BION ENVIRONMENTAL TECHNOLOGIES INC
Form 10QSB
November 19, 2003

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

FORM 10-QSB

[x] Quarterly report pursuant to Section 13 or 15 (d) of the Securities Exchange Act of 1934 for the quarterly period ended September 30, 2003

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 No. 001-31437

BION ENVIRONMENTAL TECHNOLOGIES, INC.
(Exact name of small business issuer as specified in its charter)

Colorado	84-1176672
(State of Incorporation)	(I.R.S. Employer Identification Number)

18 E. 50th Street, 10th Floor
New York, New York 10022
(Address of principal executive offices, including zip code)

(212) 758-6622
(Registrant's telephone number, including area code)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 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 [X]

As of October 31, 2003 the issuer had outstanding 5,300,021 shares of common stock. This includes 1,900,000 shares held by a majority-owned subsidiary.

BION ENVIRONMENTAL TECHNOLOGIES, INC.

QUARTERLY REPORT ON FORM 10-QSB

THIS REPORT INCLUDES FINANCIAL STATEMENTS (AND NOTES ATTACHED THERETO) FOR THE QUARTER ENDED SEPTEMBER 30, 2003 WHICH HAVE BEEN INTERNALLY PREPARED AND WHICH HAVE NOT BEEN REVIEWED BY ANY INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS. WHILE WE BELIEVE THAT THE FINANCIAL STATEMENTS ARE ACCURATE AND COMPLETE IN ALL MATERIAL RESPECTS, IT IS POSSIBLE THAT A REVIEW MAY RESULT IN ADJUSTMENTS, SOME OF WHICH MAY BE MATERIAL.

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BION ENVIRONMENTAL TECHNOLOGIES, INC.

QUARTERLY REPORT ON FORM 10-QSB

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PART I

Item 1. Financial Statements

This Form 10-QSB has not been reviewed by BDO Seidman, LLP, our independent certified public accountants, as required by Item 310(b) of Regulation S-B. BDO Seidman, LLP has not performed the review (and prior reviews and audits) because they ceased work prior to review of the impact on the Company's accounts and operations of the various items disclosed in our Report on Form 8-K dated February 7, 2003. We are not aware of any dispute with BDO Seidman, LLP as to any accounting matters. Since we owe approximately $125,000 to BDO Seidman, LLP, which must be paid or otherwise resolved in order to eliminate independence issues prior to any review or audit of our financial statements and we lack the resources to pay such amounts, no review has been performed.

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BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Unaudited Consolidated Balance Sheet
As of September 30, 2003

ASSETS	
Current assets:	
Cash and cash equivalents	$ 162,317
Accounts receivable, net of allowance for doubtful accounts of $5,935	5,785
Prepaid expenses and other current assets	61,102
Total current assets	229,204
Property and equipment, net	214,924
Claims receivable	600,000
Other assets	30,967
Total assets	$ 1,075,095

LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities:	
Accounts payable	$ 975,897
Accrued expenses	244,426
Deferred compensation B due to Trust	504,506
Accrued deferred compensation	247,500
Capital lease obligation	947
Advances from affiliates	48,977
Secured notes payable - affiliates	736,574
Secured notes payable-others	455,971
Total current liabilities	3,214,798
Minority interest	650,228
Commitments and contingencies	
Stockholders' Equity:	
Preferred Stock, $.01 par value, 10,000 shares authorized, -0- shares issued and outstanding	
Common stock, no par value, 100,000,000 shares authorized, 4,204,291 shares issued and outstanding (this does not include 1,095,730 shares held by Centerpoint which will be distributed to Bion and subsequently cancelled)	
Additional paid in capital	58,347,239
Accumulated deficit	(61,137,170)
Total stockholders' equity	(2,789,931)
Total liabilities and stockholders' equity	$ 1,075,095

See notes to consolidated financial statements

BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Unaudited Consolidated Statements of Operations

	Three Months Ended September 30,	
	2003	2002
Revenue:		
Soil sales	$ -	$ 46,638
Cost of soil	(10,370)	195,718
Gross loss	10,370	(149,080)
Expenses:		
General and administrative (excluding $158,447 and $218,231 of non-cash charges for services and compensation, respectively)	664,646	637,192

Research and development	283,374	149,862
Non-cash charges for services and compensation	-	158,447
	948,020	945,501
Operating loss	(937,650)	(1,094,581)
Other income and expense:		
Interest expense including non-cash interest charges	(64,824)	(75)
Interest income	-	5,629
Other expense, net	37,232	(16,699)
	(27,592)	(11,145)
Net loss before minority interest	(965,242)	(1,105,726)
Minority interest	(64,534)	35,052
Net loss and comprehensive loss	$(1,029,776)	$(1,070,674)
Basic and diluted loss per common share:		
Net loss per common share	$ (0.24)	$ (0.20)
Weighted-average number of common shares outstanding, basic and diluted loss per share	4,205,993	5,304,521

See notes to consolidated financial statements

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BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES
Unaudited Consolidated Statements of Operations

	Three Months Ended September 30,	
	2003	2002
Cash flows from operating activities:		
Net loss	$ (1,029,776)	$ (1,070,674)
Adjustments to reconcile net loss to net cash used in operating activities:		
Minority interest in net loss of subsidiary	259,702	(35,052)
Depreciation and amortization	5,808	20,543
Loss on disposal of asset	19,459	7,444
Issuance of note payable for consulting services		150,000
Non-cash charges for equity instruments issued for compensation and services		8,447
Changes in:		
Accounts receivable	2,160	8,349
Note receivable	-	(985)
Inventory	-	(48,646)
Prepaid expenses and other current assets	(18,114)	41,795

Deposits and other	906	(463)
Accounts payable	120,940	87,364
Accrued liabilities	41,250	2,281
Increase in accrued deferred compensation	120,000	
Increase in due to trust	7,456	
Net cash used in operating activities	(470,289)	(829,599)
Cash flows from investing activities:		
Net proceeds from sale of assets	8,313	
Purchases of property and equipment	(32,821)	(116,152)
Net cash used in investing activities	(24,508)	(116,152)
Cash flows from financing activities:		
Proceeds from secured loans from affiliates	736,574	
Proceeds of secured loans payable	455,971	
Conversion of advances from affiliates to secured Loans from affiliates	(574,823)	
Proceeds of advances from affiliates	30,000	
Payments of capital lease obligations	(74)	(445)
Net cash used in financing activities	647,648	(445)
Net decrease in cash and cash equivalents	152,931	(946,196)
Cash and cash equivalents, beginning of period	9,386	1,813,571
Cash and cash equivalents, end of period	$ 162,317	$ 867,375
Supplemental disclosure of cash flow information:		
Cash paid for interest during the period	$ -	$ 75

See notes to consolidated financial statements

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BION ENVIRONMENTAL TECHNOLOGIES, INC. AND SUBSIDIARIES

Notes to unaudited consolidated financial statement

PRELIMINARY NOTE:

THE FINANCIAL STATEMENTS AS OF SEPTEMBER 30, 2003 AND FOR THE THREE MONTHS THEN ENDED HAVE NOT BEEN REVIEWED BY ANY INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS.

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Bion Environmental Technologies, Inc. and its subsidiaries (the "Company", "Bion", "we", "us" or "our") have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") for interim financial information. In the opinion of management, such statements include all adjustments (consisting only of normal recurring adjustments) necessary for the fair presentation of the Company's financial position, results of operations and cash flows at the dates and for the periods indicated, except that no amounts have been recorded as expense for warrants issued/reissued to certain persons. See Note 5 "Related Party Transactions and Subsequent Events" below for details concerning the Black Scholes value of these warrants. Pursuant to the requirements of the Securities and Exchange Commission applicable to Quarterly Reports on Form 10-QSB, the accompanying financial statements do not include all the disclosures required by GAAP for annual financial statements. While the Company believes that the disclosures presented are adequate to make the information not misleading, these interim consolidated financial statements should be read in conjunction with the financial statements and related notes included in the Company's Annual Report on Form 10-KSB for the year ended June 30, 2003. Operating results for the periods indicated are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2004.

Certain fiscal year 2003 items have been reclassified to conform to their fiscal year 2004 presentation.

2. ORGANIZATION AND NATURE OF BUSINESS

Bion Environmental Technologies, Inc. ("Bion" or the "Company", INCLUDING ALL SUBSIDIARIES UNLESS OTHERWISE INDICATED) was incorporated in 1987 in the State of Colorado.

The Company is in the process of developing and testing a second generation of its technology to provide waste management solutions to the agricultural industry, focusing on livestock waste from confined animal feeding operations, such as large dairy and hog farms. In the past the Company has engaged in two main areas of activity by utilizing the first generation of its technology (which the Company discontinued marketing during calendar year 2001) (which areas the Company intends to re-enter during the current fiscal year pending results of field testing its second generation NMS technology during fiscal year 2004):

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1) WASTE STREAM REMEDIATION. The removal of pollutants (primarily nitrogen and phosphorus) which pollute soil and water and reduction of emissions of gases to the atmosphere which result in acid rain, smog, ground-level ozone or produce "greenhouse warming" effects). We intend to pursue this area of activity primarily through licensing our second generation technology: a) to retrofit existing confined animal feeding operations installations (with emphasis on large dairy farms utilizing anaerobic lagoons for the next 12 months) and b) for use in newly constructed dairy farms; and

2) BIONSOIL SALES. The production and sale of organic BionSoil fertilizer products made from the waste solids produced by use of our technology.

In addition, the Company intends to pursue the "Dairy Park Opportunity," which reflects what the Company believes is the potential for the Bion technology to allow very large dairy farms to vertically integrate (with pasteurization, cream separation, milk bottling, and/or cheese plants, etc.) and pursue site integration (with ethanol plants, methane production, organic farming, etc.) on relatively small plots of land. The consolidated financial statements have been prepared assuming the Company will continue as a going concern. The Company incurred losses totaling $1,029,776 during the quarter ended September 30, 2003 (including non-cash interest expense and other non-cash expenses) and has a history of losses which has resulted in an accumulated deficit of

$61,137,170 at September 30, 2003.

Effective July 8, 2002, the Company completed a 1 for 10 reverse stock split (the "stock split"). The stock split has been retroactively reflected in the Company's consolidated balance sheet and consolidated statement of operations, adjusted in the consolidated statements of changes in stockholders equity and notes to consolidated financial statements.

The consolidated financial statements have been prepared assuming the Company will continue as a going concern. The Company incurred losses totaling $1,029,776 during the quarter ended September 30, 2003 and has a history of losses which has resulted in an accumulated deficit of $61,137,170 at September 30, 2003.

The Company has been suffering from severe financial difficulties since approximately January of 2003. These financial difficulties resulted in the resignation of nearly all of the Company's officers and directors during February and March of 2003, and the termination of most of our employees. The Company has retained a core technical staff, but has drastically curtailed its business activities to include only those activities that are directly needed to complete development and testing of the Company's second generation technology.

The Company's financial difficulties resulted primarily from its inability to raise additional funds due to contractual anti-dilution provisions that were contained in the agreements related to the financing transactions that were completed in January of 2002 which provisions prevented any reasonable financing from being completed. When the Company became aware of the negative implications of these anti-dilution provisions while attempting to structure a planned financing (which financing attempts ultimately failed during January 2003), the Company attempted to either find alternative financing methods

which could be reasonably completed and/or negotiate an amendment to such provisions. After many months of negotiations, agreements related to amending such provisions were entered into during the spring of 2003 and the provisions were finally amended effective August 27, 2003.

Although the Company was able to complete a small financing through one of its subsidiaries during August of 2003 (with minor additional funding during early November 2003) which has allowed it to continue limited work on its second generation technology, the Company's operations have been severely damaged during the past year. In order to continue with business activities, the Company has had to structure interim financing on extremely dilutive terms. The Company still faces a severe working capital shortage and since it has no revenues will need to obtain additional capital to satisfy its existing creditors. There is no assurance that the Company will be able to obtain the funds that it needs to stay in business or to successfully develop its business.

The Company's main activity at present consists of work related to its Texas second generation dairy NMS installation which is currently in the testing/demonstration stage. We anticipate preliminary results during the last calendar quarter of 2003 or the first calendar quarter of 2004. See our Annual Report on Form 10-KSB for the year ended June 30, 2003 , Item 1. "Description of Business B Development of Our Business" for details concerning this matter.

There is substantial doubt about the Company's ability to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments relating to the recoverability or classification of asset carrying amounts or the amounts and classification of liabilities that may result should the Company be unable to continue as a going concern.

The Company has a stockholders' deficit of $2,789,931 accumulated deficit of $61,137,170 limited current revenues and substantial current operating losses. Our operations are not currently profitable; therefore, readers are further cautioned that our continued existence is uncertain if we are not successful in obtaining outside funding in an amount sufficient for us to meet our operating expenses at our current level.

3. SIGNIFICANT ACCOUNTING POLICIES

Principles of consolidation:

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

Revenue recognition:

Revenue from the sale of BionSoil products and associated fees are recognized when shipped, as the Company has no continuing obligations.

Revenues from fixed-price system development and construction projects are recognized on the percentage-of-completion method. For contracts accounted for under the percentage-of-completion method, the amount of revenue recognized is the percentage of the total contract price that the cost expended to date bears to the anticipated final total cost based upon current estimates of the cost to complete the contract. Contract cost includes all

labor and benefits, materials unique to or installed in the project, subcontract costs and allocations of indirect costs. General and administrative costs are charged to expense. Provisions for estimated losses on uncompleted contracts are provided when determined, regardless of the completion percentage. As contracts can extend over one or more accounting periods, revisions in costs and earnings estimated during the course of the work are reflected during the accounting period in which the facts that require such revisions become known. Project managers make assumptions concerning cost estimates for labor hours, consultant hours and other project costs. Due to uncertainties inherent in the estimation process and potential changes in customer needs as projects progress, it is at least reasonably possible that completion costs for some uncompleted projects may be further revised in the near term, and that such revisions may be material.

Depreciation and amortization:

Property and equipment are stated at cost and are depreciated using the straight-line method over the estimated useful lives of the related assets, generally three to seven years. Leasehold improvements are amortized using the straight-line method over the shorter of the term of the lease or the estimated useful life of the asset.

Income taxes:

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

Cash and cash equivalents:

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

Impairment of long-lived assets:

Long-lived assets and certain intangibles are evaluated for impairment when events or changes in circumstances indicate that the carrying value of the assets may not be recoverable through the estimated undiscounted future cash flows resulting from the use of these assets. When any such impairment exists, the related assets will be written down to fair value.

Inventory:

Inventories are stated at the lower of cost or market, principally determined by the FIFO method. Inventories include the cost of raw materials, supplies, labor and overhead.

Loss per share of common stock:

Basic earnings per share includes no dilution and is computed by dividing income or loss available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of an entity, similar to fully diluted earnings per share. In loss periods, dilutive common equivalent shares are excluded, as the effect would be anti-dilutive. Therefore, basic and diluted earnings per share are the same for all periods presented.

For the quarters ended September 30, 2003 and 2002, stock options exercisable into 342,336 and 242,232 shares of common stock, respectively, and stock warrants exercisable into 1,543,393 and 1,393,393 shares of common stock, respectively, were not included in the computation of diluted earnings per share because their effect was anti-dilutive.

Use of estimates:

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

Fair value of financial instruments:

The estimated fair value of financial instruments has been determined using available market information or other appropriate valuation methodologies, including the Black Scholes model. However, considerable judgment is required in interpreting market data to develop estimates of fair value. Consequently, the estimates are not necessarily indicative of the amounts that could be realized or would be paid in a current market exchange. The carrying amounts reported on the consolidated balance sheets approximate their respective fair values.

Stock-based compensation:

The Company accounts for its stock-based compensation arrangements with its employees in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and complies with the disclosure provisions of SFAS 123, "Accounting for Stock-Based Compensation." SFAS 123 established a fair-value-based method of accounting for stock-based compensation plans. Stock-based awards to nonemployees are accounted for at fair value in accordance with the provisions of SFAS 123. NO CALCULATIONS OF THESE ITEMS HAVE BEEN PREPARED SINCE 2002 DESPITE THE FACT THAT A SUBSTANTIAL NUMBER OF OPTIONS (290,833), IN AGGREGATE WERE GRANTED EFFECTIVE AUGUST 31,2003. See Note 5 "Related Party Transactions and Subsequent Events" below for information concerning the Black Scholes values of issuances/grants of warrants and options.

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Patents:

Patents are recorded at cost less accumulated amortization, which is calculated on a straight-line basis over a period of the estimated economic life or legal life of 17 years. Amortization expense for the years ended June 30, 2003 and 2002 was $3,232 each year or $808 per quarter.

Reclassifications:

Certain prior-year amounts have been reclassified to conform to their 2002 presentation.

Cumulative effects of accounting changes:

During the year ended June 30, 2001, the Company applied Emerging Issues Task Force Issue No. 00-27 ("EITF 00-27"), "Application of EITF Issue No. 98-5, Accounting for Convertible Securities with Beneficial Conversion Features of Contingently Adjustable Conversion Ratios, to Certain Convertible Instruments", which is effective for all such instruments. This issue clarifies the accounting for instruments with beneficial conversion features or contingently adjustable conversion ratios. The Company modified the previous calculation of the beneficial conversion features associated with previously issued convertible bridge notes. Based on further clarification, the beneficial conversion feature should be calculated by allocating the proceeds received in the financing to the convertible instruments and to any detachable warrants issued in the transactions, and measuring the intrinsic value based on the effective conversion price based on the allocated proceeds. The previous calculation was based on a comparison of the stated conversion price in the terms of the instrument to the fair value of the issuer's stock at the commitment date.

As a result of the issuance of EITF 00-27, effective October 1, 2000, the Company recorded an additional warrant discount on the 2000 convertible bridge notes of $1,050,000 due to the beneficial conversion feature calculated on the intrinsic value of the allocated proceeds received in the financing. Since the notes automatically convert into common stock one year from the date of issuance, the Company has recorded $481,250 as a cumulative effect of change in accounting principle. The remaining discount of $568,750 has been amortized to interest expense over the remaining conversion period.

4. LITIGATION

On September 30, 2003, Morrison Cohen Singer & Weinstein, LLP ("MCSW") filed a complaint in the Supreme Court of the State of New York, County of New York, against us alleging that we owe MCSW approximately $114,000 for legal services provided. We have not yet filed an answer in that proceeding. We have already recorded a liability for these legal services, and therefore we do not believe that this lawsuit will have a material adverse effect on our financial condition. During October 2003, we concluded a settlement of this matter for an aggregate sum of $65,000 (including attorneys' fees) and the litigation has been dismissed with prejudice.

On July 22, 2002, Thomas Keith Barefoot ("Barefoot"), doing business as Quin Deca Farm ("Quin Deca"), an unaffiliated party, filed a complaint against the Company in the Superior Court of the County of Harnett in the State of North Carolina regarding the Company's first generation Bion NMS System on Quin Deca

Farm and the harvesting of BionSoil. The complaint includes breach of contract claims asserting that the Company abandoned the NMS system on Quin Deca Farm and the failure of the Company to harvest BionSoil. The second claim is for fraud regarding misrepresentation of the state of the technology of the first generation NMS. The third claim is for unfair and deceptive trade practices for misrepresentation of the state of the technology of the NMS System. The fourth claim is for negligent misrepresentation made by Bion in connection with the work it performed and its suitability for the intended purpose. The fifth claim is for equity/specific performance in that Bion left Quin Deca with an economically and technically deficient waste management system that cannot continue to be used without adequate and alternative methods of waste removal. Quin Deca is seeking $830,000 in damages plus punitive damages and to have its damages trebled, reasonable attorney fees and principles of equity requiring Bion to install its second generation Bion NMS system. We have filed an answer and counterclaims. The action has been removed to the U.S. District Court for the Eastern District of North Carolina which court recently ruled that most of the substantive claims should be arbitrated between Quin Deca and our Bion Technologies, Inc. subsidiary. The Company does not believe that the claims against it have merit and, assuming that we have the funds to properly defend this action, we that the ultimate resolution of this litigation will not have a material adverse effect on the Company, its operations or its financial condition. On May 6, 2002, Arab Commerce Bank Ltd. ("ACB"), an unaffiliated party, filed a complaint against the Company in the Supreme Court of the State of New York regarding $100,000 of the Company's convertible bridge notes ("Notes") that were issued to ACB in March of 2000. The complaint includes breach of contract claim asserting that the Company owes ACB $265,400 plus interest or $121,028 including interest based on ACB's interpretation of the terms of the Notes and subsequent amendments. Effective June 30, 2001, the Company issued ACB 5,034 shares of common stock on conversion in full payment of the Notes based on the Company's interpretation of the Notes, as amended. The Company has filed an answer to the complaint denying the allegations. Assuming that we have the funds to properly defend this action. The Company does not believe that the ultimate resolution of this litigation will have a material adverse effect on the Company, its operations or its financial condition.

5. RELATED PARTY TRANSACTIONS AND SUBSEQUENT EVENTS

During February 2003 Bion entered into an agreement with Centerpoint (which agreement was amended April 23, 2003) which agreement was ratified by the shareholders of Centerpoint on August 25,2003. This agreement, upon ratification by Centerpoint's shareholders and completion of a related agreement (executed May 29,2003) with OAM, S.p.A., the former parent of Centerpoint, on August 27, 2003, amended certain contractual provisions which had prevented the raising of funds by Bion thereby creating the financial/management crisis which has afflicted Bion over the past year. For details, see Our Annual Report on Form 10-KSB for the year ended June 30, 2003, "Item 1. Description of Business---Acquisition of Centerpoint/Transactions with Centerpoint and Recent Developments - Centerpoint Shareholders' Meeting/Removal of Contractual Problems" and our Current Reports on Form 8-K dated August 25, 2003, June 9, 2003 and April 12, 2003 and the exhibits thereto.

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From January 2003 through August 2003, Dominic Bassani made advances to Bion (primarily through Bright Capital, Ltd. and D2, LLC) which totaled in excess of $600,000. From late March 2003 (when most management personnel resigned and the contract with D2, LLC under which he had been providing consulting services to Bion terminated)) through present, Mr. Bassani has provided ongoing consulting services to Bion. Mr. Bassani will provide services to Bion and Dairy through March 31,2005 for the sum of $300,000 per year in deferred compensation (to be converted into Bion common stock at a price no greater than $3.00 per share and the grant of 200,000 options to purchase Bion common stock at a price of $3.00 per share until August 31,2008. Additionally, pursuant to prior existing arrangements, adjustments were made to Class SV (650,000 increased to 800,000; exercise price reduced to $3.00; term extended to August 31,2008) now owned by family members of Mr. Bassani (and/or trust for such family members). Various agreements related to such advances, services and adjustments have been executed by Bion. See our Current Reports on Form 8-K dated March 25, 2003, April 12, 2003, June 9, 2003 and August 25, 2003 and the exhibits thereto for further details. See also "Bion Dairy Corporation Financing" below.

Mark A. Smith, our President and a director, has agreed to serve in such positions on a consulting basis through March 31,2003 in consideration of $150,000 in deferred compensation (to be converted into Bion common stock at a price no greater than $3.00 per share) and the grant (effective August 31, 2003) of 50,000 options to purchase Bion common stock at $3.00 per share until August 31, 2003. See our Current Report on Form 8-K dated June 9, 2003 and the exhibits thereto for further details. See also "Bion Dairy Corporation Financing" below.

Jon Northrop, a director of Bion, has been granted (effective August 31, 2003) an option to purchase 10,000 shares of Bion's common stock at a price of $3.00 until August 31, 2008.

Jere Northrop, director and Technology Director of Bion, has been granted (effective August 31,2003) an option to purchase 40,000 shares of Bion's common stock at a price of $3.00 per share until August 31, 2008. In addition, Jere Northrop is receiving $2,500 per month of deferred compensation (to be converted into Bion common stock at $3.00 per share) to compensate for additional duties he has taken on due to Bion's reduced technical personnel resulting from our ongoing financial crisis.

On August 31, 2003, we granted James Morris, Bion's Chief Technology Officer, 80,000 options to purchase shares of the Company's common stock at $3.00 per share expiring July 31, 2008.

On August 31, 2003, we granted George Bloom, Bion's Chief Engineer, 80,000 options to purchase shares of the Company's common stock at $3.00 per share expiring July 31, 2008.

On August 31, 2003, 1,187,343 warrants were "issued" (or reissued/amended to extend the term, reduce the exercise prices and increase the number by 150,000, in aggregate) of which 1,037,343 were previously outstanding) to related parties at an average exercise price of $3.65 and an average term of 8.29 years. If these warrants were valued using the Black Sholes method, their value would be estimated at $1,090,992. In addition, a total of 583,833 options were issued with an average exercise price of $3.10 and an average term of 4.92 years. Of these options, 460,000 were granted to related

parties. If these options were valued using the Black Sholes method, their value would be estimated at $493,017. See our Current Report on Form 8-K dated June 9, 2003 and our Annual Report on Form 10-KSB for the year ended June 30, 2003 and the exhibits thereto for additional information concerning these issuances/reissuance of warrants and grants of options. In addition, 10,573 Warrants previously issued to D. Slavney were re-issued at a new exercise price of $6.00. If these warrants were valued using the Black Sholes method, their value would be estimated at $63,478. None of these Black Scholes values have been reflected in the Financial Statements. Had these items been recorded in the Financial Statements, our losses would have been increased by the amounts recorded.

Centerpoint Shareholders Meeting/Removal of Contractual Problems

A meeting of the Centerpoint Corporation ("Centerpoint") stockholders which commenced on July 31,2003 was concluded on August 25, 2003. Centerpoint's stockholders approved the ratification of the Amended Centerpoint Agreement, with 96% of the shares present at the meeting voted in favor, including shares owned by Bion. Of the shares present at the meeting, 85% (1,179,405 shares) other than the shares owned by Bion voted in favor of the ratification and only 1,490 shares voted against the ratification (with the balance of such shares abstaining). See our Current Reports on Form 8-K dated April 12, 2003 and August 25, 2003 and the exhibits thereto for further details regarding the matters being ratified.

On August 27, 2003, Bion paid the sum of $90,000 to OAM, S.p.A. (and its designees) to complete the transaction described in our Current Report on Form 8-K dated April 12, 2003 (set forth in Exhibit 99.2 thereto) as a result of the favorable vote by Centerpoint's stockholders.

As a result, the contractual impediments to future financing described in our Current Report on Form 8-K dated April 12, 2003(see Exhibits 99.2 and 99.3 thereto) have now been remove

On November 3, 2003, Centerpoint received $430,300.74(net of litigation costs) from the settlement of a portion of its arbitration with Aprilia. See Note 5, "Claims Receivable - Aprilia Claim", to the Financial Statements in our Annual Report on Form 10-KSB for the year ended June 30, 2003 for further details. On November 10, 2003 Centerpoint made a $400,000 investment as set forth below at "Bion Dairy Corporation Financing".

On August 25, 2003, Bion Dairy Corporation ("Dairy"), of which we own all 4,000,000 shares of its common stock outstanding, closed an initial stage of financing totaling $1,117,500 (including $600,000 of prior advances from Bright Capital, Ltd. ("Brightcap") and $65,000 of prior advances from affiliates of David Mitchell, our former CEO) of secured convertible debt ("Notes"). Through September 30,2003 an additional $65,000 of the Notes were sold to Mark A. Smith our president, for a total issuance of $1,182,500. On November 10, 2003 Centerpoint purchased $400,000 of the Notes bringing the total sale and issuance to $1,582,500. Dairy has now closed the offering of these Notes. Up to an aggregate total of $4,482,500 of such Notes (or similar Notes) may be issued by Dairy in subsequent tranches. The largest holder of these Notes($600,000 principal) is Chris-Dan, LLC, which is owned by Dominic Bassani, General Manager of Dairy and a consultant to Bion. The Notes are secured by: a) all of the intellectual property of Bion (and its subsidiaries)

(which previously secured outstanding obligations to Bright Capital, Ltd. which is owned by Mr. Bassani), b) all of the outstanding shares of Dairy, and c) all of the shares of Centerpoint owned by Bion. The Notes are convertible into the common stock of Dairy at a price of $1.00 (principal and accrued interest on the Notes) under various conditions specified in the financing documentation, one or more of which conditions precedent to conversion may never be met. Under additional specified conditions (which also have no assurance of being met), the Notes (or Dairy common stock received pursuant to the conversion thereof) may in the future be exchanged for shares of the common stock of Bion. If conversion of the Notes into the common stock of Dairy takes place, all of Bion's business opportunity in the dairy industry world-wide will be conducted through Dairy, and the board of directors of Dairy will consist of three members, two of which will be designated by the majority of the shareholders of Dairy and only one will be designated by Bion. The financing restricts the use of its proceeds and, unless Dairy and/or Bion raise substantial additional funds, there will be no substantial funds available for Bion to pay its creditors and carry out its business. See Exhibit 10.1 to our Current Report on Form 8-K dated August 25,2003 for further details.

Although Dairy, our subsidiary, recently received the financing described above (which financing was not large enough to repay our creditors and is subject to a limiting "Use of Proceeds" which does not permit significant payment to our existing creditors) and we are currently seeking other outside sources of capital, as of this date we have not been able to secure the level of financing that is necessary for our current and future operations and/or to repay our existing indebtedness and there can be no assurance that sufficient funds will be available from external sources. Further, there can be no assurance that any such required funds, if available, will be available on attractive terms or that they will not have a significantly dilutive effect on our existing shareholders. Since we do not yet have the ability to generate cash flow from operations, we have substantially curtailed our current business activities and we may need to cease operations if we are not able to raise capital from outside sources. This would have a material adverse effect on our business and our shareholders.

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

THIS REPORT INCLUDES FINANCIAL STATEMENTS (AND NOTES ATTACHED THERETO) FOR THE QUARTER ENDING SEPTEMBER 30, 2003 WHICH HAVE NOT BEEN REVIEWED OR AUDITED BY INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS AND OTHER ITEMS DERIVED THEREFROM WHICH MAY NOT FULLY CONFORM THE REQUIREMENTS/REGULATIONS GOVERNING THE CONTENT OF FORM 10-QSB. Since we owe approximately $125,000 to BDO Seidman, LLP, which must be paid or otherwise resolved in order to eliminate independence issues prior to any review or audit of our financial statements and we do not presently have the funds to pay such sums and for subsequent work, no review or audit has been performed on our financial statements since December 31, 2002.

Statements made in this Form 10-QSB that are not historical or current facts are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and section 21E of the Securities Exchange Act of 1934, as amended. These statements often can be identified by the use of terms such as "may," "will," "expect," "believe," anticipate," "estimate," or "continue" or the negative thereof. Bion intends that such forward-looking statements be subject to the safe harbors for such statements. We wish to caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date made. Any forward-looking statements represent management's best judgment as to what may occur in the future. However, forward-looking statements are subject to risks, uncertainties and important factors beyond our control that could cause actual results and events to differ materially from historical results of operations and events and those presently anticipated or projected.

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

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

Overview

BION ENVIRONMENTAL TECHNOLOGIES, INC. ("BION," "WE," "US," OR "OUR") HAS BEEN SUFFERING FROM SEVERE FINANCIAL DIFFICULTIES SINCE APPROXIMATELY LATE JANUARY OF 2003, AS DISCLOSED IN OUR PERIODIC AND OTHER REPORTS FILED WITH THE SECURITIES AND EXCHANGE COMMISSION COMMENCING WITH OUR CURRENT REPORT ON FORM 8-K DATED FEBRUARY 7, 2003. THESE FINANCIAL DIFFICULTIES RESULTED IN THE RESIGNATION OF NEARLY ALL OF OUR OFFICERS AND DIRECTORS DURING FEBRUARY AND MARCH OF 2003, AND THE TERMINATION OF MOST OF OUR EMPLOYEES. WE HAVE RETAINED A CORE TECHNICAL STAFF, BUT WE HAVE DRASTICALLY CURTAILED OUR BUSINESS

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ACTIVITIES TO INCLUDE ONLY THOSE ACTIVITIES THAT ARE DIRECTLY NEEDED TO COMPLETE DEVELOPMENT AND TESTING OF OUR SECOND GENERATION TECHNOLOGY.

OUR FINANCIAL DIFFICULTIES RESULTED PRIMARILY FROM OUR INABILITY TO RAISE ADDITIONAL FUNDS DUE TO CONTRACTUAL ANTI-DILUTION PROVISIONS THAT WERE CONTAINED IN THE AGREEMENTS RELATED TO THE FINANCING TRANSACTIONS THAT WERE COMPLETED IN JANUARY OF 2002 (SEE OUR FORM 10-KSB FOR THE YEAR ENDED JUNE 30, 2002 AND OUR CURRENT REPORT ON FORM 8-K DATED DECEMBER 12, 2001 AND THE EXHIBITS AND AMENDMENT THERETO) WHICH PREVENTED ANY REASONABLE FINANCING FROM BEING COMPLETED. WHEN WE BECAME AWARE OF THE NEGATIVE IMPLICATIONS OF THESE ANTI-DILUTION PROVISIONS WHILE ATTEMPTING TO STRUCTURE A PLANNED FINANCING (WHICH FINANCING ATTEMPTS ULTIMATELY FAILED IN JANUARY OF 2003), WE ATTEMPTED TO EITHER FIND ALTERNATIVE FINANCING METHODS WHICH COULD BE REASONABLY COMPLETED AND/OR NEGOTIATE AN AMENDMENT TO SUCH PROVISIONS. AFTER MONTHS OF NEGOTIATIONS, AGREEMENTS RELATED TO AMENDING SUCH PROVISIONS WERE ENTERED INTO DURING THE SPRING OF 2003(SEE OUR CURRENT REPORT ON FORM 8-K DATED April 12, 2003) AND THE PROVISIONS WERE FINALLY AMENDED EFFECTIVE AUGUST 27, 2003 (SEE OUR CURRENT REPORT ON FORM 8-K DATED AUGUST 25, 2003 AND EXHIBITS THERETO).

ALTHOUGH WE WERE ABLE TO COMPLETE A SMALL FINANCING THROUGH ONE OF OUR SUBSIDIARIES DURING AUGUST OF 2003 WHICH HAS ALLOWED US TO CONTINUE LIMITED WORK ON OUR SECOND GENERATION TECHNOLOGY (SEE OUR CURRENT REPORT ON FORM 8-K DATED AUGUST 25, 2003), OUR OPERATIONS HAVE BEEN SEVERELY DAMAGED DURING THE PAST YEAR. NOT ONLY DID WE HAVE TO TERMINATE MOST OF OUR ACTIVITIES AND EMPLOYEES, BUT WE HAVE SUFFERED SUCH DIRE FINANCIAL CONSTRAINTS (AS WE WERE FACED WITH THE LIKELY POSSIBILITY OF A BANKRUPTCY FILING) THAT WE HAVE LOST CREDIBILITY WITH OUR VENDORS, CREDITORS, THE FINANCIAL COMMUNITY AND OUR EXISTING SHAREHOLDERS AND INVESTORS. AS A RESULT, THE MARKET PRICE FOR OUR STOCK FELL IN ORDER TO CONTINUE WITH OUR BUSINESS ACTIVITIES AND SAVE THE COMPANY WE HAVE HAD TO STRUCTURE INTERIM FINANCING ON EXTREMELY DILUTIVE TERMS WHICH HAS NEGATIVELY AFFECTED OUR SHAREHOLDERS AND WILL PROBABLY CONTINUE TO NEGATIVELY IMPACT OUR ABILITY TO OBTAIN FUTURE FINANCING ON REASONABLE TERMS. WE STILL FACE A SEVERE WORKING CAPITAL SHORTAGE AND SINCE WE HAVE NO REVENUES WE WILL NEED TO OBTAIN ADDITIONAL CAPITAL TO SATISFY OUR EXISTING CREDITORS (SEE "MANAGEMENT'S DISCUSSION AND ANALYSIS" AND "FINANCIAL STATEMENTS"). THERE IS NO ASSURANCE WE WILL BE ABLE TO OBTAIN THE FUNDS THAT WE NEED TO STAY IN BUSINESS OR TO SUCCESSFULLY DEVELOP OUR BUSINESS.

We are in the process of developing and testing a second generation of our technology ("Bion NMS" or "NMS" or "System" or "Technology") to provide waste management solutions to the agricultural industry, focusing on livestock waste from confined animal feeding operations, such as large dairy and hog farms. In the past we have engaged in two main areas of activity by utilizing the first generation of our technology (which we discontinued marketing during calendar year 2001) (which areas we intend to re-enter during the current fiscal year pending results of field testing our second generation NMS technology during fiscal year 2004):

1) WASTE STREAM REMEDIATION. The removal of pollutants (primarily nitrogen and phosphorus) which pollute soil and water and reduction of

emissions of gases to the atmosphere which result in acid rain, smog, ground-level ozone or produce "greenhouse warming" effects). We intend to pursue this area of activity primarily through licensing our second generation technology: a) to retrofit existing confined animal feeding operations installations (with emphasis on large dairy farms utilizing anaerobic lagoons for the next 12 months) and b) for use in newly constructed dairy farms; and

2) BIONSOIL SALES. The production and sale of organic BionSoil fertilizer products made from the waste solids produced by use of our technology.

In addition, we intend to pursue what we call the "Dairy Park Opportunity," which reflects what we believe is the potential for the Bion technology to allow very large dairy farms to vertically integrate (with pasteurization, cream separation, milk bottling, and/or cheese plants, etc.) and pursue site integration (with ethanol plants, methane production, organic farming, etc.) on relatively small plots of land.

Note that all of these activities completely are dependent upon two things, neither of which can be assured at this date:

1) successful completion of the field testing of our second generation technology which is presently taking place in Texas for the purpose of demonstrating its capacity for nutrient (primarily nitrogen and phosphorus)removal from the dairy confined animal feeding operations waste stream)(which will be followed, if successful, by a demonstration/test(either at the Texas site or in California pursuant to existing agreements) of our technology's capacity to reduce polluting gaseous emissions from confined animal feeding operations operation); and

2) our ability to raise sufficient funds to allow us to finance our activities and pay our existing creditors.

We believe that our waste remediation technology will provide confined animal feeding operations (primarily in the dairy and swine industries) with treatment for their animal waste outputs. In this regard, our systems are designed to microbiologically treat their entire waste stream while reducing air emissions and nutrient discharges and creating solids which are in turn the basis for the creation of organic soil and fertilizer products. We are attempting to develop our soil and fertilizer products for use in a variety of applications.

Currently, the majority of confined animal feeding operations dispose of their animal waste by spreading it on cropland (before or after placement in anaerobic lagoons). In many parts of the United States, the operation and/or expansion of confined animal feeding operations are severely restricted due to a combination of the amount of land that is necessary to dispose of the animal waste at an environmentally sustainable rate, and the pollution of existing land and water due to prior disposal of excess nutrients and/or air pollution emissions. Confined animal feeding operations are enormous polluters of our air, water and land and are under significant pressure from state and federal regulatory agencies, the media, environmental groups and the public to reduce their role as a major source of excess nutrient pollution and harmful air emissions. Although nutrient pollution from these feeding operations has gone largely unregulated in the past, they are now subject to stringent regulation under the Federal Clean Water Act and are required to become zero-discharge facilities. Air emissions from these operations are increasingly being evaluated for potential regulation under the Federal Clean Air Act and/or similar state statutes (including without limitation a law recently passed in California which explicitly makes large dairies subject to such regulation). The livestock industry and regulatory agencies are searching for affordable waste treatment solutions to this widespread and immediate problem.

Although we have been conducting business since 1989, we recently have, effectively, re-entered the "development stage" pending completion of testing/demonstration of our second generation technology during the current fiscal year. Our original systems were wastewater treatment systems for dairy farms and food processing plants. The basic design was modified in late 1994 to create Nutrient Management Systems (NMS) that produced organic soil products as a by-product of remediation of the waste stream when installed on large dairy or swine farms. Through June 30, 2001, we sold and subsequently installed, in the aggregate, 32 of these first generation systems in 7 states., of which 19 were still in operation through June 30, 2002. There are presently approximately 12 first generation Bion NMS soil production system installations operating in 3 states.

We discontinued marketing of our first generation NMS systems during calendar 2001. We were unable to produce a business model based on the first generation technology which would generate sufficient revenues to create a profitable business. While continuing to market and operate the first generation systems, during the second half of calendar year 2000 we began to focus our activities on developing the next generation of the Bion NMS technology. We no longer operate any of the first generation NMS systems.

As a result of our research and development efforts during the last three years, the second generation of our technology has been developed. We have designed and tested NMS systems that use state-of-the-art, computerized, real-time monitoring and system control that have the potential to be remotely accessed for both reporting requirements and control functions. These systems are smaller, faster and require less capital per animal than our first generation NMS systems. The new generation of NMS system is designed to harvest solids used to produce our BionSoil(R) products in a few weeks as compared to six to twelve months with our first generation systems.

The Company's main activity at present consists of work related to its Texas second generation dairy NMS installation which is currently in the testing/demonstration stage. We anticipate preliminary results during the last calendar quarter of 2003 or the first calendar quarter of 2004. See our Annual Report on Form 10-KSB for the year ended June 30, 2003 , Item 1. "Description of Business B Development of Our Business" for details concerning this matter.

Critical Accounting Policies and Significant Use of Estimates in Financial Statements

The Securities and Exchange Commission ("SEC") recently issued disclosure guidance for "critical accounting policies." The SEC defines "critical accounting policies" as those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in subsequent periods.

The following list of critical accounting policies (WHICH HAS NOT BEEN UPDATED SINCE 2002) is not intended to be a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by generally accepted accounting principles with no need for management's judgment in their application. There are also areas in which management's judgment in selecting any available

alternative would not produce a materially different result. We have identified the following to be critical accounting policies of the Company:

Revenue recognition: Revenues from fixed-price system development and construction projects are recognized on the percentage-of-completion method. For contracts accounted for under the percentage-of-completion method, the amount of revenue recognized is the percentage of the total contract price that the costs expended to date bear to the anticipated final total cost based upon current estimates of the cost to complete the contract. Contract costs includes all labor and benefits, materials unique to or installed in the project, subcontract costs and allocations of indirect costs. General and administrative costs are charged to expense. Provisions for estimated losses on uncompleted contracts are provided when determined, regardless of the completion percentage. As contracts can extend over one or more accounting periods, revisions in costs and earnings estimated during the course of the work are reflected during the accounting period in which the facts that require such revisions become known. Project managers make assumptions concerning cost estimates for labor hours, consultant hours and other project costs. Due to uncertainties inherent in the estimation process and potential changes in customer needs as projects progress, it is at least reasonably possible that completion costs for some uncompleted projects may be further revised in the near term, and that such revisions may be material.

Revenue from the sale of BionSoil(R) products and associated fees are recognized when shipped, as the Company has no continuing obligations.

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

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

Use of estimates: The preparation of financial statements in conformity with generally accepted accounting principles in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosures of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates and assumptions.

Results of Operations - Comparison of Quarter Ended September 30, 2003 with Quarter Ended September 30, 2002

We recorded no sales of of BionSoil(R) during the quarter ended September 30, 2003 ("2003@). This compares to total sales of $47,000 for the quarter ended September 30, 2002 ("2002"). The amount decreased due to our financial/management crisis and our focus on research and development in 2003. Cost of soil was $(10,370) for 2003 and $196,000 for 2002. The decrease in cost was due to the fact that no new soil was produced for sale and settlements with vendors resulted in a credit for the 2003 quarter.

General and administrative expenses increased to $664,646 for 2003 from $637,000 for 2002. The increase is primarily attributable to an increase in accrued deferred compensation even with a reduction in salaries and expenses due to a general reduction in overall staff size.

Research and development costs increased by $133,000 during the 2003 quarter. This increase is primarily the result of the construction/testing during 2003 of the second generation NMS system built in Texas. No such prototype was in construction/testing in the 2002 quarter.

Non-cash expenses for services and compensation decreased to $0 for 2003 from $158,000 for 2002. The decrease is due to a reduction in amortization expense for the value of options previously issued to various individuals.

Interest expense increased to $64,824 for 2003 from $75 for 2002. The increase was due to new loans in 2003.

We did not record income tax expense during the quarters ended September 30, 2003 and 2002, as a result of our net losses. A valuation allowance of $15,394,000 at June 30, 2002, was established because we have not been able to determine that it is more likely than not that the deferred tax asset will be realized.

WE HAVE NOT YET HAD THE RESOURCES (FINANCIAL AND PERSONNEL) TO ADDRESS OUR TAX ITEMS FOR THE YEAR ENDED JUNE 30, 2003 AND PERIODS SUBSEQUENT THERETO. HOWEVER, AS SET FORTH IN THE FINANCIAL STATEMENTS, IT IS CLEAR THAT WE HAD ADDITIONAL LOSSES DURING THE QUARTER.

DUE TO OUR INABILITY TO OBTAIN ACCOUNTING SERVICES, WE ARE UNABLE TO DETERMINE THE AMOUNTS OF THE VALUATION ALLOWANCES OR CARRY-FORWARDS AT SEPTEMBER 30, 2003.

The net loss and comprehensive loss decreased $41,000 (4%) during the quarter ended September 30, 2003. The decrease primarily related to any decrease in overall operations.

Basic and diluted loss per common share increased by $0.04 from $0.20 to $0.21. The decrease in the loss per share is primarily attributable to the use of a calculation which "netted out" our 57.7% portion of the 1.900,000 shares of our common stock owned by Centerpoint in the 2003 calculation, which was offset by our lower level of activity and the decrease in non-cash charges.

We have not recorded any expense for options/warrants granted/issued during the period. See Note 5 "Related Party Transactions and Subsequent Events" for details related to these items including without limitation the Black Scholes vales of such options/warrants.

Seasonality

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

Liquidity and Capital Resources

Our principal sources of liquidity, which consist of cash and cash equivalents, are $162,000 as of September 30, 2003. We believe we will not generate sufficient operating cash flow to meet our needs without additional external financing. THE LACK OF ADDITIONAL CAPITAL RESULTING FROM THE INABILITY TO GENERATE CASH FLOW FROM OPERATIONS OR TO RAISE CAPITAL FROM EXTERNAL SOURCES HAVE ALREADY FORCED THE COMPANY TO SUBSTANTIALLY CURTAIL OPERATIONS, CAUSED US TO REDUCE STAFF, AND MAY CAUSE THE COMPANY TO CEASE OPERATIONS AND WOULD, THEREFORE, HAVE A MATERIAL ADVERSE EFFECT ON ITS BUSINESS. There can be no assurances that any financing will be available or that the terms will be acceptable to us, or that any financing will be consummated. Any failure on our part to do so will have a material adverse impact on us and may cause us to cease operations.

The level of funding required to accomplish our objectives is ultimately dependent on the success of our research and development efforts, which at this time is unknown.

Effective February 12, 2003, in order to eliminate an impediment to a possible future financing, we entered into an agreement with Centerpoint Corporation, our majority-owned subsidiary, to immediately cancel Section 2.4 "Post-Closing Adjustment" and Section 1.2(b) "Failure to Register or Lapse of Effectiveness" from the January 2002 Subscription Agreement between us and Centerpoint. Our management believes that it is in the best interest of all of the shareholders of both companies that these obstacles to a possible future financing be removed. As majority stockholder, we have fiduciary obligation to act in the best interests of the Centerpoint minority stockholders.As consideration to Centerpoint for canceling the sections noted above we will forgive all amounts due from Centerpoint, totaling approximately $450,000 (this amount has been eliminated in consolidation). In addition, we will return to Centerpoint, for cancellation, warrants to purchase one million shares of Centerpoint's common stock. On August 25, 2003 Centerpoint's shareholders ratified these agreements. On August 27, 2003 a payment of $90,000 was made to the former controlling shareholder of Centerpoint (and its attorneys) to remove our remaining contractual impediments. See our Current Report on Form 8-K dated August 25,2003 and the exhibits thereto.

During the period from January 2003 to September 30, 2003, Bright Capital LLC ("Brightcap"), an entity owned and controlled by Dominic Bassani, a consultant whose services were provided to us as a part of our management agreement with D2CO, LLC ("D2"), advanced us in excess of $600,000 pursuant to various agreements. These advances were made for the purpose of providing funds to allow us to be able to pay operating expenses that are critical to our operations primarily consisting of salaries paid to retain critical personnel (which now consists of six employees), to take actions to protect and expand our intellectual property and to commence work on the system installation in Texas. On August 25, 2003, in connection with the financing of Bion Dairy Corporation ("Dairy"), $600,000 of advances from Brightcap were converted into secured convertible debt of Dairy. See our Current Report on Form 8-K dated August 25, 2003 and the exhibits thereto.

Going Concern

IN CONNECTION WITH THEIR REPORT ON OUR CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED JUNE 30, 2002, BDO SEIDMAN, LLP, OUR INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS, EXPRESSED SUBSTANTIAL DOUBT ABOUT OUR ABILITY TO CONTINUE AS A GOING CONCERN BECAUSE OF RECURRING NET LOSSES AND NEGATIVE CASH FLOW FROM OPERATIONS. SINCE THAT DATE, BION'S FINANCIAL SITUATION HAS GREATLY WORSENED AND HAS EXPERIENCED SUBSTANTIAL FINANCIAL AND MANAGEMENT DISTRESS.

At September 30, 2003, we had stockholders' deficit of $2,789,931 and, an accumulated deficit of $61,137,170. We have no significant current revenues and substantial current operating losses. Our operations are not currently profitable; therefore, readers are further cautioned that our continued existence is uncertain if we are not successful in obtaining outside funding in an amount sufficient for us to meet our operating expenses at our current level. Management is currently engaged in seeking additional capital or other financing arrangements to fund operations until Bion system and BionSoil(R) are sufficient to fund operations.

Consolidated Working Capital

Consolidated working capital decreased to a deficit of $2,217,185 at September 30, 2003 from $1,814,000 at September 30, 2002. This decrease is primarily due to the loss incurred during the year and our inability to raise funds to replace the funds expended. As of September 30, 2003 we have only secured limited funding to carry forwards limited operations.

Analysis of Cash Flows

Cash used in operating activities decreased to $470,209 in 2003 from $830,000 in 2002. The decrease is primarily the result of a decrease in overall operations due to a lack of available funds.

Cash used in investing activities decreased to $25,000 in 2003 compared to $116,000 cash used in investing activities in 2002. The decrease is primarily the result of minimal investing activities in 2003 due to a lack of available funds.

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Cash provided by financing activities increased to $648,000 in 2003 compared to $0 cash used for financing activities in 2002. The increase is primarily the result of new advances from affiliates, new secured loans and conversion of advances from affiliates into secured loans in 2003 versus payment of loans in 2002.

We currently have no commitments for material capital expenditures except as to ongoing work related to our Texas installation/demonstration which is being funded through Dairy, our subsidiary. See "Item 1. Description of Business" in our Annual Report on Form 10-KSB for the year ended June 30, 2003.

Bion Dairy Corporation Financing

On August 25, 2003, Bion Dairy Corporation (" Dairy"), of which we own all 4,000,000 shares of its common stock outstanding, closed an initial stage of financing totaling $1,117,500 (including $600,000 of prior advances from Bright Capital, Ltd. ("Brightcap") and $65,000 of prior advances from affiliates of David Mitchell, our former CEO) of secured convertible debt ("Notes"). Through September 30,2003 an additional $65,000 of the Notes were sold to Mark A. Smith our president, for a total issuance of $1,182,500. On November 10, 2003 Centerpoint purchased $400,000 of the Notes bringing the total sale and issuance to $1,582,500. Dairy has now closed these offering of these Notes. Up to an aggregate total of $4,482,500 of such Notes (or similar Notes) may be issued by Dairy in subsequent tranches. The largest holder of these Notes($600,000 principal) is Chris-Dan, LLC, which is owned by Dominic Bassani, General Manager of Dairy and a consultant to Bion. The Notes are secured by: a) all of the intellectual property of Bion (and its subsidiaries) (which previously secured outstanding obligations to Bright Capital, Ltd. which is owned by Mr. Bassani), b) all of the outstanding shares of Dairy, and c) all of the shares of Centerpoint owned by Bion. The Notes are convertible into the common stock of Dairy at a price of $1.00 (principal and accrued interest on the Notes) under various conditions specified in the financing documentation, one or more of which conditions precedent to conversion may never be met. Under additional specified conditions (which also have no assurance of being met), the Notes (or Dairy common stock received pursuant to the conversion thereof) may in the future be exchanged for shares of the common stock of Bion. If conversion of the Notes into the common stock of Dairy takes place, all of Bion's business opportunity in the dairy industry world-wide will be conducted through Dairy, and the board of directors of Dairy will consist of three members, two of which will be designated by the majority of the shareholders of Dairy and only one will be designated by Bion. The financing restricts the use of its proceeds and, unless Dairy and/or Bion raise substantial additional funds, there will be no substantial funds available for Bion to pay its creditors and carry out its business. See Exhibit 10.1 to our Current Report on Form 8-K dated August 25,2003 for further details.

This Form 10-QSB (and our prior filing on Form 10-KSB for the year ended June 30, 2003 and Forms 10-QSB for the quarters ended December 21, 2002 and March 31, 2003) have not been reviewed by BDO Seidman, LLP, our independent certified public accountants, as required by Item 310(a)) of Regulation S-B. BDO Seidman, LLP has not performed the review (or prior reviews) initially because they had not reviewed the impact on the Company's accounts and operations of the various items disclosed in our Form 8-K dated February 7,2003. No review or audit has been performed since that date. We are not

aware of any dispute with BDO Seidman, LLP as to any accounting matters. We owe approximately $125,000 to BDO Seidman, LLP which must be paid or otherwise resolved in order to eliminated independence issues prior to any review or audit of our financial statements.

Item 3. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including the chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosure. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures, which, by their nature, can provide only reasonable assurance regarding management's control objectives.

With the participation of management, our chief executive officer and interim chief financial officer evaluated the effectiveness of the design and operation of our disclosure controls and procedures at the conclusion of the period ended September 30, 2003. Based upon this evaluation, the chief executive officer and chief financial officer concluded that our disclosure controls and procedures were effective in ensuring that material information required to be disclosed is included in the reports that it files with the Securities and Exchange Commission.

Changes in Internal Controls

There were no significant changes in our internal controls or, to the knowledge of our management, in other factors that could significantly affect internal controls subsequent to the date of most recent evaluation of our disclosure controls and procedures utilized to compile information included in this filing.

Within the twenty-four (24) months prior to the date of our most recent Financial Statements and through the date of this report, we have had no disagreements with our accountants on accounting or financial disclosure.

PART II

Item 1. Legal Proceedings

On September 30, 2003, Morrison Cohen Singer & Weinstein, LLP ("MCSW") filed a complaint in the Supreme Court of the State of New York, County of New York, against us alleging that we owe MCSW approximately $114,000 for legal services provided. We have not yet filed an answer in that proceeding. We have already recorded a liability for these legal services, and therefore we do not believe that this lawsuit will have a material adverse effect on our financial condition. During October 2003, we concluded a settlement of this matter for an aggregate sum of $65,000 (including attorneys' fees) and the litigation has been dismissed with prejudice.

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On July 22, 2002, Thomas Keith Barefoot ("Barefoot"), doing business as Quin Deca Farm ("Quin Deca"), an unaffiliated party, filed a complaint against the Company in the Superior Court of the County of Harnett in the State of North Carolina regarding the Company's first generation Bion NMS System on Quin Deca Farm and the harvesting of BionSoil. The complaint includes breach of contract claims asserting that the Company abandoned the NMS system on Quin Deca Farm and the failure of the Company to harvest BionSoil. The second claim is for fraud regarding misrepresentation of the state of the technology of the first generation NMS. The third claim is for unfair and deceptive trade practices for misrepresentation of the state of the technology of the NMS

System. The fourth claim is for negligent misrepresentation made by Bion in connection with the work it performed and its suitability for the intended purpose. The fifth claim is for equity/specific performance in that Bion left Quin Deca with an economically and technically deficient waste management system that cannot continue to be used without adequate and alternative methods of waste removal. Quin Deca is seeking $830,000 in damages plus punitive damages and to have its damages trebled, reasonable attorney fees and principles of equity requiring Bion to install its second generation Bion NMS system. We have filed an answer and counterclaims. The action has been removed to the U.S. District Court for the Eastern District of North Carolina which court recently ruled that most of the substantive claims should be arbitrated between Quin Deca and our Bion Technologies, Inc. subsidiary. The Company does not believe that the claims against it have merit and, assuming that we have the funds to properly defend this action, we that the ultimate resolution of this litigation will not have a material adverse effect on the Company, its operations or its financial condition.

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

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

Item 5. Other Information

We have been informed that effective approximately November 17, 2003 our stock will no longer be listed on the OTC Electronic Bulletin Board because we filed our Annual Report on Form 10-KSB without audited financial statements. We anticipate that a limited "over-the-counter" "pink sheets" trading market may develop in our common stock.

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Item 6. Exhibits and Reports on Form 8-K

Exhibits.

31.1 Certification of Chief Executive Officer and Interim Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. Filed herewith electronically.

32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350. Filed herewith electronically.

Reports on Form 8-K.

We filed a Report on Form 8-K dated August 25, 2003 reporting information under Items 5 and 7 of that form concerning the initial stage of Bion Dairy Corporation Financing.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: November 18, 2003 BION ENVIRONMENTAL TECHNOLOGIES, INC.

By: /s/ Mark A. Smith

Mark A. Smith
President and Interim Chief
Financial Officer

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