company has the right to prepay the Series II Notes with a ten percent (10%) penalty.

The Note holder may, at any time prior to maturity or prepayment, convert any unpaid principal and accrued interest into common stock of the Company at \$5.00 per share. At the time of conversion, the holder would receive a warrant to purchase additional common shares of the Company for \$7.50 per share, such warrant expiring on December 31, 2018.

On June 30, 2015, the Company entered into conversion agreements with six (6) note holders. Principal and interest in the amount of \$809,784 plus \$33,120 of accrued interest (total of \$842,903) was contracted to convert into 337,162 common shares. In addition, 337,162 warrants were issued which provide the option to purchase common shares at \$2.50, with all warrants expiring December 31, 2017. The Company recorded \$826,347 inducement expense related to these conversion transactions. On August 17, 2015, these common shares and warrants were issued.

At September 30, 2017, the principal and capitalized interest balance on the remaining Series I Notes was \$759,375, and the principal and capitalized interest on the Series II Notes was \$191,250, for a total Note balance of \$950,625. The accrued interest for these notes was \$29,965 and \$29,883 as of September 30, 2017 and 2016, respectively.

Notes Payable

In June 2017, the Company entered into financing agreements in the amount of \$541,245 in order to retain the rights to, and maintain exploratory mineral concessions. The Company paid twenty percent as an initial payment, \$108,249, and financed the balance, payable over thirty-six months. In accordance with the Company's policy of treatment of exploratory mineral concessions or properties, the Company capitalized all costs associated with the financing of the exploratory mineral concessions, including annual taxes or fees, and the Company expects to prepare an annual impairment analysis.

The following is a summary of the Notes Payable at September 30, 2017 and December 31, 2016:

	2017	2016
Convertible Promissory Notes Current Portion	\$956,250	\$956,250
Purchase of Note	(5,625)	—
Total Notes Payable	\$950,625	956,250

NOTE 7 – Long Term Accrued Expense

In June 2017, the Company entered into financing agreements for unpaid mining concession taxes for the period July 1, 2014 through December 31, 2015 in the amount of \$541,245. The Company paid 20% as an initial payment, \$108,249, and financed the balance over thirty-six months.

The following is a summary of the transactions during the second and third quarters:

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	Sept 30, 2017
Property Holding Taxes June 1, 2014 – December 31, 2015	\$541,245
Initial payment of 20%	(108,249)
2017 principal payments	(47,607)
Balance at September 30, 2017	\$385,389
Short-Term Portion	\$120,361
Long-Term Portion	265,028
Total	\$385,389

NOTE 8 – STOCKHOLDERS' EQUITY

The only change in our stockholders' equity in the three and nine months ended September 30, 2017 was the exercise of 1,000,000 warrants for cash at \$2.50 per share.

Authorized Capital. The total number of shares of all classes of capital stock which the corporation shall have the authority to issue is 45,001,000 shares, consisting of (i) twenty million and one thousand (20,001,000) shares of Preferred Stock, par value \$0.0001 per share ("Preferred Stock"), of which one thousand (1,000) shares shall be designated as Series A Preferred Stock and (ii) twenty-five million (25,000,000) shares of Common Stock, par value \$.01 per share ("Common Stock").

Series A Preferred Stock

The Company has designated 1,000 shares of its Preferred Stock as Series A, having a par value of \$0.0001 per share. Holders of the Series A Preferred Stock have the right to elect a majority of the Board of Directors of the Company. In October 2007, the Company issued 1,000 shares of Series A Preferred Stock to its CEO. At September 30, 2017 and December 31, 2016, there were 1,000 shares and 1,000 shares of Series A Preferred Stock outstanding, respectively.

Series C Senior Convertible Preferred Shares

On June 30, 2015, the Company issued 1,600,000 Series C Senior Convertible Preferred Shares (the "Series C Preferred Shares") at \$2.50 per share for gross proceeds of \$ 4,000,000, as well as issuing 133,221 additional Series C Preferred Shares due to anti-dilution provisions (with no cash remuneration). Legal fees of \$45,000 were deducted from the proceeds of this transaction at closing. These Series C Preferred Shares are convertible to common shares at \$2.50 per share, through February 20, 2020. The Series C Preferred Shares may receive a 4% per annum dividend, payable if available, and in arrears. A description of the transaction which included the issuance of the Series C Preferred Shares is included below. During 2016, the company paid Dividends of \$160,000 to the holder of Series C Convertible Preferred Stock. The Dividend is calculated at 4.0% of \$4,000,000 payable annually on June 30. The accumulated dividends were \$128,211 and \$120,000 for the nine months ended September 30, 2017 and 2016 respectively.

Common Stock

The Company is authorized to issue 25,000,000 common shares at a par value of \$0.01 per share. These shares have full voting rights. At September 30, 2017 and December 31, 2016, there were 17,722,825 and 16,722,825 shares outstanding, respectively. No dividends were paid for the periods ended September 30, 2017.

Preferred Rights

The Company issued "Preferred Rights" for the rights to percentages of revenues generated from the San Jose de Gracia Pilot Production Plant, and received \$158,500 in 2003 and \$626,000 in 2002. This has been reflected as "Preferred Rights" in stockholders' equity. As of December 31, 2004, \$558,312 was repaid and as of December 31, 2005, an additional \$186,188 was repaid, leaving a current balance of \$40,000 and \$40,000 as of September 30, 2017 and December 31, 2016, respectively.

Exercise of 1,000,000 Common Share Options at \$2.50 per Share – Total of \$2,500,000 USD

On August 22, 2017, the Company received proceeds in the amount of \$2.5 M USD following the exercise of one million outstanding options at a price of \$2.50 per share. The option exercise was completed and funded on August

22, 2017.

Stock Issuances

2016 Activity – None.

2017 Activity – On August 22, 2017, 1,000,000 options to purchase common shares were exercised, and 1,000,000 common shares were issued.

Treasury Stock

At September 30, 2017 and 2016, 1,112,313 treasury shares were outstanding.

Note Repayments

In the three months ended September 30, 2017, the Company did not repurchase any Notes.

In the nine months ended September 30, 2017, the Company repaid Notes with a principal balance of \$5,625.

Warrants

Shareholders of the Company exercised 1,000,000 warrants for cash at \$2.50 per share.

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Intrinsic Value
Balance at December 31, 2016	3,593,689	\$ 2.45	2.51	\$ —
Granted	—	—		\$ —
Exercised	(1,000,000)	\$ 2.50		\$ —
Forfeited	—	—		\$ —
Balance at September 30, 2017	2,593,689	\$ 2.42	2.34	\$ —
Exercisable at September, 2017	2,593,689	\$ 2.42	2.34	\$ —

NOTE 9 – RELATED PARTY TRANSACTIONS**Related Party Transactions**

The Company follows FASB ASC subtopic 850-10, Related Party Disclosures, for the identification of related parties and disclosure of related party transactions. Pursuant to ASC 850-10-20, related parties include: a) affiliates of the Company; b) entities for which investments in their equity securities would be required, absent the election of the fair value option under the Fair Value Option Subsection of Section 825-10-15, to be accounted for by the equity method by the investing entity; c) trusts for the benefit of employees, such as pension and profit-sharing trusts that are managed by or under the trusteeship of management; d) principal owners of the Company; e) management of the Company; f) other parties with which the Company may deal if one party controls or can significantly influence the management or operating policies of the other to an extent that one of the transacting parties might be prevented from fully pursuing its own separate interests; and g) other parties that can significantly influence the management or operating policies of the transacting parties or that have an ownership interest in one of the transacting parties and can significantly influence the other to an extent that one or more of the transacting parties might be prevented from fully pursuing its own separate interests.

Material related party transactions are required to be disclosed in the consolidated financial statements, other than compensation arrangements, expense allowances, and other similar items in the ordinary course of business. However, disclosure of transactions that are eliminated in the preparation of consolidated or combined financial statements is not required in those statements. The disclosures shall include: a) the nature of the relationship(s) involved; b) a description of the transactions, including transactions to which no amounts or nominal amounts were ascribed, for each of the periods for which statements of operation are presented, and such other information deemed necessary to an understanding of the effects of the transactions on the financial statements; c) the dollar amounts of transactions for each of the periods for which statements of operations are presented and the effects of any change in the method of establishing the terms from that used in the preceding period; and d) amounts due from or to related parties as of the

date of each balance sheet presented and, if not otherwise apparent, the terms and manner of settlement.

Dynacap Group Ltd.

The Company paid \$124,000 and \$91,000 to Dynacap Group, Ltd. (“Dynacap”, an entity controlled by the CEO of the Company) for consulting and other fees during the nine months ended September 30, 2017 and 2016, respectively. Dynacap retains 2 individuals who are family members of the CEO, as well as 2 consultants, as independent contractors who provide administrative and executive support services to the Company. Dynacap has provided these services to the Company for recent years.

Cash Advances by Management

Company Chairman/CEO loaned \$75,000 and a former Company CFO loaned \$150,000 as advances to the Company in 2015.

In 2015, the Company converted \$175,000 of advances from the CEO for the issuance of 70,000 shares of common (at \$2.50 per share) as well as 70,000 warrants, exercisable at \$2.50 per share, expiring December 31, 2017. These shares were issued in August 2015. The Company repaid the \$150,000 advance to the former CFO in 2016.

NOTE 10 – DERIVATIVE LIABILITIES**Preferred Series C Stock**

As discussed in Note 8, the Company analyzed the embedded conversion features of the Series C Preferred Stock and determined that the stock qualified as a derivative liability and is required to be bifurcated and accounted for as such since the host and the embedded instrument are not clearly and closely related. The Company performed a valuation of the conversion feature. In performing the valuation, the Company applied the guidance in ASC 820, “*Fair Value Measurements*”, to nonfinancial assets and liabilities that are recognized or disclosed at fair value on a nonrecurring basis. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). To measure fair value, the Company incorporates assumptions that market participants would use in pricing the asset or liability, and utilizes market data to the maximum extent possible.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company’s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The Company considered the inputs in this valuation to be level 3 in the fair value hierarchy under ASC 820 and used an equity simulation model to determine the value of conversion feature of the Series C Preferred Stock based on the assumptions below for the nine months ended September 30, 2017 and year ended December 31, 2016:

	09/30/17		12/31/16	
Annual volatility rate	97	%	123	%
Risk free rate	1.50	%	1.93	%
Holding Period	5 years		5 years	
Fair Value of common stock	\$1.50		\$1.75	

The below table represents the change in the fair value of the derivative liability (Preferred Series C Stock) during the nine months ending September 30, 2017 and the year ending December 31, 2016:

Period Ended	09/30/17	12/31/16
Fair value of derivative (Preferred Series C Stock), beginning of year	\$2,592,452	\$2,419,359
Change in fair value of derivative (Preferred Series C Stock)	(1,518,891)	173,093
Fair value of derivative (Preferred Series C Stock), end of period	\$1,073,561	\$2,592,452

Preferred Series C Warrants

As discussed in Note 8, the Company analyzed the embedded conversion features of the Series C Preferred Stock and determined that the Warrants qualified as a derivative liability and is required to be bifurcated and accounted for as such since the host and the embedded instrument are not clearly and closely related. The Company performed a valuation of the conversion feature. In performing the valuation, the Company applied the guidance in ASC 820, “*Fair Value Measurements*”, to nonfinancial assets and liabilities that are recognized or disclosed at fair value on a nonrecurring basis. ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). To measure fair value, the Company incorporates assumptions that market participants would use in pricing the asset or liability, and

utilizes market data to the maximum extent possible.

In instances where the determination of the fair value measurement is based on inputs from different levels of the fair value hierarchy, the level in the fair value hierarchy within which the entire fair value measurement falls is based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability.

The Company considered the inputs in this valuation to be level 3 in the fair value hierarchy under ASC 820 and used an equity simulation model to determine the value of conversion feature of the Warrants based on the assumptions below for the periods ended September 30, 2017 and December 31, 2016:

	09/30/17		12/31/16	
Annual volatility rate	97	%	123	%
Risk free rate	1.50	%	1.93	%
Holding Period	5 years		5 years	
Fair Value of common stock	\$1.50		\$1.75	

The below table represents the change in the fair value of the derivative liability (Preferred Series C Warrants) for the period ended September 30, 2017 and the year ending December 31, 2016.

Period Ended 09/30/17