Cyanotech

2017 ANNUAL REPORT

A LETTER FROM OUR CEO

To Our Shareholders:

We saw modest growth in fiscal 2017 even though we continued to face challenges that arose in fiscal 2016. Compared to fiscal 2016, our total sales increased by 0.6% to $32.0 million and gross profit increased by 3% to $12.2 million. Net loss for the year was $1.2 million compared to a loss of $4.4 million in fiscal 2016.

Growth of total sales was limited by the loss of a European bulk astaxanthin customer and a shift in retail marketing strategy to a more profitable channel which initially suppressed sales. Our bottom line performance for the year was impacted by legal fees of $1.2 million related to a shareholder lawsuit.

With the challenges have come progress on many fronts.

- Astaxanthin production has stabilized with a record winter production level for the fourth quarter of FY17 with a concomitant lower production cost.
- We are beginning to see the full cost savings of the personnel restructuring that occurred in FY17.
- Our supercritical carbon dioxide extraction plant is at full, stable, commercial operation and continues to provide significant savings over 3rd party extractors.
- Costco sales increased by 25% compared to FY16 and we are now in 251 or 64% of warehouses nationwide.
- Our shift to a higher-margin retail marketing strategy within Amazon yielded a 4-fold increase in sales to Amazon in the last quarter of the year, compared to the previous quarter, and Amazon sales continue to grow.
- BioAstin® Hawaiian Astaxanthin® and Hawaiian Spirulina® Pacifica® remain the #1 selling brand in their categories commanding a 59% and 54% market share, respectfully, in the Natural Products Channel.
- The Company is no longer a party to the shareholder lawsuit, which should reduce our legal costs.

Our foundation is strong, and the strategies we developed and progress we made in FY17 position us well for the coming year as we focus on controlling costs and growing higher-margin markets for our superior branded consumer products.

Our 126 employees are dedicated to making Cyanotech a success and realizing the full potential of our Company for shareholders. I thank you for your continued support.

Gerald R. Cysewski, Ph.D.

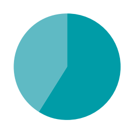
Gerald R. Cysewski

CEO, Chief Scientific Officer

RECORD Q4 PRODUCTION LEVELS (AX)

251
COSTCO WAREHOUSES

4X
SALES TO AMAZON (Q4 VS. Q3)

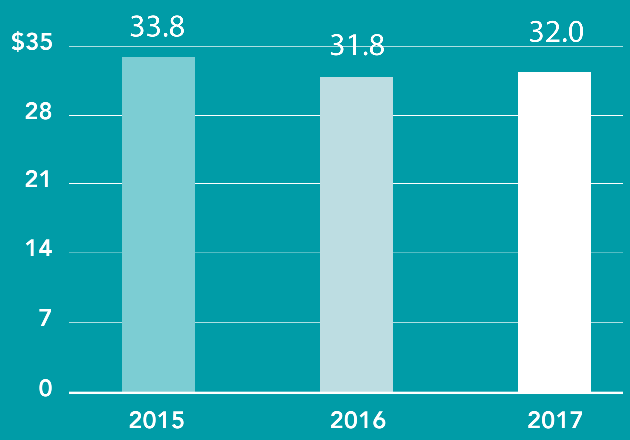


59%
MARKET SHARE IN NATURAL PRODUCTS

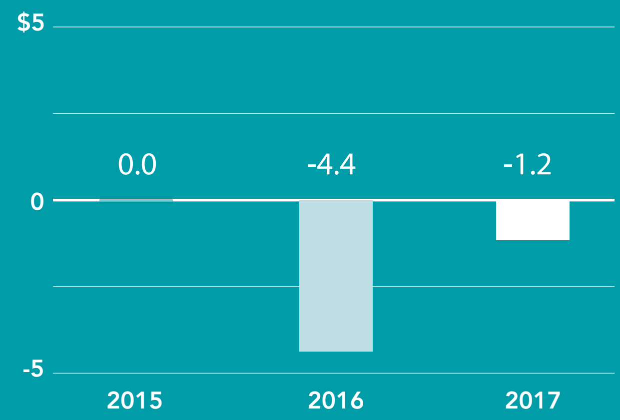
#1
SELLING BRANDS IN CATEGORY

FINANCIAL HIGHLIGHTS

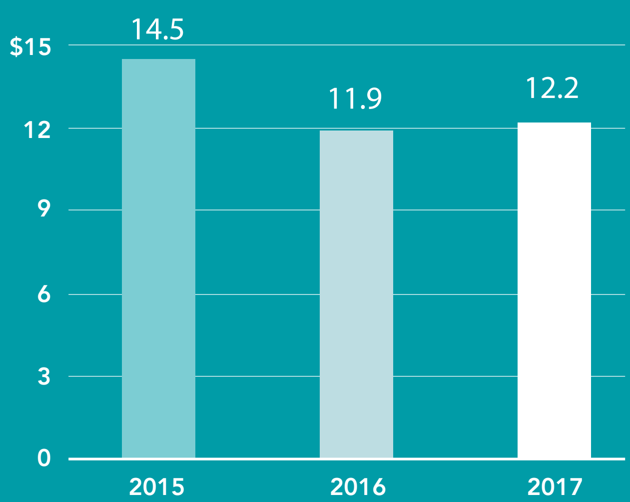
SALES $M



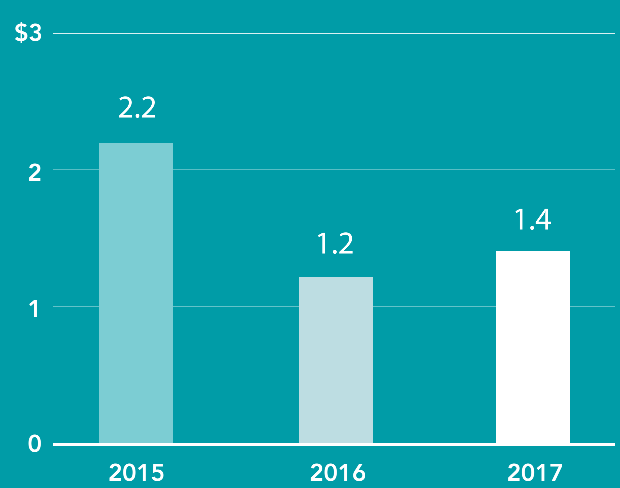
NET INCOME $M



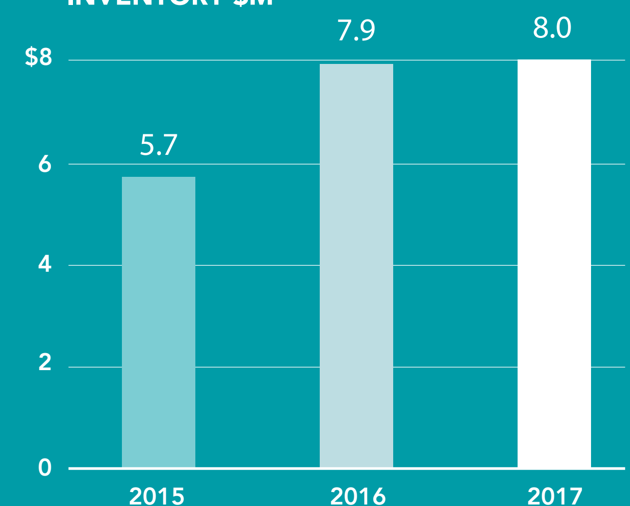
GROSS PROFIT $M



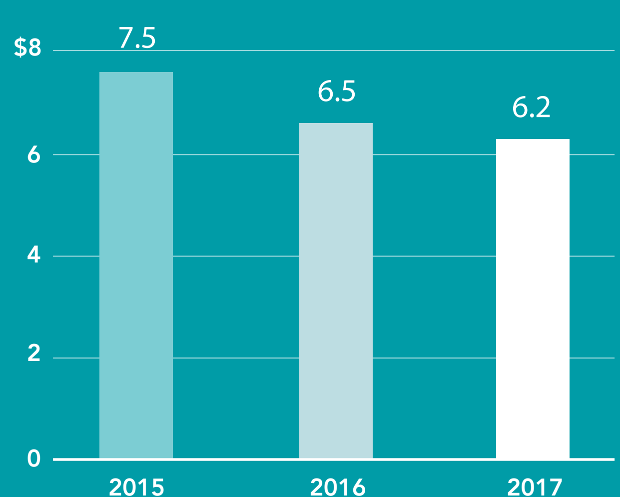
CASH $M



INVENTORY $M



WORKING CAPITAL $M

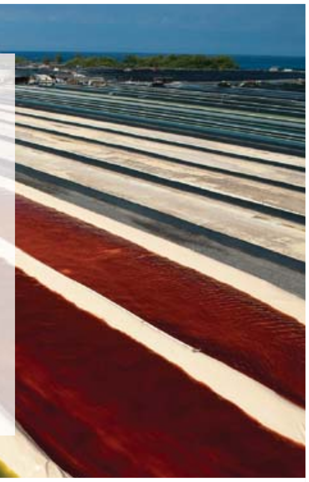


BioAstin®
Hawaiian Astaxanthin®

JOURNEY FROM POND TO BOTTLE

1 Ideal Growing Conditions

BioAstin Hawaiian Astaxanthin comes from a microalgae grown in one of the most pristine locations on earth... Kona, Hawaii! Year-round sunshine, warm temps and fresh water from Hawaiian aquifers create an ideal growing environment for *Haematococcus pluvialis* microalgae.

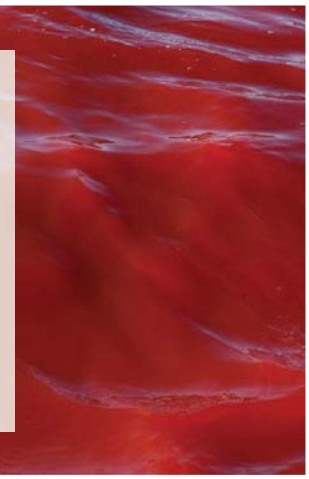


2 Superior Science

Growing the microalgae that astaxanthin comes from is a delicate and complicated process that is ever-evolving. Our scientific team of researchers work around the clock to ensure that the algae produces significant amounts of the antioxidant astaxanthin for harvest.

3 State of the Art Processing

When the algae pond is bright red and full of astaxanthin, it is ready to be harvested. The algae cell is then cracked, dried, and sent to our on-site, state of the art extraction facility. The astaxanthin is extracted from the algae using high-pressure, solvent-free supercritical CO_2 to reveal a pure, deep red oil, full of astaxanthin.



4 Laboratory Testing

BioAstin Hawaiian Astaxanthin goes through numerous quality tests to ensure potency, purity, strength, and safety. Our BioAstin maintains GRAS status.

5 End Result

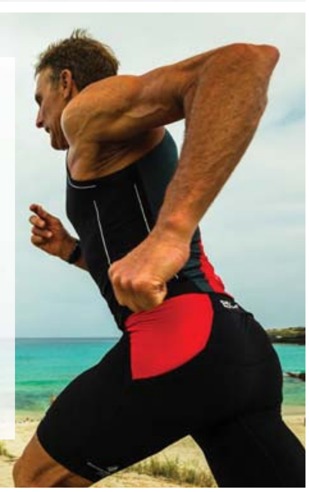
The astaxanthin oil is then encapsulated in a soft gel in either a 4mg dosage for preventative maintenance or a 12mg dosage for more specific conditions like joint discomfort and eye & brain health.* BioAstin is available in a gelatin or vegan soft gel.

6 Deliver and Distribute

BioAstin Hawaiian Astaxanthin is sold in over 40 countries, and is available online directly from Nutrex-Hawaii.com or other websites such as Amazon.com, as well as through a variety of traditional brick-and-mortar stores such as Costco, Whole Foods, Sprouts, and The Vitamin Shoppe. BioAstin is the nation's #1 brand of astaxanthin.

7 Benefits of Use

It is proven in over 300 scientific studies to help the body in many ways, like supporting joints & tendons, skin, eye & brain, and cardiovascular health. BioAstin is also beneficial with recovery from excercise, a reason why many elite athletes swear by it.*



*These statements have not been evaluated by the Food and Drug Administration. This product is not intended to diagnose, treat, cure, or prevent any disease.

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year Ended March 31, 2017

Commission File Number 0-14602

CYANOTECH CORPORATION
(Exact name of registrant as specified in its charter)

Nevada	**91-1206026**
(State or other jurisdiction of incorporation or organization)	(I. R. S. Employer Identification No.)
73-4460 Queen Kaahumanu Highway, Suite 102, Kailua-Kona, Hawaii	**96740**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: **(808) 326-1353**

Securities registered pursuant to Section 12(b) of the Act:	Name of each exchange on which registered:
None	**NASDAQ Capital Market**

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, $0.02 par value
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. ☐ Yes ☒ No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. ☐ Yes ☒ No

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

Indicate by checkmark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§229.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐ No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☐

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

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	☐	(Do not check if a smaller reporting company)	
		Smaller reporting company	☒
		Emerging growth company	☐

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

The aggregate market value of the Registrant's Common Stock held by non-affiliates of the Registrant on September 30, 2016 was approximately $20,918,171 based on the closing sale price of the Common Stock on the NASDAQ Capital Market on that date.

Number of shares outstanding of Registrant's Common Stock at June 22, 2017 was 5,685,381.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Definitive Proxy Statement for its 2017 Annual Meeting of Stockholders, expected to be filed with the Securities and Exchange Commission on or prior to July 7, 2017 and to be used in connection with the Annual Meeting of Stockholders expected to be held on August 24, 2017, are incorporated by reference in Part III of this Form 10-K.

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FORWARD-LOOKING STATEMENTS

This Report and other presentations made by Cyanotech Corporation ("CYAN") and its subsidiary contain "forward-looking statements," which include statements that are predictive in nature, depend upon or refer to future events or conditions, and usually include words such as "expects," "anticipates," "intends," "plan," "believes," "predicts", "estimates" or similar expressions. In addition, any statement concerning future financial performance, ongoing business strategies or prospects and possible future actions are also forward-looking statements. Forward-looking statements are based upon current expectations and projections about future events and are subject to risks, uncertainties and the accuracy of assumptions concerning CYAN and its subsidiary (collectively, the "Company"), the performance of the industry in which CYAN does business, and economic and market factors, among other things. **These forward-looking statements are not guarantees of future performance. You should not place undue reliance on forward-looking statements.**

Forward-looking statements speak only as of the date of the Report, presentation or filing in which they are made. Except to the extent required by the Federal Securities Laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Our forward-looking statements in this Report include, but are not limited to:

- Statements relating to our business strategy;
- Statements relating to our business objectives; and
- Expectations concerning future operations, profitability, liquidity and financial resources.

These forward-looking statements are subject to risk, uncertainties and assumptions about us and our operations that are subject to change based on various important factors, some of which are beyond our control. The following factors, among others, could cause our financial performance to differ significantly from the goals, plans, objectives, intentions and expectations expressed in our forward-looking statements:

- Environmental restrictions, soil and water conditions, levels of sunlight and seasonal weather patterns, particularly heavy rain, wind and other hazards;
- Consumer perception of our products due to adverse scientific research or findings, publicity regarding nutritional supplements, litigation, regulatory investigations or other events, conditions and circumstances involving the Company which receive national media coverage;
- Effects of competition, including tactics and locations of competitors and operating and market competition;
- Demand for our products, the quantities and qualities thereof available for sale and levels of customer satisfaction, including significant unforeseen fluctuations in global demand for products similar to our products;
- Our dependence on the experience, continuity and competence of our executive officers and other key employees;
- The added risks associated with or attributed to the current local, national and world economic conditions, including but not limited to, the volatility of crude oil prices, inflation and currency fluctuations;
- Changes in domestic and/or foreign laws, regulations or standards, affecting nutraceutical products or our methods of operation;
- Access to available and reasonable financing on a timely basis;
- The Company's inability to generate enough revenues to meet its obligations or repay maturing indebtedness;
- Failure of capital projects to operate as expected or meet expected results;
- Changes in laws, corporate governance requirements and tax rates, regulations, accounting standards and the application to us or the nutritional products industry of new decisions by courts, regulators or other government authorities;
- Legal costs associated with any legal proceedings, and the potential direct and indirect cost and other effects on our business or financial condition resulting from any legal proceedings.
- Risk associated with the geographic concentration of our business;
- Acts of war, terrorist incidents or natural disasters; and
- Other risks or uncertainties described elsewhere in this Report and in other periodic reports previously and subsequently filed by us with the Securities and Exchange Commission.

PART I

Item 1. Business

Unless otherwise indicated, all references in this report to the "Company", "we", "us", "our", and "Cyanotech" refer to Cyanotech Corporation and its wholly owned subsidiary, Nutrex Hawaii, Inc. ("Nutrex Hawaii" or "Nutrex"), a Hawaii corporation.

General

We are a world leader in the production of high value natural products derived from microalgae. Incorporated in 1983, we are guided by the principle of providing beneficial, quality microalgal products for health and human nutrition in a sustainable, reliable and environmentally sensitive operation. We are GMP (Good Manufacturing Practices) certified by the Natural Products Association™, reinforcing our commitment to quality in our products, quality in our relationships (with our customers, suppliers, employees and the communities we live in), and quality of the environment in which we work. Our products include:

- Hawaiian *BioAstin*® natural astaxanthin - a powerful dietary antioxidant shown to support and maintain the body's natural inflammatory response, to enhance skin, and to support eye and joint health. It has expanding applications as a human nutraceutical and functional food ingredient; and

- Hawaiian *Spirulina Pacifica*® - a nutrient-rich dietary supplement used for extra energy, a strengthened immune system, cardiovascular benefits and as a source of antioxidant carotenoids

Microalgae are a diverse group of microscopic plants that have a wide range of physiological and biochemical characteristics and contain, among other things, high levels of natural protein, amino acids, vitamins, pigments and enzymes. Microalgae have the following properties that make commercial production attractive: (1) microalgae grow much faster than land grown plants, often up to 100 times faster; (2) microalgae have uniform cell structures with no bark, stems, branches or leaves, permitting easier extraction of products and higher utilization of the microalgae cells; and (3) the cellular uniformity of microalgae makes it practical to control the growing environment in order to optimize a particular cell characteristic. Efficient and effective cultivation of microalgae requires consistent light, warm temperatures, low rainfall and proper chemical balance in a very nutrient-rich environment, free of environmental contaminants and unwanted organisms. This is a challenge that has motivated us to design, develop and implement proprietary production and harvesting technologies, systems and processes in order to commercially produce human nutritional products derived from microalgae.

Our production of these products at the 90-acre facility on the Kona Coast of the island of Hawaii provides several benefits. We selected the Keahole Point location in order to take advantage of relatively consistent warm temperatures, sunshine and low levels of rainfall needed for optimal cultivation of microalgae. This location also offers us access to cold deep ocean water, drawn from an offshore depth of 2,000 feet, which we use in our *Ocean-Chill Drying* system to eliminate the oxidative damage caused by standard drying techniques and as a source of trace nutrients for microalgal cultures. The area is also designated a Biosecure Zone, with tight control of organisms allowed into the area and free of genetically modified organisms (GMO's). We believe that our technology, systems, processes and favorable growing location generally permit year-round harvest of our microalgal products in a cost-effective manner.

Our Business

We operate entirely in one operating segment, the cultivation and production of microalgae into high-value, high-quality natural health and nutrition products. We cultivate, on a large-scale basis, two microalgal species from which our two major product lines, natural astaxanthin products and spirulina products, are derived. We record revenue and cost of sales information by product category, but do not record operating expenses by such product category.

The following table sets forth, for the three years ended March 31, 2017, the net sales contributed by each of our product lines (in thousands):

	Net Sales		
	2017	2016	2015
Natural astaxanthin products:			
BioAstin®	$ 19,357	$ 19,829	$ 22,087
Spirulina products:			
Spirulina Pacifica®	12,685	12,011	11,722
Total	$ 32,042	$ 31,840	$ 33,809

Natural Astaxanthin Products

We commenced commercial production of natural astaxanthin in 1997 and in 1999 introduced *BioAstin®*, our natural astaxanthin product for the human health and nutrition market. *BioAstin®* represents approximately 60% of our net sales. Astaxanthin's antioxidant properties are believed to surpass many of the antioxidant properties of vitamin C, vitamin E, beta-carotene and other carotenoids. Independent scientific studies indicate that in certain models, natural astaxanthin has up to 550 times the antioxidant activity of vitamin E and 10 times the antioxidant activity of beta-carotene. In addition, a growing body of scientific literature suggests that natural astaxanthin has beneficial properties as an anti-inflammatory, with additional benefits for joint, skin and eye health.

BioAstin® is produced in two forms: a liquid lipid extract and gelcaps, both of which are sold in bulk quantities. *BioAstin®* gelcaps are also sold in packaged consumer form under the Nutrex Hawaii label as well as private label consumer packaged product. Over time, we have shifted our focus and resources on producing and marketing natural astaxanthin for the higher value packaged consumer market.

BioAstin® is GRAS (generally recognized as safe) as determined by the United States Food and Drug Administration. Our all natural *BioAstin®* is cultivated without the use of herbicides or pesticides, and is not genetically modified (non GMO). In fiscal 2012, we applied for a new dietary ingredient (NDI), with the United States Food and Drug Administration, providing for a daily dosage of 12mg of astaxanthin which was reviewed without comment.

We produce natural astaxanthin from *Haematococcus pluvialis* microalgae grown in fresh water supplemented with nutrients. As these algae are extremely susceptible to contamination by unwanted algae, protozoa and amoebae, we developed a proprietary system known as the *PhytoDome Closed Culture System* or *PhytoDome CCS* to overcome this problem. Using these large-scale photobioreactors, we have generally been able to grow consistently large volumes of contaminant-free *Haematococcus* culture, although quarterly production levels are subject to seasonality. Fresh water is critical to the production of our natural astaxanthin and while we have not experienced any constraint on fresh water availability to date, availability could be impacted by a significant population growth in the region as well as throughput constraints on the water delivery infrastructure. We have met with officials of the County of Hawaii to assess the fresh water situation and evaluate the probability of future risks. We recycle fresh water in our production process where possible and continue to explore further recycling opportunities.

For the final stage of cultivation, the *Haematococcus* algae is transferred to open ponds where an environmental stress is applied causing the algae to form spores which accumulate high levels of astaxanthin. Once ready for harvest, the media containing these spores is transported through underground pipes to our astaxanthin processing building where the culture media and algal spores are separated. Fresh water recovered from this stage of processing is recycled for further use in cultivation. Unlike spirulina, astaxanthin is produced in a batch-mode and each cultivation pond must be completely drained and thoroughly cleaned between cycles. As sunlight is a major component of cultivation, production can be impacted by inclement weather and seasonal changes during the winter months, with shorter daylight hours and increased cloud cover.

The harvested algal spores are dried to flakes or a fine powder. During processing, the spores are cracked in a proprietary system to assure high bioavailability of astaxanthin. Each production lot of astaxanthin is sampled and tested for astaxanthin concentration. Finally, the bulk powder is vacuum-packed. Natural astaxanthin for human consumption is processed further utilizing a high-pressure supercritical carbon dioxide extraction process at our facility in Kona. The resulting product is a lipid extract insoluble in water used in the production of gelcaps.

All natural astaxanthin products undergo a prescribed set of microbiological food product tests to ensure safety and quality. We use third party contract manufacturers for the encapsulation and packaging of gelcaps. All third party contract manufacturers are audit inspected by our Quality Department and are required to comply with the Food and Drug Administration (FDA) Good Manufacturing Practices (GMP) regulations. These contract manufacturers hold independent third party GMP certifications.

BioAstin® is sold primarily as a packaged consumer product through Nutrex Hawaii directly to natural product distributors, retailers and consumers. It is also sold in liquid lipid form as a raw ingredient to dietary supplement manufacturers, health food formulators and cosmetic manufacturers. *BioAstin®* gelcaps are sold in bulk quantities to international distributors. In 2007, we also introduced a line of *BioAstin®* based nutritional supplements, *MDFormulas*. *MDFormulas* combined the health benefits of *BioAstin®* with other proven nutrients with benefits for targeted applications such as skin, heart and joint health. In 2012, we began selling our 12 milligram *BioAstin®* consumer product and in fiscal 2016 we introduced vegetarian formulas of both 4 and 12 milligram consumer products.

BioAstin® competes directly with similar products marketed by other manufacturers including Fuji Chemical of Japan, Algatechnologies of Israel and BGG of China. In the general category of nutritional supplements, *BioAstin®* and *MDFormulas* also compete with a variety of vitamins, dietary supplements and other antioxidant products available to consumers. The nutritional products market is highly competitive and includes international, national, regional and local producers and distributors, many of whom have greater resources than we have, and many of whom offer a greater variety of products.

The potential benefits of astaxanthin to human health are continuing to emerge. As one of the most potent and bioactive biological antioxidants found in nature, the number of potential roles of natural astaxanthin for human health is growing. Much research has been published in recent years on the beneficial roles of antioxidants in our health, in the aging process and on specific health conditions. The full efficacy of *BioAstin®* as a human nutraceutical supplement requires further significant clinical study. We have spent limited amounts on clinical trials over the past few fiscal years. Independent antioxidant research and prior clinical trials show promising human applications. We hold three United States patents relating to the usage of *BioAstin®* in the treatment of Carpal Tunnel Syndrome, the treatment of canker/cold sores and for its use as a topical and oral sunscreen.

Spirulina Products

We have been producing a strain of spirulina microalgae marketed as Hawaiian *Spirulina Pacifica®* since 1984. *Spirulina Pacifica®* represents approximately 40% of our net sales. *Spirulina Pacifica®* provides a vegetable-based, highly absorbable source of protein, natural beta-carotene, mixed carotenoids, B vitamins, gamma linolenic acid, essential amino acids and other phytonutrients.

Spirulina Pacifica® is produced in two forms: powder and tablets. Powder is used as an ingredient in nutritional supplements and health beverages; tablets are consumed as a daily dietary supplement. Both forms are sold as raw material ingredients in bulk quantities, as packaged consumer products under the Nutrex Hawaii label and as private label consumer packaged products. We recently launched three new spirulina products. Spearmint spirulina tablets provide a fresh, new flavor option for both current consumers and those trying spirulina for the first time, Greens Complete Superfood Powder formula is our entry into the green superfood category, each serving is packed with three grams of spirulina plus organic greens, organic antioxidants and probiotics, and Hawaiian Spirulina Plant Protein Shake is our entry into the Protein supplement category, each serving is packed with three grams of spirulina and is an excellent source of Vitamin B12, Vitamin K, Iron and supplies 32% recommended daily protein.

Spirulina Pacifica® is GRAS (generally recognized as safe) for addition to a variety of foods as determined by the United States Food and Drug Administration. Our all natural *Spirulina Pacifica®* is cultivated without the use of herbicides or pesticides, is not genetically modified (non GMO) and is certified Kosher by Organized Kashrus Laboratories of Brooklyn, New York and certified Halal by the Islamic Food and Nutrition Council of America.

Our *Spirulina Pacifica®* is cultivated in a combination of fresh water and a metered amount of nutrient-rich deep ocean water (containing essential trace elements), drawn from a depth of 2,000 feet below sea level. This water mixture is supplemented with other major required nutrients. With the exception of deep ocean water, the raw materials and nutrients required in our spirulina production are available from multiple sources. In the case of deep ocean water, although abundantly available at this location, the facility to pump and deliver the water to our location is owned by the State of Hawaii. The facility is constructed of two separately located pump stations providing redundancy should one station fail. The State of Hawaii sets the price for deep ocean water annually based on its cost to deliver the water. Fresh water is critical to the production of our *Spirulina Pacifica*® algae and while we have not experienced any constraint on fresh water availability to date, availability could be impacted by a significant population growth in the region as well as throughput constraints on the water delivery infrastructure. We have met with officials of the County of Hawaii to assess the fresh water situation and evaluate the probability of future risks. We recycle fresh water in our production process where possible and continue to explore further recycling opportunities.

The spirulina crop in each pond is circulated by paddlewheels to keep an even blend of nutrients in suspension and a uniform exposure of the algae to sunlight. Our ponds are engineered to maintain the right media depth for sunlight to permeate each crop completely, facilitating rapid growth. The design of our cultivation ponds promotes efficient growing conditions, allowing the *Spirulina Pacifica*® algae to reproduce rapidly. Each pond can be harvested, on average, in six days. As sunlight is a major component of cultivation, production can be impacted by inclement weather and seasonal changes during the winter months, with shortened daylight hours.

Once ready for harvest, a majority of the spirulina algae are pumped from a pond to our processing building where the crop is separated from the culture media. The culture remaining in the ponds serves as an inoculum for the next growth cycle. Harvested spirulina is washed with fresh water and filtered before moving to the drying stage. Culture media separated from spirulina algae during processing are conserved and recycled. Our *Integrated Culture Biology Management* ("ICBM") technology for microalgae cultivation has proven to be a reliable and stable operating environment, allowing us to grow and harvest spirulina without significant contamination by unwanted microorganisms and without associated loss of productivity.

Spirulina Pacifica® powder is dried via our low-oxygen *Ocean-Chill Drying* process, thereby preserving high levels of antioxidant carotenoids and other nutrients sensitive to heat and oxygen. The rapid drying process results in a dark green powder. Spirulina powder is difficult to form into tablets. Most tablet manufacturers either add high amounts (from 10% to 30%) of inert substances to "glue" the tablet together or use a heat granulation process that destroys nutrients. In contrast, our *Spirulina Pacifica*® tablets contain a maximum of 2% of such substances and are produced in cold press compression tablet-making machines.

Each production lot of *Spirulina Pacifica*® is sampled and subjected to thorough quality control analyses including testing for moisture, carotenoids, minerals, color and taste, among others. Further, each lot of our *Spirulina Pacifica*® undergoes a prescribed set of microbiological food product tests, including total aerobic bacteria, coliform bacteria and E. coli. The *Spirulina Pacifica*® powder and tablets are packaged to extend shelf life and ensure product freshness. Our packaged consumer products are bottled and labeled by third party contractors in California. These contractors are subject to regular government inspections and hold Drug Manufacturing Licenses & Processed Food Registrations with the State of California Department of Health. These contract manufacturers hold independent third party GMP certifications. Such packaging services are readily available from multiple sources.

The majority of our bulk spirulina is sold to international health food manufacturers and formulators, many of whom identify and promote our Hawaiian *Spirulina Pacifica*® in their products. Such customers purchase bulk powder or bulk tablets and package these products under their brand label for sale to the health and natural food markets in their countries. Some of the brands produced by these customers are marketed and sold in direct competition with the packaged consumer products sold through our Nutrex Hawaii subsidiary in international channels. In the domestic market, Nutrex Hawaii packaged consumer products are sold through an established health food distribution network or directly to consumers. In selected international markets, we have exclusive sales distributors for both our bulk and packaged consumer products.

Our *Spirulina Pacifica*® products compete with a variety of vitamins, dietary supplements, other algal products and similar nutritional products available to consumers. The nutritional products category is highly competitive and includes international, national, regional and local producers and distributors, many of whom have greater resources than Cyanotech and many of whom offer a greater variety of products. Our direct competition in the spirulina market is currently from Dainippon Ink and Chemical Company's Earthrise facility in California, Parry Nutraceuticals, a division of Murugappa Group of India and several farms in China. In addition, there are numerous other smaller farms throughout the world. We have experienced increased price competition due to the large number of spirulina suppliers as well as customers who generally treat these products as commodities with price being the major determining factor driving their purchasing decision. As one of the largest producers of spirulina, our challenge is to increase our market share among customers who seek the high-quality products we produce while concurrently adjusting our product mix to meet our revenue and profitability targets.

Major Customers

One customer accounted for 24% of our total net sales in the fiscal year ended March 31, 2017. Two customers accounted for 19% and 11%, respectively, of our total net sales in the fiscal year ended March 31, 2016. One customer accounted for 13% of our total net sales in the fiscal year ended March 31, 2015.

Research and Development

Our expertise for many years has been in the development of efficient, stable and cost-effective production systems for microalgal products. We have learned production levels from our systems may not be sustainable across periods of days, weeks, or even months. Accordingly, we typically investigate each specific microalgae identified in the scientific literature for potentially marketable products and for solutions to production stability and efficiency challenges, and then strive to develop the technology to grow such microalgae on a commercial scale or to incorporate procedures or technology to improve production stability and efficiency. Successful microalgal product developments and technical solutions are highly uncertain and dependent on numerous factors, many beyond our control. Products and solutions or improvements that appear promising in early phases of development may be found to be ineffective, may be uneconomical because of manufacturing costs or other factors, may be precluded from commercialization due to the proprietary rights of other companies, or may fail to receive necessary regulatory approvals. We had research and development expenses of $593,000, $633,000 and $517,000 in fiscal years 2017, 2016 and 2015, respectively. We invested $0, $80,000 and $6,000 in scientific clinical trials during fiscal 2017, 2016 and 2015, respectively.

Patents, Trademarks and Licenses

We have been granted four United States patents: one on aspects of our production methods and three relating to usage of our *BioAstin*® products.

Our production method patent is directed to microalgae production technology, and expired in April 2016. Our patents relating to usage of our *BioAstin*® products are three utility patents on the use of astaxanthin, which will expire in December 2019, February 2020 and April 2020.

Although we view our proprietary rights as important, we currently believe that a loss of patent rights is not likely to have a material adverse effect on our present business as a whole. Instead, our commercial results mainly depend upon our trade secrets, know-how, other non-patent proprietary rights, customer relationships, our climate and our location. As a result, we feel that our competitors in the U.S. would not be able to implement competing technology covered by our patents now, after their expirations or otherwise, without our same combination of non-patented attributes.

We have registered trademarks in the U.S. and in some foreign markets, such as the European Union. Our operations are not dependent upon any single trademark, although some trademarks are identified with a number of our products and are important in the sale and marketing of such products.

Regulations

Several governmental agencies regulate various aspects of our business and our products in the United States, including the Food and Drug Administration, the Federal Trade Commission, the Consumer Product Safety Commission, the State of Hawaii Department of Health, the Department of Agriculture, the Environmental Protection Agency, the United States Postal Service, state attorney general offices and various agencies of the states and localities in which our products are sold. We believe we are in compliance with all material government regulations which apply to our products and operations. However, we are not able to predict the nature of any future laws, regulations, interpretations or applications, nor can we predict what effect future changes would have on our business.

Our international customers are subject to similar governmental agency regulations in their various geographic regions. Compliance by our customers with such local regulations is beyond our control and we cannot predict their ability to maintain such compliance. However, we strive to assist our customers in meeting local regulations pertaining to the use and sale of our products whenever possible.

Environmental Matters

In 2002, we were issued under the Endangered Species Act ("ESA") an Incidental Take Permit ("ITP") by the United States Department of Interior Fish and Wildlife Service ("FWS"). The ESA defines "incidental take" as "incidental to, and not for the purpose of, the carrying out of an otherwise lawful activity." This permit authorizes incidental take of the endangered Hawaiian stilt (*Himantopus mexicanus knudseni)* that is anticipated to occur as a result of ongoing operations and maintenance at our Kona facility. As a mandatory component for the issuance of such permit, we submitted and maintain a Habitat Conservation Plan ("HCP") to ensure that the effects of the permitted action on listed species are adequately minimized and mitigated.

The HCP called for the creation of a nesting and breeding ground for the Hawaiian stilt to offset any take activity. We have complied with these requirements since 2002. The breeding program was so successful that the increase in the Hawaiian stilt population in the area became a potential hazard for the adjacent State airport facility. We disassembled the stilt habitat and are mitigating "take" by using standard non-lethal hazing devices to discourage nesting and breeding.

A requirement of the ITP is to provide insurance coverage for funding the project for the term of the ITP. Our insurance broker was unable to locate an underwriter who would provide such a bond. As permitted by law, the FWS waived this requirement recognizing that this HCP did not involve a significant capital expenditure. However, under Hawaii state law, no waiver provision is available. A new ITP was issued by the FWS on September 29, 2006 and by the State of Hawaii Division of Forestry and Wildlife (DOFAW) on October 13, 2006, both of which expired on March 17, 2016.

On March 14, 2016 the Company submitted an application for "Amendment and Extension to Cyanotech Corporation's Habitat Conservation Plan and Incidental Take Permit" to FWS and DOFAW. The term of the requested extension is 19 years ending in 2035. The application was reviewed by the Federal and State Agencies and was conditionally granted at a meeting of the State of Hawaii Endangered Species Recovery Committee (ESRC) on June 13, 2016. The condition was that the Company reach an agreement with a specified property owner for offsite predator mitigation by June 2017. The Company was unable to reach an agreement with the specified property owner. At its June 13, 2017 meeting the ESRC asked that detailed options for offsite mitigation be presented to them within six months. We are working with FWS and DOFAW to develop details of offsite predator mitigation to comply with ESRC requests. While we do not anticipate any significant problems because we have satisfied all conditions of past HCP's/ITP's and our operation is considered by the State of Hawaii as "low effect", there can be no guarantees that FWS and/or DOFAW will not impose additional requirements on us in connection with offsite predator mitigation which may impose additional costs on us.

Employees

As of March 31, 2017, we employed 124 people on a full-time basis. Of the total, 60 are involved in harvesting, production and quality, with the remainder in maintenance, shipping, sales, administration and support. None of our employees are subject to collective bargaining agreements. Management believes that its relations with employees are good.

Company Website and SEC Filings

Our corporate website is *www.cyanotech.com*. There we make available copies of Cyanotech documents, news releases and our filings with the Securities Exchange Commission, or the "SEC", including financial statements. Also included are copies of the Board of Directors Code of Conduct, the Company's Code of Conduct and Ethics, the Nominating and Corporate Governance Committee Charter, the Compensation Committee Charter and the Charter and Powers of the Audit Committee. We also maintain the website *www.nutrex-hawaii.com* dedicated to our wholly owned subsidiary, Nutrex Hawaii, Inc. On that website, *Spirulina Pacifica®* and *BioAstin®* are sold directly online. The information found on our websites, unless otherwise indicated, is not part of this or any other report we file or furnish to the Securities and Exchange Commission.

Item 1A. Risk Factors

You should carefully consider the risks described below which we believe are significant but not the only ones we face. Any of the following risks could have a material adverse effect on our business, financial condition and operating results. You should also refer to the other information contained in this report, including our financial statements and the related notes.

Our production of algae involves an agricultural process, subject to such risks as weather, disease and contamination.

The production of our algae products involves complex agricultural systems with inherent risks including weather, disease, and contamination. These risks are unpredictable and also include such elements as the control and balance of necessary nutrients and other factors. The efficient and effective cultivation of microalgae requires consistent light, warm temperatures, low rainfall and proper chemical balance in a very nutrient-rich environment. If the chemical composition of a pond changes from its required balance, unusually high levels of contamination due to the growth of unwanted organisms or other biological problems may occur and would result in a loss of harvestable output. These often arise without warning and sometimes there are few or no clear indicators as to appropriate remediation or corrective measures. We believe that our technology, systems, processes and favorable growing location generally permit year-round harvest of our microalgal products in a cost-effective manner. However, environmental factors cannot be controlled in an open air environment, therefore, we cannot, and do not attempt to, provide any form of assurance with regard to our systems, processes, location, or cost-effectiveness. To the extent that our production is negatively impacted by environmental factors, we may be unable to fill large orders for one or more months until such time that production improves.

There is risk in operating entirely in one business segment such as the cultivation and production of microalgae at a single production facility.

Single location agricultural and production facilities do not provide the protections and assurances afforded by operations in two or more widely separated locations. Our single location in Hawaii is susceptible to catastrophic natural disasters such as earthquakes, tsunamis, hurricanes and volcanic eruptions. In the event of a natural disaster or localized extended outages of critical utilities or transportation systems, we could experience a significant business interruption. Also, a single agricultural facility provides limited biologic diversity protection against invasive, mutant, or harmful organisms.

Hawaii from time to time has experienced shortages of water, electric power and fuels. Future shortages could disrupt our operations and could result in additional expense. Our *Spirulina Pacifica®* is cultivated in a combination of fresh water and deep ocean water. In the case of deep ocean water, although abundantly available at this location, the facility to pump and deliver the water to our location is owned by the State of Hawaii. The State of Hawaii sets the price for deep ocean water annually based on its cost to deliver the water. Any significant increase in the price could adversely affect our business. In addition, while we have not experienced any constraint on fresh water availability to date, availability could be impacted by a significant population growth in the region as well as throughput constraints on the water delivery infrastructure. We have met with officials of the County of Hawaii to assess the fresh water situation and evaluate the probability of future risks. If we are unable to obtain enough fresh water at reasonable prices to cultivate our products, our business could be negatively impacted.

Our facilities in Hawaii are located adjacent to a major airport, and an aircraft disaster could disrupt our operations.

Our production facility and corporate headquarters in Hawaii are located adjacent to the Keahole International airport. In the event of an aircraft disaster, we could experience a significant business interruption, including loss of water, electrical and communication services as well as inability to access our facilities.

Unfavorable publicity or consumer perception of our products and any similar products distributed by other companies could have a material adverse effect on our business.

The nutritional supplements market is highly dependent upon consumer perception regarding the safety, efficacy and quality of nutritional supplements. Consumer perception of our products can be significantly influenced by scientific research and findings, as well as by national media attention and other publicity regarding the consumption of nutritional supplements. There can be no assurance that future research or publicity will be favorable to the nutritional supplements market or any product in particular, or consistent with earlier publicity. Our dependence on consumer perception means that any adverse reports, findings or publicity, whether or not accurate or with merit, could have a material adverse effect on the demand for our products and on our results of operations, cash flow and financial condition.

We may become subject to legal proceedings.

We may become subject to claims and legal proceedings in the ordinary course of business. The costs of such proceedings could vary from quarter to quarter based on the status of the proceedings and could have a material impact on our results in any given quarter.

The nutritional products industry is extremely competitive. Many of our significant competitors have greater financial and other resources than we do, and one or more of these competitors could use their greater resources to gain market share at our expense.

The nutritional products market includes international, national, regional and local producers and distributors, many of whom have substantially greater production, financial, research and development, personnel and marketing resources than we do, and many of whom offer a greater variety of products. As a result, each of these companies could compete more aggressively and sustain that competition over a longer period of time than we could. Our lack of resources relative to our significant competitors may cause us to fail to anticipate or respond adequately to development of new products and changing consumer demands and preferences, or may cause us to experience significant delays in obtaining or introducing new or enhanced products. These failures or delays could reduce our competitiveness and cause a decline in our market share and sales. Increased competition in our industry could result in price reductions, reduced gross profit margin or loss of market share, any of which could have a material effect on our business, results of operations and financial condition.

We depend heavily on the unique abilities and knowledge of our officers and key personnel. If we are unable to recruit and retain key personnel, we may be unable to achieve our goals.

Our success depends, to a significant extent, upon the services of key personnel. For example, our Chief Executive Officer (who is also our founder and former Chief Scientific Officer) is our primary scientific resource, continuing to improve production and cultivation technology and to investigate new microalgal products. Our Chief Financial Officer has a unique understanding of our financial systems and needs. Our Vice President of Operations has years of experience with the mechanical operation of the production facility and continues to improve our production process. Our Vice President of Quality and Regulatory Affairs has experience and knowledge of federal and state regulations governing our production processes and product representation essential to continuing compliance. The loss of any such personnel or the delay in the replacement of such personnel could significantly delay the achievement of our business objectives and could adversely affect our ability to do business or provide needed management. We are also in the process of searching for a permanent Chief Executive Officer. Attracting permanent skilled executives in Hawaii can be difficult due to limited local qualified applicants. If we are unable to attract qualified candidates, or if the search process takes longer than expected, it could adversely impact our business.

Our operations are vulnerable because we have limited personnel and redundancy and backup systems in our data management function.

Our internal order, inventory and product data management system is an electronic system through which orders are placed for our products and through which we manage product pricing, shipment, returns and other matters. This system’s continued and uninterrupted performance is critical to our day-to-day business operations. Despite our precautions, unanticipated interruptions in our computer and telecommunications systems have, in the past, caused problems or stoppages in this electronic system. These interruptions, and resulting problems, could occur again in the future. We also have limited personnel available to process purchase orders and to manage product pricing and other matters in any manner other than through this electronic system. Any significant interruption or delay in the operation of this electronic management system could cause a decline in our sales and profitability.

The loss of a major customer could result in a material reduction in our revenues and profitability.

Our top ten customers generated 60% and 58% of our net sales during fiscal 2017 and fiscal 2016, respectively. One customer accounted for 24% of our total net sales in the fiscal year ended March 31, 2017. Accordingly, the loss of one or more of those customers or a substantial decrease in such customers' purchases from us could result in a material reduction in our revenues and profitability.

We could be subject to breaches of our information technology systems, which could damage our reputation and customer relationships. Such breaches could subject us to significant reputational, financial, legal, and operational consequences.

Our business relies on information systems to obtain, rapidly process, analyze and manage data to, among other things:

- facilitate the purchase and distribution of inventory items through numerous distributors;
- receive, process and ship orders on a timely basis;
- accurately bill and collect from customers;

- process payments to suppliers; and
- provide technical support to our customers.

A cyberattack that bypasses our security, or employee error, malfeasance or other disruptions that cause a security breach could lead to a material disruption of our information systems and/or the loss of business information. Such an attack could result in, among other things:

- the theft, destruction, loss, misappropriation or release of confidential data and intellectual property;
- operational or business delays;
- liability for a breach of personal information belonging to our customers or our employees; and
- damage to our reputation any of which could have a material adverse effect on our business, financial condition, and results of operations. In the event of an attack, we would be exposed to a risk of loss or litigation and possible liability, including under laws that protect the privacy of personal information.

Compliance with new and existing governmental regulations could increase our costs significantly and adversely affect our results of operations.

The processing, formulation, manufacturing, packaging, labeling, advertising and distribution of our products are subject to federal laws and regulation by one or more federal agencies, including the FDA, the FTC, the USDA and the EPA. These activities are also regulated by various state, local and international laws and agencies of the states and localities in which our products are sold. Regulations may prevent or delay the introduction, or require the reformulation, of our products, which could result in lost sales and increased costs to us. A regulatory agency may not accept the evidence of safety for any new ingredients that we may want to market, may determine that a particular product or product ingredient presents an unacceptable health risk, may determine that a particular statement of nutritional support on our products or that parties use on the products we manufacture for them, or that we want to use on our products or that third parties want to use on the products we manufacture for them, is an unacceptable drug claim or an unauthorized version of a food “health claim”. A regulatory agency may determine that particular claims are not adequately supported by available scientific evidence. Any such regulatory determination would prevent us from marketing particular products or using certain statements on those products, which could adversely affect our sales of those products.

Additional or more stringent laws and regulations of dietary supplements and other products have been considered from time to time. These developments could require reformulation of some products to meet new standards, recalls or discontinuance of some products not able to be reformulated, additional record-keeping requirements, increased documentation of the properties of some products, additional or different labeling, additional scientific substantiation, or other new requirements. Any of these developments could increase our costs significantly. In addition, regulators' evolving interpretation of existing laws could have similar effects.

If we fail to comply with the reporting obligations of the Exchange Act and Section 404 of the Sarbanes Oxley Act, or if we fail to maintain adequate internal control over financial reporting, our business, financial condition, and results of operations, and investors’ confidence in us, could be materially and adversely affected.

As a public company, we are required to comply with the periodic reporting obligations of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), including preparing annual reports, quarterly reports, and current reports. Our failure to prepare and disclose this information in a timely manner and meet our reporting obligations in their entirety could subject us to penalties under federal securities laws and regulations of The Nasdaq Stock Market LLC (“NASDAQ”), expose us to lawsuits, and restrict our ability to access financing on favorable terms, or at all.

In addition, pursuant to Section 404 of the Sarbanes Oxley Act, we are required to evaluate and provide a management report of our systems of internal control over financial reporting. During the course of the evaluation of our internal control over financial reporting, we could identify areas requiring improvement and could be required to design enhanced processes and controls to address issues identified through this review. This could result in significant delays and costs to us and require us to divert substantial resources, including management time, from other activities. In addition, if we fail to maintain the adequacy of our internal control over financial reporting, we may not be able to ensure that we can conclude on an ongoing basis that we have effective internal control over financial reporting in accordance with the Sarbanes Oxley Act. Moreover, effective internal controls are necessary for us to produce reliable financial reports and are important to help prevent fraud. Any failure to maintain compliance with the requirements of Section 404 on a timely basis could result in the loss of investor confidence in the reliability of our financial statements, which in turn could, negatively impact the trading price of our stock, and adversely affect investors’ confidence in the Company and our ability to access capital markets for financing.

Our three largest shareholders own a substantial portion of our common stock and could exert substantial influence over our business, particularly if any of them choose to work together.

Our three largest shareholders collectively own approximately 46.4% of our common stock. According to publicly filed beneficial ownership reports, Michael Davis, chairman of our board of directors, beneficially held 1,104,011 of shares representing a 19.5% beneficial ownership, the Rudolph Steiner Foundation, or RSF, beneficially owned 767,133 shares representing a 13.6% beneficial ownership, and Meridian OHC Partners held 749,610 shares representing a 13.3% beneficial ownership. The shares held by RSF were originally donated by a foundation affiliated with Mr. Davis or acquired from the proceeds of donations made by that foundation. In addition, Mr. Davis and RSF filed a Schedule 13D with the SEC on March 17, 2017 announcing the formation of a "group" among the two of them and certain of Mr. Davis' affiliates under Section 13 of the Exchange Act. As part of the agreement between Mr. Davis and RSF, RSF has agreed not to sell, transfer or otherwise dispose of any of its shares in the Company unless RSF provides concurrent written notice to an affiliate of Mr. Davis and the Company at least three days prior to the consummation of any such sale, transfer or other disposition.

Our significant stockholders, particularly if they choose to work together, may have the ability to exert significant influence over our business policies and affairs on matters submitted to our stockholders for approval, such as the election or removal of directors, amendments to our certificate of incorporation, the approval of a business combination or certain corporate financing activities. The interests of our significant stockholders could differ from those of other stockholders in ways that could be adverse to the interests of other shareholders. For example, this concentration of ownership could have the effect of delaying or preventing a change of control of our company even if such a transaction is at a premium to the prevailing market price of our common stock and is supported by other shareholders. Concentration of ownership could also harm the market price of our common stock because investors may perceive disadvantages in owning stock in a company that a substantial portion of common stock is controlled by a small number of stockholders.

Some provisions of our charter documents and Nevada law may discourage an acquisition of us by others, even if the acquisition may be in the best interest of our stockholders.

Provisions in our Restated Articles of Incorporation and Amended and Restated Bylaws, as well as certain provisions of Nevada law, could make it more difficult for a third-party to acquire us, even if doing so may benefit our stockholders. These provisions include the authorization of "blank check" preferred stock, the rights, preferences and privileges of which may be established and shares of which may be issued by our board of directors at its discretion from time to time and without stockholder approval.

Because we are incorporated in Nevada, we may be governed by Nevada's statutes governing combinations with interested stockholders and control share acquisitions, which may discourage, delay or prevent someone from acquiring us or merging with us, whether or not it is desired by or beneficial to our stockholders. We have not opted out of the application of these laws but may elect to opt out in the future. Under Nevada's laws governing combinations with interested stockholders, a Nevada corporation may not, in general, engage in certain types of business combinations with any beneficial owner of 10% or more of the corporation's voting shares or an affiliate of the corporation who at any time within two years immediately prior to the date in question was the beneficial owner of 10% or more of the corporation's voting shares, unless the holder has held the stock for two years or the board of directors approved the beneficial owner's acquisition of its shares, the board of directors approved the transaction before the beneficial owner acquired its shares, or holders of at least a majority of the outstanding voting power approve the transaction after the beneficial owner acquired its shares. In addition, Nevada's control share acquisition laws prohibit a purchaser of the shares of an issuing corporation from voting those shares, under certain circumstances and subject to certain limitations, after crossing specified threshold ownership percentages, unless the purchaser obtains the approval of the issuing corporation's disinterested stockholders.

Any provision of our Restated Articles of Incorporation or Amended and Restated Bylaws or of Nevada law that is applicable to us that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock in the event that a potentially beneficial acquisition is discouraged, and could also affect the price that some investors are willing to pay for our common stock.

A significant or prolonged economic downturn could have a material adverse effect on our results of operations.

Our results of operations are affected by the business activity of our customers who in turn are affected by the level of economic activity in the industries and markets that they serve. A decline in the level of business activity of our clients or the economy as a whole could have a material adverse effect on our revenues and profit margin.

The global cost of oil derived energy impacts us in several ways, and it may hinder our efforts to achieve profitability. Oil prices primarily impact us through the costs of electricity, transportation, materials and supplies which are tied to the cost of oil either directly or indirectly. The return of a high cost of oil on a global basis may signal a prolonged economic downturn resulting in a material adverse effect on our business.

Our quarterly operating results may vary from quarter to quarter, which may result in increased volatility of our share price.

We have experienced, and may in the future continue to experience, fluctuations in our quarterly operating results. These fluctuations could reduce the market price of our common stock. Factors that may cause our quarterly operating results to vary include, but are not limited to:

- weather-related cultivation difficulties;
- any non-routine legal fees;
- fluctuations in customer demand;
- business decisions of our customers regarding orders for our products;
- changes in energy costs;
- changes in raw material costs;
- production problems which we cannot solve technically or economically;
- contamination of our cultivation and production facilities;
- effects of weather on our ability to meet customer demand;
- timing of promotional activities;
- the introduction of new products by us or our competitors;
- changes in our pricing policies or those of our competitors;
- changes in seasonal and other trends in our customers' buying patterns;
- changes in government regulation, both domestic and foreign;
- fluctuation in foreign currency exchange rates;
- global economic and political conditions and related risks, including acts of terrorism; and
- other factors beyond our control.

A significant portion of our expense levels are relatively fixed. If net sales are below expectations in any given period, the adverse impact on results of operations may be magnified by our inability to reduce expenses quickly enough to compensate for the sales shortfall.

Our global operations expose us to complex management, foreign currency, legal, tax and economic risks, which we may not be able to address quickly and adequately.

Our products are marketed in a number of countries around the world. For the year ended March 31, 2017, approximately 28% of our net sales were from sales to foreign customers. As a result, we are subject to a number of risks which include, but are not limited to:

- the burden of complying with a wide variety of national and local laws;
- potentially longer payment cycles for foreign sales;
- restrictions (government and otherwise) on the movement of cash;

- the absence in some jurisdictions of effective laws protecting our intellectual and proprietary property rights, or of enforcement of such laws where they do exist;
- changes in government regulations, both domestic and foreign;
- global economic and political conditions and related risks, including acts of terrorism; and
- fluctuations in foreign currency exchange rates.

Climate change initiatives could materially and adversely affect our business, financial condition, and results of operations.

Our manufacturing processes require that we purchase significant quantities of energy from third parties, which results in the generation of greenhouse gases, either directly onsite or indirectly at electric utilities. Both domestic and international legislation to address climate change by reducing greenhouse gas emissions and establishing a price on carbon could create increases in energy costs and price volatility. Considerable international attention is now focused on development of an international policy framework to address climate change. Proposed and existing legislative efforts to control or limit greenhouse gas emissions could affect our energy source and supply choices as well as increase the cost of energy and raw materials derived from sources that generate greenhouse gas emissions. If our suppliers are unable to obtain energy at a reasonable cost in the future, the cost of our raw materials could be negatively impacted which could result in increased manufacturing costs.

If we are unable to protect our intellectual property rights or if we infringe upon the intellectual property rights of others our business may be harmed.

We currently have three United States patents in force for use of our *BioAstin*® products. We regard our proprietary technology, trade secrets, trademarks and similar intellectual property as important and we rely on a combination of trade secret, contract, patent, copyright and trademark law to establish and protect our rights in our products and technology. However, there can be no assurance that we will be able to protect our technology adequately or that competitors will not be able to develop similar technology independently. In addition, the laws of certain foreign countries may not protect our intellectual property rights to the same extent as the laws of the United States. Litigation in the United States or abroad may be necessary to enforce our patent or other intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others or to defend against claims of infringement. Such litigation, even if successful, could result in substantial costs and diversion of resources and could have a material adverse effect on our business, results of operations and financial condition. Additionally, if any such claims are asserted against us, we may seek to obtain a license under the third party’s intellectual property rights. There can be no assurance, however, that a license would be available on terms acceptable or favorable to us, if at all.

Our insurance liability coverage is limited and may not be adequate to cover potential losses.

In the ordinary course of business, we purchase insurance coverage (e.g., property and liability coverage) to protect us against loss of or damage to our properties and claims made by third parties and employees for property damage or personal injuries. However, the protection provided by such insurance is limited in significant respects and, in some instances, we have no coverage and certain of our insurance policies have substantial “deductibles” or limits on the maximum amounts that may be recovered. For example, if a tsunami, earthquake or other catastrophic natural disaster should occur, we may not be able to recover all facility restoration costs and revenues lost from business interruption. In addition, we maintain product liability insurance in limited amounts for all of our products involving human consumption; however, broader product liability coverage is prohibitively expensive. Insurers have also introduced new exclusions or limitations of coverage for claims related to certain perils including, but not limited to, mold and terrorism. If a series of losses occurred, such as from a series of lawsuits in the ordinary course of business each of which were subject to the deductible amount, or if the maximum limit of the available insurance were substantially exceeded, we could incur losses in amounts that would have a material adverse effect on our results of operations and financial condition.

Our ability to develop and market new products or modify existing products and production methods may be adversely affected if we lose the services of or cannot replace certain employees knowledgeable in advanced scientific and other fields.

Our products are derived from and depend on proprietary and non-proprietary processes and methods founded on advanced scientific knowledge, skills, and expertise. If the services of employees knowledgeable in these fields are lost and cannot be replaced in a reasonable time frame at reasonable costs, our ability to develop and market new products or modify existing products and production methods would be adversely impacted. At the same time, regulatory compliance surrounding our products and financial matters generally requires a basic knowledge and level of expertise related to production, quality assurance, and financial control. If we lose the services or cannot reasonably replace employees who have the necessary knowledge and expertise our ability to remain in regulatory compliance could be adversely affected.

We may need to raise additional capital in the future which may not be available.

We believe our cash to be provided from operations will be sufficient to meet our working capital and operating requirements for at least the next 12 months, but we may need to raise additional funds and we may not be able to secure such funding on acceptable terms, if at all. If we raise additional funds through the issuance of equity or convertible debt securities, the percentage ownership of our then current stockholders may be reduced. If we raise additional funds through the issuance of convertible debt securities, or through additional debt or similar instruments, such securities, debt, or similar instruments could have rights senior to those of our common stockholders and such instruments could contain provisions restricting our operations. If adequate funds are not available to satisfy either short-term or long-term capital requirements, we may be required to limit operations with adverse results.

We have incurred significant losses in the past. If we incur significant losses in the future, we will experience negative cash flow which may hamper current operations and prevent us from sustaining or expanding our business.

As of March 31, 2017, we had an accumulated deficit of approximately $15.1 million, primarily as a result of significant losses incurred during fiscal years ended March 31, 2017, 2016, 2008 and 2007 of $1.2 million, $4.4 million, $1.1 million and $7.4 million, respectively. The 2016 loss included a non-cash impairment of a deferred tax asset, and the 2007 loss included a non-cash impairment loss on equipment and leasehold improvements of $4.5 million. These account for approximately 93% of our accumulated deficit since our inception. Historically, we have relied upon cash from operations and financing activities to fund all of the cash requirements of our business. However, no assurance can be provided that we will return to profitability and extended periods of profitability and net income do not assure positive cash flows. Future periods of net losses from operations could result in negative cash flow, and may hamper ongoing operations and prevent us from sustaining or expanding our business. We cannot assure you that we will achieve, sustain or increase profitability on a quarterly or annual basis in the future. If we do not achieve, sustain or increase profitability, our business will be adversely affected and our stock price may decline.

Our stock price is volatile, which could result in substantial losses for investors purchasing shares of our common stock.

Stock markets have experienced extreme volatility that has often been unrelated to the operating performance of particular companies. These broad market fluctuations may adversely affect the trading price of our common stock. In addition, the average daily trading volume of the securities of small companies can be very low. Limited trading volume of our stock may contribute to its future volatility. Price declines in our common stock could result from general market and economic conditions and a variety of other factors, including any of the following:

- volatility resulting from minimal trading activity;
- changes in market valuations of similar companies;
- stock market price and volume fluctuations generally;
- economic conditions specific to the nutritional products industry;
- economic conditions tied to global resource markets, such as fuel costs;
- announcements by us or our competitors of new or enhanced products or of significant contracts, acquisitions, strategic relationships, joint ventures or capital commitments;
- fluctuations in our quarterly or annual operating results;
- changes in our pricing policies or the pricing policies of our competitors;
- changes in foreign currency exchange rates affecting our product costs, pricing or our customers markets;
- regulatory developments effecting our specific products or industry; and

- additions or departures of key personnel.

The price at which you purchase shares of our common stock may not be indicative of the price that will prevail later in the trading market. You may be unable to sell your shares of common stock at or above your purchase price, which may result in substantial losses to you. As of March 31, 2017, there were approximately 5.7 million shares of our common stock outstanding and stockholders holding at least 5% of our stock, individually or with affiliated persons or entities, collectively beneficially owned or controlled approximately 46% of such shares. Sales of large numbers of shares by any of our large stockholders could adversely affect our trading price, particularly given our relatively small historic trading volumes. If stockholders holding shares of our common stock sell, indicate an intention to sell, of if it is perceived that they will sell, substantial amounts of their common stock in the public market, the trading price of our common stock could decline. Moreover, if there is no active trading market of if the volume of trading is limited, holders of our common stock may have difficulty selling their shares.

Recent European Union regulations include stringent requirements for health claims on food and supplement labels.

The European Union has harmonized standards among Member States for health claims on food and supplement labels. The scientific assessment of health claims is performed by the European Food Safety Authority (EFSA), an advisory panel to the European Commission. The European Commission will consider the opinions of EFSA in determining whether to include a health claim on a Positive List of permissible claims. Once the list is published, only health claims for ingredients and products included on the list may be used in promotional materials for products marketed and sold in the European Union. This could severely decrease or limit the marketability for our products in this market area. We have implemented strategies that we believe will allow for continued and increasing sales of our products in the European Union. However there can be no guarantee that such strategies will be successful.

Item 2. Properties

Our principal facility and corporate headquarters is located at the Natural Energy Laboratory of Hawaii Authority ("NELHA") at Keahole Point in Kailua-Kona, Hawaii. It encompasses approximately 90 fully developed acres containing microalgal cultivation ponds, processing facilities, research and quality control laboratories, and sales and administrative offices. The property is leased from the State of Hawaii under a 40-year commercial lease expiring in 2035. Our lessee interest in the NELHA lease is encumbered by a mortgage securing approximately $7.5 million of debt (see footnote 4 and 6 of the financial statements). If we were to require additional land for expansion, we believe that there is sufficient available land at NELHA, provided a revised NELHA lease can be negotiated with acceptable terms. Under the terms of the existing NELHA lease, we could be required to remove improvements at the end of the lease term. Based upon our analysis, we do not believe the projected cost for such removal to be reasonably estimable, or likely, given historical practices. However, conditions could change in the future. It is not possible to predict such changes or estimate any impact thereof. We also rent warehouse space in Rancho Cucamonga, California, and office space in Los Angeles, California.

Item 3. Legal Proceedings

From time to time, we may become party to lawsuits and claims that arise in the ordinary course of business relating to employment, intellectual property, and other matters. There were no significant legal matters outstanding at March 31, 2017.

As we have previously reported, we were previously a party to a litigation action initiated by Meridian OHC Partners, LP ("Meridian") in the United States District Court, District of Nevada. As disclosed in our Form 8-K filed with the Securities and Exchange Commission on February 16, 2017, the court granted our motion to dismiss the lawsuit on January 23, 2017, but granted Meridian a 20-day period to file an amended complaint. On February 13, 2017, Meridian filed an amended complaint in which we were not named as a defendant. As a result, we is no longer a party to the Meridian lawsuit. The lawsuit has continued against other defendants.

On April 6, 2017, after a mediation session before Dispute Resolution & Prevention in Honolulu, Hawaii, the Company and Brent D. Bailey, our former Chief Executive Officer, entered into a Settlement Agreement (the "Settlement Agreement") resolving all disputes between the Company and Mr. Bailey with respect to that certain Separation Agreement and Release of Claims, dated March 31, 2016 (the "Separation Agreement"). The Settlement Agreement is further described in our Form 8-K filed with the Securities and Exchange Commission on April 11, 2017.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is listed and traded on the NASDAQ Capital Market under the symbol "CYAN". The closing price of our common stock was $3.38 as of June 20, 2017. The approximate number of holders of record of our common stock was 400 as of June 20, 2017. The high and low selling prices as reported by NASDAQ were as follows:

Quarter Ended:	June 30	September 30	December 31	March 31
Fiscal 2017				
Common stock price per share:				
High	$ 5.65	$ 5.36	$ 4.30	$ 4.70
Low	$ 4.76	$ 3.43	$ 3.60	$ 3.70
Fiscal 2016				
Common stock price per share:				
High	$ 10.25	$ 9.63	$ 6.08	$ 5.41
Low	$ 8.75	$ 5.73	$ 5.10	$ 3.89

We are prohibited from declaring any common stock dividends without the prior written consent of a lender per the conditions of an existing term loan agreement with such lender. We have never declared or paid cash dividends on our common stock. We currently do not anticipate paying any cash dividends on common stock.

The following table sets forth the Company's common shares authorized for issuance under equity compensation plans:

	Common shares to be issued upon exercise of options and restricted stock units outstanding (in shares)	Weighted-average exercise price of outstanding options and restricted stock units	Common shares available for future grant under equity compensation plans (in shares)
Equity compensation, plans approved by security holders	528,000	$ 3.91	1,564,124

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to provide a reader of our financial statements with a narrative of our financial condition, results of operations, liquidity and certain other factors that may affect our future results from the perspective of management.

Our MD&A should be read in conjunction with the consolidated financial statements and notes thereto appearing elsewhere in this Form 10-K. A more comprehensive description of our products and markets for such products is provided in Part I. Item 1. Business.

Overview

We are a world leader in the production of natural products derived from microalgae, with a core competency in cultivating and processing microalgae into high-value, high-quality natural products for the human nutrition market. We produce our algae in Hawaii and manufacture the finished products in Hawaii and California. Our products are sold as consumer packaged goods to distributors, retailers and direct consumers, primarily in the U.S., as well as in bulk form to manufacturers, formulators and distributors worldwide in the health foods and nutritional supplements markets. We will continue to focus on growing the market for our high quality, higher margin consumer products by emphasizing the higher nutritional content of our Hawaiian spirulina and the benefits of our natural astaxanthin. We generated 28%, 29% and 29% of our revenues outside of the United States during the years ended March 31, 2017, 2016 and 2015, respectively. Competing in a global marketplace, we are influenced by the general economic conditions of the countries in which our customers operate, including adherence to our customers' local governmental regulations and requirements. Since all sales are made in U.S. currency, we have no material foreign exchange exposure.

Our production levels have a significant impact on our gross profit margin, as well as our ability to meet customer demand. Because our processes are agricultural, it is important to maintain production volumes in order to support the minimal resource levels required to sustain a large-scale open culture agricultural facility. Our production costs include customary variables such as availability and costs of personnel, raw materials, energy, water and freight. These variables fluctuate based on changes in the local, national and world economies. More complex variables include cultivation methods, feeding formulations and harvesting processes, all of which include efforts to anticipate the extent of weather and environmental events and make timely and sufficient adjustments. Although the variability of such costs cannot be fully anticipated, we have focused increased effort in this area in order to produce both spirulina and astaxanthin at levels sufficient to fully absorb production costs into inventory.

Fresh water is critical for our natural astaxanthin and spirulina production, while we have not experienced any constraint on fresh water availability, future availability could be negatively impacted by significant growth in the local population as well as by throughput constraints on the water delivery infrastructure owned by the County of Hawaii. Given the criticality of fresh water to our operations and the community, we recycle fresh water where possible and have developed additional water recycling systems in our efforts to utilize fresh water efficiently. Both fresh and sea water require electricity for pumping; and electricity, our single largest expenditure, depends on the cost of fuel which is, in turn, tied to the global price of crude oil.

Complex biological processes in the cultivation and processing of our microalgae are influenced by factors beyond our control—the weather, for example. As a result, we cannot assure that adequate production levels will be consistent period over period. To the extent that our production levels are not sufficient to absorb these costs on a period basis, we recognize abnormal and non-inventoriable production costs, including fixed cost variances from normal production capacity, as an expense in the period incurred. Abnormal amounts of freight, handling costs and wasted material (spoilage) are recognized as current-period charges and fixed production overhead costs are allocated to inventory based on the normal capacity of production facilities. Normal capacity is defined as "the production expected to be achieved over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance." To offset increased production costs, we seek ways to increase production efficiencies in volume yield, potency, and quality consistent with our commitment to produce high-value, high-quality products.

We utilize several third-party contractors for encapsulation of our gelcaps and for the packaging of our finished Nutrex Hawaii products. Although these services are available from a limited number of sources, we believe that we have the ability to use other parties if any of the current contractors become unavailable.

Fiscal 2017 summary:

- Net sales for the year were flat at $32.0 million, an increase of 0.6% from the prior year, driven primarily by a 0.4% decrease in sales of bulk products, offset by a 0.9% increase in sales of our consumer products.

- Fiscal 2017 pretax loss was $1.2 million compared to pretax loss of $1.1 million in fiscal 2016. The loss in fiscal 2017 was primarily a result of an increase in legal costs of $1.2 million related to a shareholder lawsuit.

- Cash provided by operating activities was $1.2 million, an increase of $0.5 million from fiscal year 2016 due primarily to flat inventory levels year over year. Cash at March 31, 2017 increased $0.2 million compared to last year due primarily to decreased spending on equipment and leasehold improvements.

Results of Operations for the 2017, 2016 and 2015 Fiscal Years

The following tables present selected consolidated financial data for each of the past three fiscal years ($ in thousands):

Consolidated Performance Summary	2017	2016	2015
Net sales	$ 32,042	$ 31,840	$ 33,809
Net sales increase (decrease)	0.6%	(5.8)%	20.0%
Gross profit	$ 12,224	$ 11,866	$ 14,466
Gross profit as % of net sales	38.1%	37.3%	42.8%
Operating expenses	$ 12,906	$ 12,651	$ 14,144
Operating expenses as % of net sales	40.3%	39.7%	41.8%
Operating (loss) income	$ (682)	$ (785)	$ 322
Operating (loss) income as % of net sales	(2.1)%	(2.5)%	1.0%
Income tax expense	$ (5)	$ (3,328)	$ (253)
Net loss	$ (1,215)	$ (4,395)	$ (24)

Net sales by product	2017	2016	2015
Packaged sales			
Astaxanthin packaged	$ 18,367	$ 18,347	$ 17,579
Astaxanthin packaged sales increase	0.1%	4.4%	50.7%
Spirulina packaged	$ 7,489	$ 7,282	$ 7,192
Spirulina packaged sales increase	2.8%	1.3%	29.3%
Total Packaged sales	$ 25,856	$ 25,629	$ 24, 771
Total Packaged sales increase	0.9%	3.5%	43.8%
Bulk sales			
Astaxanthin bulk	$ 990	$ 1,482	$ 4,508
Astaxanthin bulk sales (decrease) increase	(33.2)%	(67.1)%	(39.0)%
Spirulina bulk	$ 5,196	$ 4,729	$ 4,530
Spirulina bulk sales increase (decrease)	9.9%	4.4%	27.2%
Total Bulk sales	$ 6,186	$ 6,211	$ 9,038
Total Bulk sales (decrease)	(0.4)%	(31.3)%	(17.5)%

Fiscal 2017 results compared with Fiscal 2016

Net Sales Net sales increased 0.6% in the year ended March 31, 2017 compared with 2016. This increase was driven by a 5.6% increase in spirulina sales, offset by a 2.4% decrease in astaxanthin sales. The increase in spirulina sales was driven by an increase in bulk sales (+9.9%) due to higher production in the last quarter of fiscal 2016 through the third quarter of fiscal 2017. Sales of packaged spirulina also showed modest growth (+2.8%), due to a shift to channels with lower sales discounts. The decrease in astaxanthin sales is due primarily to the discontinuation of a product by one of our European bulk customers. Sales of packaged astaxanthin showed modest growth. One customer accounted for 24% of our total revenue in fiscal 2017. In fiscal 2016, two customers who accounted for 19% and 11% of our total revenue, respectively.

Competition for sales of bulk astaxanthin remains intense due to the large number of suppliers. We expect competitive pricing pressure to continue in future periods and will continue to focus on the higher quality of Hawaiian astaxanthin in support of customers who demand higher quality raw materials for their formulations.

Gross Profit Our gross profit percent of net sales increased by 0.8 percentage points compared to fiscal 2016. This improvement was the result of savings from a full year's utilization of our new extraction facility, coupled with an 8% increase in astaxanthin production with lower production costs. We incurred $0.2 million of non-inventoriable costs during fiscal 2017 related to lower spirulina production in the 4th quarter of fiscal 2017, compared to $0.5 million in fiscal 2016, which included $0.4 million related to start-up costs of our new extraction facility.

Operating Expenses Operating expenses increased by $0.3 million, or 2.0%, in fiscal 2017 and increased as a percentage of net sales by 0.6%. The majority of the increase is in General and Administrative expenses, which increased $0.3 million, or 4.5%, due to an increase in legal fees of $1.2 million related to a shareholder lawsuit, offset by lower costs for stock compensation expense (-$0.4 million), severance costs (-$0.1 million), bad debt expense (-$0.1 million) and audit fees (-$0.1 million).

Other Expense Other expense is comprised primarily of interest expense on term loans, amortization of debt issuance costs and interest on other financing agreements, offset by a nominal amount of interest earned and miscellaneous sales.

Income Taxes We recorded income tax expense of $5,000 in fiscal 2017. For fiscal 2016 we recorded a valuation allowance of $3.6 million against our remaining deferred tax asset, resulting in an income tax expense of $3.3 million and an effective tax rate of (312%).

Fiscal 2016 results compared with Fiscal 2015

Net Sales The net sales decline of 5.8% in fiscal 2016 was driven primarily by a reduction of bulk astaxanthin sales due to lower production. Sales of our spirulina products grew 2.5%, driven by a 4.4% increase in bulk sales and a 1.3% increase in packaged sales. Our astaxanthin sales decreased 10.2% from the prior year, driven by a 67.1% decrease in bulk sales, offset by a 4.4% increase in packaged sales. Both spirulina and astaxanthin are sold in consumer packaged goods distributed primarily in the U.S. and in bulk form for use worldwide. Two customers accounted for 30% of our total revenue in fiscal 2016, compared to one customer who accounted for 13% of revenue in fiscal 2015.

Gross Profit Our gross profit percent of net sales decreased by 5.5 percentage points compared to fiscal 2015. Gross profit was impacted by a 14% decrease in astaxanthin production, which resulted in a higher cost per kilo of astaxanthin sold during the year. Our production was impacted by lower sunlight and an unusual level of mid-day cloud cover in Kona, HI in the first two quarters of fiscal 2016 as a result of the El Nino conditions we experienced. We incurred $0.5 million of non-inventoriable costs during fiscal 2016, including $0.4 million related to start-up costs of our new extraction facility. In fiscal 2015, we incurred $0.2 million of non-inventoriable costs. The decline in gross profit was also due to changes in our customer mix in the first three quarters of the year, which resulted in higher overall sales allowances and reduced gross profit by $0.9 million or 3.6 percentage points during fiscal 2016 compared with fiscal 2015.

Operating Expenses Operating expenses decreased by $1.5 million, or 11%, in fiscal 2016 and decreased as a percentage of net sales by 2.1%. General and Administrative expenses decreased $2.2 million, or 27%, due to a decrease in legal fees of $2.5 million related to matters that were settled in the third quarter of fiscal 2015, offset by higher salaries and benefits ($0.2 million) and costs related to the Company's separation with its former CEO as of March 31, 2106 ($0.5 million). Sales and Marketing expenses increased $0.6 million, or 10%, as a result of the expansion of our distribution of consumer products. A major component of this increase is product demonstration costs which are up by $0.9 million, offset by a decrease of $0.3 million in advertising and promotion costs. Research and development expenses increased $0.1 million, or 22%, due to an increase in salaries and benefits.

Other Expense Other expense is comprised primarily of interest expense on term loans, amortization of debt issuance costs and interest on other financing agreements, offset by a nominal amount of interest earned and miscellaneous sales.

Income Taxes For fiscal 2016 we recorded a valuation allowance of $3.6 million against our remaining deferred tax asset, resulting in an income tax expense of $3.3 million and an effective tax rate of (312%). In fiscal 2015, income tax expense was $0.3 million, an effective tax rate of 111%.

Liquidity and Capital Resources

Sources of Liquidity As of March 31, 2017, we had cash of $1.4 million and working capital of $6.2 million compared to $1.2 million and $6.5 million, respectively, at March 31, 2016. On August 30, 2016, the Credit Agreement, which we entered into with First Foundation Bank (the Bank) on June 3, 2016, became effective. The Credit Agreement allows us to borrow up to $2.0 million on a revolving basis. At March 31, 2017, we had borrowed $0.6 million and had $1.4 million available on the line. The line of credit is subject to renewal on August 30, 2017 and we intend to renew or replace it with another line of credit on or before the expiration date. The Bank has issued a letter to us dated June 12, 2017 indicating it intends to renew the line of credit subject to approval by its credit committee.

As of March 31, 2017, we had $6.9 million of term loans payable to the Bank that require the payment of principal and interest monthly through August 2032. Pursuant to the term loans, we are subject to annual financial covenants, customary affirmative and negative covenants and certain subjective acceleration clauses. As of March 31, 2017 and 2016, our current ratio of 1.92:1 and 1.97:1, respectively, fell short of the Bank's annual requirement of 2.10:1. The Bank has provided us with letters stating they found us to be in compliance with this covenant requirement and all other financial covenants as of March 31, 2017 and 2016, and do not consider these shortfalls to be defaults under the Loan Agreement.

Funds generated by operating activities and available cash continue to be our most significant sources of liquidity for working capital requirements, debt service and funding of maintenance levels of capital expenditures. Based upon our fiscal year 2018 operating plan and related cash flow projections and our projected consolidated financial position as of March 31, 2018, cash flows expected to be generated by operating activities and available financing are expected to be sufficient to fund our operations for at least the next twelve months, and our current ratio is expected to be in compliance with the annual term loan covenant requirement as of March 31, 2018. However, no assurances can be provided that we will achieve our operating plan and cash flow objectives for the next fiscal year ended March 31, 2018 or our projected consolidated financial position as of March 31, 2018. Such estimates are subject to change based on future results and such change could cause future results to vary significantly from expected results.

As indicated above, the Bank has not considered the shortfalls as of March 31, 2017 and 2016 in our current ratio relative to the covenant requirement to be violations of the Loan Agreements. However, in the event we have a shortfall under the Loan Agreements as of March 31, 2018 or future fiscal year ends, there is no assurance that the Bank will not consider such to be a violation of the Loan Agreements and pursue its rights under the arrangements to call for the repayment of the outstanding borrowings payable to the Bank. If this occurs, we may need to raise additional funds to repay the loans; however, we may not be able to secure such funding on acceptable terms, or at all.

Our results of operations and financial condition can be affected by numerous factors, many of which are beyond our control and could cause future results of operations to fluctuate materially as it has in the past. Future operating results may fluctuate as a result of changes in sales volumes to our largest customers, weather patterns, increased competition, increased materials, nutrient and energy costs, government regulations and other factors beyond our control.

A significant portion of our expense levels are relatively fixed, so the timing of increases in expenses is based in large part on forecasts of future sales. If net sales are below expectations in any given period, the adverse impact on results of operations may be magnified by our inability to adjust spending quickly enough to compensate for the sales shortfall. We may also choose to reduce prices or increase spending in response to market conditions, which may have a material adverse effect on financial condition and results of operations.

Contractual Obligations

The following table presents our contractual obligations at March 31, 2017 (in thousands):

	Less Than 1 Year	2-3 Years	4-5 Years	After 5 Years	Total
Term Loans(1)	$ 530	$ 1,156	$ 1,299	$ 3,918	$ 6,903
Capital Leases	93	119	24	—	236
Interest payments(2)	386	661	508	1,156	2,711
Operating Leases(3)	615	1,241	1,064	4,290	7,210
Purchase obligations(4)	406	—	—	—	406
Total	$ 2,030	$ 3,177	$ 2,895	$ 9,364	$ 17,466

Note: For additional information refer to Note 6, *Long-Term Debt* and Note 7, *Leases* in the Notes to Consolidated Financial Statements, included in Item 8, *Financial Statements and Supplementary Data*, of this Annual Report on Form 10-K.

(1) Includes term loans with a balance of $6,903,000 as of March 31, 2017, secured by substantially all of the assets of the Company.

(2) Interest calculated from loan amortization using current rates.

(3) Operating lease obligations do not include percentage rent, property taxes and payments for common area maintenance.

(4) Purchase obligations include agreements to purchase goods or services that are enforceable, are legally binding and specify all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Purchase obligations do not include agreements that are cancelable without penalty.

Cash Flows The following table summarizes our cash flows from operating, investing and financing activities for each of the past three fiscal years ($ in thousands):

	2017	2016	2015
Total cash is provided by (used in):			
Operating activities	$ 1,220	$ 745	$ 1,208
Investing activities	(847)	(3,817)	(3,297)
Financing activities	(206)	2,086	3
Increase (decrease) in cash	$ 167	$ (986)	$ (2,086)

Cash provided by operating activities improved by $0.5 million due primarily to holding inventory flat, compared to last year when we had built safety stock for our packaged items. Reductions in our accounts receivable balance relate to large outstanding balances for two customers at the end of fiscal 2016 that were paid in fiscal 2017, and was offset by reductions of payables and accrued expenses. The decrease in cash provided by operating activities of $0.5 million from $1.2 million in fiscal 2015 to $0.7 million in fiscal 2016 is due primarily to higher increases in inventories and accounts payable.

Cash used in investing activities in fiscal 2017 consisted primarily of small equipment purchases, whereas the prior year activity included the completion of our extraction facility and an expansion of our production capacity. Net cash used in investing activities increased $0.5 million in fiscal 2016 compared to fiscal 2015 due primarily to higher self-funded capital expenditures over and above the use of the remaining restricted cash provided for the completion of our new extraction and warehouse facility

Cash used in financing activities during fiscal 2017 included proceeds of $0.6 million, net, from our line of credit, offset by payments long-term debt and payments in lieu of stock issuance and settlement of taxes related to the former CEO separation agreement. Cash used in financing activities during fiscal 2016 included proceeds from long-term debt to fund our $2.5 million capacity expansion.

Effect of Recently Issued Accounting Standards and Estimates

In December 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-20 *“Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers”* (“ASU No. 2016-20”) and ASU 2016-19 *“Technical Corrections and Improvements”* ("ASU No. 2016-19") which contains amendments that affect a wide variety of topics in the Accounting Standards Codification (“ASC”). The amendments generally fall into one of the following four categories: (a) Amendments related to differences between original guidance and the ASC that either carry forward pre-codification guidance or subsequent amendments into the ASC or to guidance that was codified without some text, reference, or phrasing that, upon review, was deemed important to the guidance; (b) Guidance clarification and reference corrections; (c) Simplification; and (d) Minor improvements. ASU 2016-20 will take effect for public companies for the fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. This guidance is applicable to our fiscal year beginning April 1, 2018. We do not expect that the adoption of this guidance will have a significant impact on our consolidated financial position, results of operations or cash flows.

In November 2016, the FASB issued ASU 2016-18, “*Statement of Cash Flows (Topic 230): Restricted Cash”* (“ASU No. 2016-18”). This update addresses the fact that diversity exists in the classification and presentation of changes in restricted cash on the statement of cash flows under Topic 230, Statement of Cash Flows. ASU 2016-18 will take effect for public companies for the fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. This guidance is applicable to our fiscal year beginning April 1, 2018. We do not anticipate that this guidance will have a material impact on our consolidated financial statements and related disclosures.

In August 2016, FASB issued ASU 2016-15, “*Statement of Cash Flows (Topic 230)*: *Classification of Certain Cash Receipts and Cash Payments”* (“ASU No. 2016-15”). This ASU clarifies and provides specific guidance on eight cash flow classification issues that are not currently addressed by current GAAP and thereby reduces the current diversity in practice. ASU No. 2016-15 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early application permitted. This guidance is applicable to our fiscal year beginning April 1, 2018. We do not anticipate that this guidance will have a material impact on our consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, "*Compensation – Stock Compensation (Topic 718)*: *Improvements to Employee Share-Based Payment Accounting" ("*ASU No. 2016-09*")*. This ASU makes several modifications to Topic 718 related to the accounting for forfeitures, employer tax withholding on share-based compensation, and the financial statement presentation of excess tax benefits or deficiencies. ASU No. 2016-09 also clarifies the statement of cash flows presentation for certain components of share-based awards. The standard is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods, with early adoption permitted. We expect to adopt this guidance on April 1, 2017, and do not anticipate that this guidance will have a material impact on our consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU No. 2016-08, *"Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)"* ("ASU No. 2016-08"), which clarified the revenue recognition implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU No. 2016-10, *"Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing"*, which clarified the revenue recognition guidance regarding the identification of performance obligations and the licensing implementation. In May 2016, the FASB issued ASU No. 2016-12, *"Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients"*, which narrowly amended the revenue recognition guidance regarding collectability, noncash consideration, presentation of sales tax and transition. ASU No. 2016-08, ASU No. 2016-10 and ASU No. 2016-12 are effective during the same period as ASU No. 2014-09, *Revenue from Contracts with Customers*, which is effective for annual reporting periods beginning after December 15, 2017, with the option to adopt one year earlier. This guidance is applicable to our fiscal year beginning April 1, 2018. We do not anticipate that the adoption of ASU No. 2016-08, ASU No. 2016-10 and ASU No. 2016-12 will have a material impact on our consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, *"Leases (Topic 842)" (*"ASU No. 2016-02"). The principle objective of ASU No. 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet. ASU No. 2016-02 continues to retain a distinction between finance and operating leases but requires lessees to recognize a right-of-use asset representing its right to use the underlying asset for the lease term and a corresponding lease liability on the balance sheet for all leases with terms greater than twelve months. ASU No. 2016-02 is effective for fiscal years and interim periods beginning after December 15, 2018. Early adoption of ASU No. 2016-02 is permitted. Entities are required to apply the amendments at the beginning of the earliest period presented using a modified retrospective approach. This guidance is applicable to our fiscal year beginning April 1, 2019. We expect this guidance will have a material impact on our consolidated balance sheets due to the recognition of lease rights and obligations as assets and liabilities, respectively. We do not expect this guidance to have a material effect on our consolidated results of operations and cash flows.

In November 2015, the FASB issued ASU No. 2015-17, "*Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes"*. This guidance simplifies the presentation of deferred income taxes and requires that deferred tax assets and liabilities be classified as noncurrent in the classified statement of financial position. ASU 2015-17 will take effect for public companies for the fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. This guidance is applicable to the Company beginning April 1, 2017. We do not expect this guidance to have a material effect on our consolidated financial position, results of operations or cash flows.

In August 2015, the FASB issued ASU 2015-14, *"Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date"*, which defers the effective date of ASU 2014-09 by one year to December 15, 2017 for interim and annual reporting periods beginning after that date, and permitted early adoption of the standard, but not before the original effective date.

In July 2015, the FASB issued ASU No. 2015-11, *"Inventory: Simplifying the Measurement of Inventory"*, that requires inventory not measured using either the last in, first out (LIFO) or the retail inventory method to be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable cost of completion, disposal, and transportation. The new standard will be effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and will be applied prospectively. Early adoption is permitted. This guidance is applicable to our fiscal year beginning April 1, 2017. We do not anticipate that this guidance will have a material impact on our consolidated financial statements and related disclosures.

In August 2014, the FASB issued ASU No. 2014-15, "*Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern"*, which requires management to assess, at each annual and interim reporting period, the entity's ability to continue as a going concern within one year from the date the financial statements are issued and provide related disclosures. As required, we adopted this standard as of December 31, 2016.

In May 2014, The FASB issued ASU No 2014-09, *"Revenue from Contracts with Customers (Topic 606)"*. This guidance, as amended by subsequent ASUs on the topic, supersedes current guidance on revenue recognition in topic 605, Revenue Recognition. This guidance will be effective for annual periods beginning after December 15, 2017, including interim reporting periods. Early application of the guidance is permitted for annual periods beginning after December 31, 2016. This guidance is applicable to our fiscal year beginning April 1, 2018. We expect to adopt this guidance when effective in the first quarter of the fiscal year ended March 31, 2019 and is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures. We expect to complete this evaluation in December 2017.

Application of Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. The preparation of financial statements in conformity with those accounting principles requires management to make judgments and estimates that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates. Management regularly re-evaluates its judgments and estimates which are based upon historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Management believes that of its significant accounting policies, policies that may involve a higher degree of judgment and complexity are inventory valuations, valuation of equipment and leasehold improvements and long-lived assets, and income taxes.

Revenue - We recognize revenues when the customer takes ownership and assumes the risk of loss. We have determined that transfer of title and risk of loss generally occurs when product is received by the customer, except in instances where the shipment terms are explicitly FOB Origin, and accordingly we recognize revenue at the point of delivery to the customer. For shipments with terms of FOB Origin where transfer of title and risk of loss occurs at the point of shipping, revenue is recognized upon shipment to the customer. Sales returns and allowances are estimated and recorded as a reduction to sales in the period in which sales are recorded. We record net shipping charges and sales tax in cost of goods sold.

Inventory - We record inventories at the lower of cost or net realizable value. Cost is defined as the sum of the applicable expenditures and charges directly or indirectly incurred in bringing inventories to their existing condition and location. Cost for inventory purposes may be determined under any one of several assumptions as to the flow of cost factors, such as first-in, first-out; average cost; and last-in, first-out. Our inventories are stated using the first-in, first-out method. Inventory values are subject to many critical estimates, including production levels and capacity, changes in the prices paid for raw materials, supplies, and labor, changes in yield, potency, and quality of biomass, changes in processing or production methods, and changes in the carrying value of our inventories resulting from the prices our customers are willing to pay for our products. Such estimates are revised quarterly. Changes in management's estimates could result in increases or decreases in the recorded amounts of inventory and cost of sales.

To the extent that our production levels are not sufficient to absorb all production costs on a period basis, we recognize abnormal production costs, including fixed cost variances from normal production capacity, as an expense in the period incurred. Abnormal amounts of freight, handling costs and wasted material (spoilage) are recognized as current-period charges and fixed production overhead costs are allocated to inventory based on the normal capacity of production facilities. Normal capacity is defined as "the production expected to be achieved over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance." Changes in management's estimates could result in increases or decreases in the recorded amounts of inventory and cost of sales.

Management reviews inventory levels, inventory turnover, product age and product marketability quarterly to evaluate recoverability and determine if a reserve for inventory is deemed necessary. At March 31, 2017 an inventory reserve in the amount of $3,000 has been recorded, compared to $8,000 as of March 31, 2016.

Equipment and leasehold improvements - Equipment and leasehold improvements are reported at cost less accumulated depreciation and amortization. Self-constructed leasehold improvements include design, construction and supervision costs. These costs are recorded in construction in progress and are transferred to equipment and leasehold improvements when construction is completed and the facilities are placed in service. Long-lived assets, such as property, plant and equipment and purchased intangibles subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized to the extent that the carrying amount exceeds the asset's fair value. We have not recognized any impairment of long lived assets as of March 31, 2017 or 2016.

Stock-Based Compensation - We provide compensation benefits in the form of stock options, restricted stock units and restricted stock grants to employees and non-employee directors. Our stock-based compensation expense is based on the fair value of awards, adjusted for estimated forfeitures, and amortized on a straight-line basis over the requisite service period for stock options and restricted stock units ("RSUs"). The fair value of stock options is estimated as of the date of grant using the Black-Scholes option-pricing model. This model requires input assumptions for our expected dividend yield, expected stock price volatility, risk-free interest rate and the expected option term. Restricted stock and RSUsare valued at the fair value of our common stock as of the date of the grant. See Note 9 in the Notes to our consolidated financial statements included in this 10-K.

Income taxes - Income taxes are accounted for under the asset and liability method. The asset and liability method requires the recognition of deferred tax assets and liabilities for the expected future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using enacted income tax rates applicable to the period in which the deferred tax assets or liabilities are expected to be recovered or settled. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible.

Our judgment is required in determining any valuation allowance recorded against deferred tax assets, specifically net operating loss carryforwards, tax credit carryforwards and deductible temporary differences that may reduce taxable income in future periods. In assessing the need for a valuation allowance, we consider all available evidence including past operating results, estimates of future taxable income and tax planning opportunities. In the event we change our determination as to the amount of deferred tax assets that can be realized, we will adjust our valuation allowance with a corresponding impact to income tax expense in the period in which such determination is made.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

We do not enter into any transactions using derivative financial instruments or derivative commodity instruments and believe that our exposure to market risk associated with other financial instruments is not material.

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Shareholders
Cyanotech Corporation

We have audited the accompanying consolidated balance sheets of Cyanotech Corporation (a Nevada corporation) and subsidiary (the “Company”) as of March 31, 2017 and 2016, and the related consolidated statements of operations, stockholders’ equity and cash flows for each of the three years in the period ended March 31, 2017. Our audits of the basic consolidated financial statements included the financial statement schedule listed in the index appearing under Item 15(a)(2). These financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of the Company’s internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Cyanotech Corporation and subsidiary as of March 31, 2017 and 2016, and the results of their operations and their cash flows for each of the three years in the period ended March 31, 2017 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ GRANT THORNTON LLP

Irvine, California
June 22, 2017

CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

March 31,

	2017	2016
	(in thousands, except share data)	
ASSETS		
Current assets:		
Cash	$ 1,407	$ 1,240
Accounts receivable, net of allowance for doubtful accounts of $49 in 2017 and $136 in 2016	2,135	2,983
Inventories, net	7,972	7,856
Deferred tax assets	157	74
Prepaid expenses and other current assets	565	502
Total current assets	12,236	12,655
Equipment and leasehold improvements, net	16,712	17,796
Other assets	213	696
Total assets	$ 29,161	$ 31,147
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Line of credit	$ 611	$ —
Current maturities of long-term debt	623	574
Customer deposits	119	117
Accounts payable	3,666	4,000
Accrued expenses	1,013	1,430
Total current liabilities	6,032	6,121
Long-term debt, less current maturities	6,249	7,094
Deferred tax liabilities	157	74
Other long term liabilities	116	30
Total liabilities	12,554	13,319
Commitments and contingencies		
Stockholders' equity:		
Preferred stock of $0.01 par value, authorized 10,000,000 shares; no shares issued and outstanding	—	—
Common stock of $0.02 par value, authorized 50,000,000 shares; issued and outstanding 5,685,381 shares at March 31, 2017 and 5,599,797 shares at March 31, 2016	114	112
Additional paid-in capital	31,577	31,585
Accumulated deficit	(15,084)	(13,869)
Total stockholders' equity	16,607	17,828
Total liabilities and stockholders' equity	$ 29,161	$ 31,147

See accompanying notes to consolidated financial statements

CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended March 31,

	2017	2016	2015
	(in thousands, except per share data)		
Net sales	$ 32,042	$ 31,840	$ 33,809
Cost of sales	19,818	19,974	19,343
Gross profit	12,224	11,866	14,466
Operating expenses:			
General and administrative	6,054	5,796	7,960
Sales and marketing	6,259	6,222	5,667
Research and development	593	633	517
Total operating expense	12,906	12,651	14,144
(Loss) income from operations	(682)	(785)	322
Other expense:			
Interest expense, net	(528)	(282)	(93)
Total other expense, net	(528)	(282)	(93)
(Loss) income before income tax expense	(1,210)	(1,067)	229
Income tax expense	(5)	(3,328)	(253)
Net loss	$ (1,215)	$ (4,395)	$ (24)
Net loss per share:			
Basic and diluted	$ (0.21)	$ (0.79)	$ (0.00)
Shares used in calculation of net loss per share:			
Basic and diluted	5,658	5,581	5,517

See accompanying notes to consolidated financial statements

CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years ended March 31, 2017, 2016 and 2015

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
	(in thousands, except per share data)				
Balances at March 31, 2014	5,488,038	$ 110	$ 29,891	$ (9,450)	$ 20,551
Issuances of common stock for Director Stock Grants	16,561	—	78	—	78
Issuance of common stock for exercise of stock options for cash	60,200	1	214	—	215
Compensation expense related to stock options	—	—	663	—	663
Net loss	—	—	—	(24)	(24)
Balances at March 31, 2015	5,564,799	111	30,846	(9,474)	21,483
Issuances of common stock for Director Stock Grants	13,198	—	78	—	78
Issuance of common stock for exercise of stock options for cash	21,800	1	74	—	75
Compensation expense related to stock options	—	—	587	—	587
Net loss	—	—	—	(4,395)	(4,395)
Balances at March 31, 2016	5,599,797	112	$ 31,585	(13,869)	17,828
Issuances of common stock for Director Stock Grants	19,117	—	78	—	78
Issuance of common stock for exercise of stock options for cash	18,000	1	50	—	51
Issuance of common stock in connection with severance of former executive	77,500	1	(1)	—	—
Shares withheld from former executive for tax payments	(29,033)	(1)	(146)	—	(147)
Settlement agreement with former executive			(140)	—	(140)
Compensation expense related to stock options	—	1	151	—	152
Net loss	—	—	—	(1,215)	(1,215)
Balances at March 31, 2017	5,685,381	$ 114	$ 31,577	$ (15,084)	$ 16,607

See accompanying notes to consolidated financial statements

CYANOTECH CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended March 31,

	2017	2016	2015
		(in thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	$ (1,215)	$ (4,395)	$ (24)
Adjustments to reconcile net loss to cash provided by operating activities:			
Loss on sale or disposal of assets	63	11	96
Depreciation and amortization	1,978	1,520	1,243
Amortization of debt issue costs and other assets	67	57	56
Share based compensation expense	232	665	741
Provision for allowance for doubtful accounts	—	130	—
Deferred income tax expense	—	3,350	163
Net (increase) decrease in assets:			
Accounts receivable	848	145	(882)
Inventories	(116)	(2,149)	(337)
Prepaid expenses and other assets	27	(39)	22
Net increase (decrease) in liabilities:			
Customer deposits	2	86	1
Accounts payable	(334)	1,036	(219)
Accrued expenses	(417)	306	348
Deferred rent and other liabilities	85	22	—
Net cash provided by operating activities	1,220	745	1,208
CASH FLOWS FROM INVESTING ACTIVITIES:			
Investment in equipment and leasehold improvements	(847)	(4,303)	(4,179)
Proceeds from restricted cash	—	486	882
Net cash used in investing activities	(847)	(3,817)	(3,297)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from short term notes payable	600	500	—
Net draw down on line of credit	611	—	—
Payment of short term notes payable	(600)	(500)	—
Proceeds from long-term debt, net of costs	—	2,407	—
Payments on capitalized leases	(77)	(44)	(2)
Principal payments on long-term debt	(504)	(352)	(210)
Shares withheld from former executive for tax payments	(147)	—	—
Settlement agreement with former executive	(140)	—	—
Proceeds from issuance of common stock and exercise of stock options	51	75	215
Net cash (used in) provided by financing activities	(206)	2,086	3
Net increase (decrease) in cash	167	(986)	(2,086)
Cash at beginning of year	1,240	2,226	4,312
Cash at end of year	$ 1,407	$ 1,240	$ 2,226
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Cash paid during the year for:			
Interest	$ 431	$ 362	$ 294
Income taxes	$ —	$ 47	$ 8

See accompanying notes to consolidated financial statements

CYANOTECH CORPORATION AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 Description of Business and Summary of Accounting Policies

Description of Business

Cyanotech Corporation (the “Company”) cultivates and produces high-value, high-quality natural products derived from microalgae for the nutritional supplements market. The Company currently cultivates, on a large-scale basis, two microalgal species from which its two major product lines are derived. The Company manufactures all of its products in the United States and sells its products worldwide. As the Company’s operations are solely related to microalgae-based products, management of the Company considers its operations to be in one industry segment. Correspondingly, the Company records revenue and cost of sales information by product category.

Basis of Presentation

The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. The accompanying consolidated financial statements include the accounts of Cyanotech Corporation and its wholly owned subsidiary, Nutrex Hawaii, Inc. (“Nutrex Hawaii” or “Nutrex”). All significant intercompany balances and transactions have been eliminated in consolidation.

Liquidity and Debt Covenant Compliance

As of March 31, 2017, the Company had cash of $1.4 million and working capital of $6.2 million compared to $1.2 million and $6.5 million, respectively, at March 31, 2016. On August 30, 2016, the Credit Agreement, which the Company and First Foundation Bank (the Bank) entered into on June 3, 2016, became effective. The Credit Agreement allows the Company to borrow up to $2.0 million on a revolving basis. At March 31, 2017, the Company had borrowed $0.6 million and had $1.4 million available on the line. The line of credit is subject to renewal on August 30, 2017 and the Company intends to renew or replace it with another line of credit on or before the expiration date. The Bank has issued a letter to the Company dated June 12, 2017 indicating it intends to renew the line of credit subject to approval by its credit committee.

As of March 31, 2017, the Company had $6.9 million of term loans payable to the Bank that require the payment of principal and interest monthly through August 2032. Pursuant to the term loans, the Company is subject to annual financial covenants, customary affirmative and negative covenants and certain subjective acceleration clauses. As of March 31, 2017 and 2016, the Company's current ratio of 1.92:1 and 1.97:1, respectively, fell short of the Bank's annual requirement of 2.10:1. The Bank has provided the Company with letters stating they found the Company to be in compliance with this covenant requirement and all other financial covenants as of March 31, 2017 and 2016, and do not consider these shortfalls to be defaults under the Loan Agreements..

Funds generated by operating activities and available cash continue to be the Company's most significant sources of liquidity for working capital requirements, debt service and funding of maintenance levels of capital eexpenditures. Based upon the Company's fiscal year 2018 operating plan and related cash flow projections and the Company's projected consolidated financial position as of March 31, 2018, cash flows expected to be generated by operating activities and available financing are expected to be sufficient to fund the Company's operations for at least the next twelve months, and the Company's current ratio is expected to be in compliance with the annual term loan covenant requirement as of March 31, 2018. However, no assurances can be provided that the Company will achieve its operating plan and cash flow objectives for the next fiscal year or its projected consolidated financial position as of March 31, 2018. Such estimates are subject to change based on future results and such change could cause future results to vary significantly from expected results.

As indicated above, the Bank has not considered the shortfalls as of March 31, 2017 and 2016 in the Company's current ratio relative to the covenant requirement to be violations of the Loan Agreements. However, in the event the Company has a shortfall under the Loan Agreements as of March 31, 2018 or future fiscal year ends, there is no assurance that the Bank will not consider such to be a violation of the Loan Agreements and pursue its rights under the arrangements to call for the repayment of the outstanding borrowings payable to the Bank. If this occurs, the Company may need to raise additional funds to repay the loans; however, the Company may not be able to secure such funding on acceptable terms, or at all.

Estimates and Assumptions

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of any contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the period reported. Management reviews these estimates and assumptions periodically and reflects the effect of revisions in the period that they are determined to be necessary. Actual results could differ significantly from those estimates and assumptions. Significant estimates include forecast of future operating results, cash flows and financial position, inventory valuation and determination of production capacity and abnormal product costs, reserve for inventory, allowance for bad debts and valuation of deferred tax assets.

Financial Instruments

Cash primarily consists of cash on hand and cash in bank deposits.

The Company applies a framework for measuring fair value. That framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 — Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 — Inputs to the valuation methodology include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets;
- Inputs other than quoted prices that are observable for the asset or liability; and
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

If the asset or liability has a specified (contractual) term, the Level 2 input must be observable for substantially the full term of the asset or liability.

Level 3 — Inputs to the valuation methodology are unobservable and significant to the fair value.

Cash, Accounts Receivable, Accounts Payable and Accrued Expenses - Due to the short-term nature of these instruments, management believes that the carrying amounts approximate fair value.

Line of Credit and Long-Term Debt - The carrying amount of our line of credit and long-term debt approximates fair value as interest rates applied to the underlying debt are adjusted quarterly to market interest rates, which approximate current interest rates for similar debt instruments of comparable maturities.

Concentration of Credit Risk

The Company maintains its cash accounts with several banks located in Hawaii. The total cash balances are insured by the Federal Deposit Insurance Corporation (“FDIC”) up to $250,000 per bank. The Company had cash balances at March 31, 2017 that exceeded the balance insured by the FDIC by $810,000. One customer accounted for 24% of total net sales in the fiscal year ended March 31, 2017. Three customers accounted for 60% of accounts receivable at March 31, 2017. Two customers accounted for 19% and 11%, respectively, of total net sales in the fiscal year ended March 31, 2016. Two customers accounted for 44% of accounts receivable at March 31, 2016. One customer accounted for 13% of total net sales in the fiscal year ended March 31, 2015. Our top ten customers generated 60%, 58% and 55% of our net sales during fiscal 2017, fiscal 2016 and fiscal 2015, respectively.

Accounts Receivable and Allowance for Doubtful Accounts

Accounts receivable are recorded at the invoiced amount and do not accrue interest. Credit is extended based on evaluation of the customer's financial condition. Collateral is not required. The allowance for doubtful accounts reflects management’s best estimate of probable credit losses inherent in the accounts receivable balance. Management determines the allowance based on historical experience, specifically identified nonpaying accounts and other currently available evidence. Management reviews its allowance for doubtful accounts monthly with a focus on significant individual past due balances over 90 days. All other balances are reviewed on a pooled basis. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. The Company does not have any off-balance sheet credit exposure related to its customers or otherwise.

Inventories, net

Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out (FIFO) method. Market is defined as sales price less cost to dispose and a normal profit margin. Inventory costs include materials, labor, overhead and third party costs.

Management provides a reserve against inventory for known or expected inventory obsolescence. The reserve is determined by specific review of inventory items for product age and quality which may affect salability. At March 31, 2017 and 2016, the inventory reserve was $3,000 and $8,000, respectively.

The Company recognizes abnormal production costs, including fixed cost variances from normal production capacity, as an expense in the period incurred. Abnormal amounts of freight, handling costs and wasted material (spoilage) are recognized as current period charges and fixed production overhead costs are allocated to inventory based on the normal capacity of production facilities. Normal capacity is defined as "the production expected to be achieved over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance." The Company expensed abnormal production costs of $120,000, $395,000 and $639,000 to cost of sales for the fiscal years ended March 31, 2017, 2016 and 2015, respectively. Non-inventoriable fixed costs were $134,000, $149,000 and $182,000 for the fiscal years ended March 31, 2017, 2016 and 2015, respectively, and have been classified in cost of sales.

Equipment and Leasehold Improvements, net

Equipment and leasehold improvements are stated at cost. Depreciation and amortization are provided using the straight-line method over the estimated useful lives for equipment and furniture and fixtures, and the shorter of the land lease term (see Notes 3 and 6) or estimated useful lives for leasehold improvements as follows:

Equipment (in years)	3	to	10
Furniture and fixtures (in years)	3	to	7
Leasehold improvements (in years)	10	to	25

Capital project costs are accumulated in construction-in-progress until completed, at which time the costs are transferred to the relevant asset and commence depreciation. Repairs and Maintenance costs are expensed in the period incurred. Repairs and maintenance that significantly increase the useful life or value of the asset are capitalized and depreciated over the remaining life of the asset. The Company capitalizes interest cost incurred on funds used to construct property, plant, and equipment. The capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life. Interest cost capitalized was $0, $173,000 and $228,000 for the fiscal years ended March 31, 2017, 2016 and 2015, respectively.

Impairment of Long-Lived Assets

Management reviews long-lived assets, such as equipment, leasehold improvements and purchased intangibles subject to amortization for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized to the extent that the carrying amount exceeds the asset's fair value. Assets to be disposed of and related liabilities would be separately presented in the consolidated balance sheet. Assets to be disposed of would be reported at the lower of the carrying value or fair value less costs to sell and would not be depreciated.

Accounting for Asset Retirement Obligations

Management evaluates quarterly the potential liability for asset retirement obligations under the Company's lease for its principal facility and corporate headquarters. No liability has been recognized as of March 31, 2017 and 2016 (see Note 7).

Revenue Recognition

We recognize revenues when the customer takes ownership and assumes the risk of loss. We have determined that transfer of title and risk of loss generally occurs when product is received by the customer, except in instances where the shipment terms are explicitly FOB Origin, and accordingly we recognize revenue at the point of delivery to the customer. For shipments with terms of FOB Origin where transfer of title and risk of loss occurs at the point of shipping, revenue is recognized upon shipment to the customer. Sales returns and allowances are estimated and recorded as a reduction to sales in the period in which sales are recorded. We record net shipping charges and sales tax in cost of goods sold.

Research and Development

Research and development costs are expensed as incurred and consist primarily of labor, benefits and outside research.

Advertising

Advertising costs are expensed as incurred. Total advertising expense for the years ended March 31, 2017, 2016 and 2015 was $813,000, $942,000 and $1,082,000, respectively.

Income Taxes

Income taxes are accounted for under the asset and liability method. The asset and liability method requires the recognition of deferred tax assets and liabilities for the expected future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using income tax rates applicable to the period in which the tax difference is expected to reverse.

Judgment is required in determining any valuation allowance recorded against deferred tax assets, specifically net operating loss carryforwards, tax credit carryforwards and deductible temporary differences that may reduce taxable income in future periods. In assessing the need for a valuation allowance, we consider all available evidence including past operating results, estimates of future taxable income and tax planning opportunities. In the event we change our determination as to the amount of deferred tax assets that can be realized, we will adjust our valuation allowance with a corresponding impact to income tax expense in the period in which such determination is made.

In evaluating a tax position for recognition, management evaluates whether it is more-likely-than-not that a position will be sustained upon examination, including resolution of related appeals or litigation processes, based on the technical merits of the position. If the tax position meets the more-likely-than-not recognition threshold, the tax position is measured and recognized in the Company's financial statements as the largest amount of tax benefit that, in management's judgment, is greater than 50% likely of being realized upon settlement. As of March 31, 2017 and 2016, there was no significant liability for income tax associated with unrecognized tax benefits.

The Company recognizes accrued interest related to unrecognized tax benefits as well as any related penalties in interest expense in its condensed consolidated statements of operations. As of the date of adoption and during the years ended March 31, 2017, 2016 and 2015, there was no accrual for the payment of interest and penalties related to uncertain tax positions.

Share-Based Compensation

The Company accounts for share-based payment arrangements using fair value. The Company currently has no liability-classified awards. Equity-classified awards, including grants of employee stock options, are measured at the grant-date fair value of the award and are not subsequently remeasured unless an award is modified. The cost of equity-classified awards is recognized in the statement of operations over the period during which an employee is required to provide the service in exchange for the award, or the vesting period. All of the Company's restricted stock units and stock options are service-based awards, and considered equity-classified awards; as such, they are reflected in Equity and Stock Compensation Expense accounts.

The Company utilizes the Black-Scholes option pricing model to determine the fair value of each option award. Expected volatilities are based on the historical volatility of the Company's common stock over a period consistent with that of the expected term of the options. The expected term of the options are estimated based on factors such as vesting periods, contractual expiration dates and historical exercise behavior. The risk-free rates for periods within the contractual life of the options are based on the yields of U.S. Treasury instruments with terms comparable to the estimated option terms.

Per Share Amounts

Basic earnings per common share is calculated by dividing net income for the year by the weighted average number of common shares outstanding during the year. Diluted earnings per common share is calculated by dividing net income for the year by the sum of the weighted average number of common shares outstanding during the year plus the number of potentially dilutive common shares (“dilutive securities”) that were outstanding during the year. Dilutive securities include options granted pursuant to the Company’s stock option plans, potential shares related to the Employee Stock Purchase Plan and Restricted Stock grants to employees and non-employees. Dilutive securities related to the Company’s stock option plans are included in the calculation of diluted earnings per common share using the treasury stock method. Potentially dilutive securities are excluded from the computation of earnings per share in periods in which a net loss is reported, as their effect would be antidilutive. A reconciliation of the numerators and denominators of the basic and diluted loss per common share calculations for the years ended March 31, 2017, 2016 and 2015 is presented in Note 11.

New Accounting Pronouncements

In December 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-20 *“Technical Corrections and Improvements to Topic 606, Revenue from Contracts with Customers”* (“ASU No. 2016-20”) and ASU 2016-19 *“Technical Corrections and Improvements”* ("ASU No. 2016-19") which contains amendments that affect a wide variety of topics in the Accounting Standards Codification (“ASC”). The amendments generally fall into one of the following four categories: (a) Amendments related to differences between original guidance and the ASC that either carry forward pre-codification guidance or subsequent amendments into the ASC or to guidance that was codified without some text, reference, or phrasing that, upon review, was deemed important to the guidance; (b) Guidance clarification and reference corrections; (c) Simplification; and (d) Minor improvements. ASU 2016-20 will take effect for public companies for the fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. This guidance is applicable to the Company beginning April 1, 2018. The Company does not expect that the adoption of this guidance will have a significant impact on its consolidated financial position, results of operations or cash flows.

In November 2016, the FASB issued ASU 2016-18, “*Statement of Cash Flows (Topic 230): Restricted Cash”* (“ASU No. 2016-18”). This update addresses the fact that diversity exists in the classification and presentation of changes in restricted cash on the statement of cash flows under Topic 230, Statement of Cash Flows. ASU 2016-18 will take effect for public companies for the fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. This guidance is applicable to the Company beginning April 1, 2018. The Company does not anticipate that this guidance will have a material impact on its consolidated financial statements and related disclosures.

In August 2016, FASB issued ASU 2016-15, “*Statement of Cash Flows (Topic 230)*: *Classification of Certain Cash Receipts and Cash Payments”* (“ASU No. 2016-15”). This ASU clarifies and provides specific guidance on eight cash flow classification issues that are not currently addressed by current GAAP and thereby reduces the current diversity in practice. ASU No. 2016-15 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early application permitted. This guidance is applicable to the Company beginning April 1, 2018. The Company does not anticipate that this guidance will have a material impact on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, “*Compensation – Stock Compensation (Topic 718)*: *Improvements to Employee Share-Based Payment Accounting” (*“ASU No. 2016-09*”).* This ASU makes several modifications to Topic 718 related to the accounting for forfeitures, employer tax withholding on share-based compensation, and the financial statement presentation of excess tax benefits or deficiencies. ASU No. 2016-09 also clarifies the statement of cash flows presentation for certain components of share-based awards. The standard is effective for annual periods beginning after December 15, 2016, and interim periods within those fiscal years, with early adoption permitted. The Company plans to adopt this guidance on April 1, 1, 2017. The Company does not anticipate that the adoption of this guidance will have a material impact on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU No. 2016-08, *“Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)”* (“ASU No. 2016-08”), which clarified the revenue recognition implementation guidance on principal versus agent considerations. In April 2016, the FASB issued ASU No. 2016-10, *“Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing”*, which clarified the revenue recognition guidance regarding the identification of performance obligations and the licensing implementation. In May 2016, the FASB issued ASU No. 2016-12, *"Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients"*, which narrowly amended the revenue recognition guidance regarding collectability, noncash consideration, presentation of sales tax and transition. ASU No. 2016-08, ASU No. 2016-10 and ASU No. 2016-12 are effective during the same period as ASU No. 2014-09, *Revenue from Contracts with Customers*, which is effective for annual reporting periods beginning after December 15, 2017, with the option to adopt one year earlier. This guidance is applicable to the Company's fiscal year beginning April 1, 2018. The Company does not anticipate that the adoption of ASU No. 2016-08, ASU No. 2016-10 and ASU No. 2016-12 will have a material impact on its consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-02, "*Leases (Topic 842)" (*"ASU No. 2016-02"). The principle objective of ASU No. 2016-02 is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet. ASU No. 2016-02 continues to retain a distinction between finance and operating leases but requires lessees to recognize a right-of-use asset representing its right to use the underlying asset for the lease term and a corresponding lease liability on the balance sheet for all leases with terms greater than twelve months. ASU No. 2016-02 is effective for fiscal years and interim periods beginning after December 15, 2018. Early adoption of ASU No. 2016-02 is permitted. Entities are required to apply the amendments at the beginning of the earliest period presented using a modified retrospective approach. This guidance is applicable to the Company beginning April 1, 2019.The Company expects this guidance will have a material impact on the Company's consolidated balance sheets due to the recognition of lease rights and obligations as assets and liabilities, respectively. The Company does not expect this guidance to have a material effect on the Company's consolidated results of operations and cash flows.

In November 2015, the FASB issued ASU No. 2015-17, "*Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes"*. This guidance simplifies the presentation of deferred income taxes and requires that deferred tax assets and liabilities be classified as noncurrent in the classified statement of financial position ASU 2015-17 will take effect for public companies for the fiscal years beginning after December 15, 2016, and interim periods within those fiscal years. This guidance is applicable to the Company beginning April 1, 2017. The Company does not expect this guidance to have a material effect on the Company's consolidated financial position, results of operations or cash flows.

In August 2015, the FASB issued ASU 2015-14, *"Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date"*, which defers the effective date of ASU 2014-09 by one year to December 15, 2017 for interim and annual reporting periods beginning after that date, and permitted early adoption of the standard, but not before the original effective date.

In July 2015, the FASB issued ASU No. 2015-11, *"Inventory: Simplifying the Measurement of Inventory"*, that requires inventory not measured using either the last in, first out (LIFO) or the retail inventory method to be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable cost of completion, disposal, and transportation. The new standard will be effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years, and will be applied prospectively. Early adoption is permitted. This guidance is applicable to the Company beginning April 1, 2017. The Company plans to adopt this guidance on April 1, 2017. The Company does not anticipate that the adoption of this guidance will have a material impact on its consolidated financial statements and related disclosures.

In August 2014, the FASB issued ASU No. 2014-15, *"Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern"*, which requires management to assess, at each annual and interim reporting period, the entity's ability to continue as a going concern within one year from the date the financial statements are issued and provide related disclosures. As required, the Company adopted this standard as of December 31, 2016.

In May 2014, The FASB issued ASU No 2014-09, *"Revenue from Contracts with Customers (Topic 606)"*. This guidance, as amended by subsequent ASUs on the topic, supersedes current guidance on revenue recognition in topic 605, Revenue Recognition. This guidance will be effective for annual periods beginning after December 15, 2017, including interim reporting periods. Early application of the guidance is permitted for annual periods beginning after December 31, 2016. This guidance is applicable to the Company beginning April 1, 2018. The Company expects to adopt this guidance when effective in the first quarter of the fiscal year ended March 31, 2019 and is currently evaluating the effect that the updated standard will have on its consolidated financial statements and related disclosures. The Company expects to complete this evaluation in December 2017.

Note 2 Inventories, net

Inventories consist of the following as of March 31, 2017 and 2016:

	2017	2016
	(in thousands)	
Raw materials	$ 347	$ 375
Work in process	2,036	3,782
Finished goods(1)	5,460	3,543
Supplies	129	156
Inventories, net	$ 7,972	$ 7,856

(1) Net of reserve for obsolescence of $3,000 and $8,000 at March 31, 2017 and 2016, respectively.

Note 3 Equipment and Leasehold Improvements, net

Equipment and leasehold improvements consists of the following as of March 31, 2017 and 2016:

	2017	2016
	(in thousands)	
Equipment(1)	$ 17,492	$ 17,040
Leasehold improvements	13,892	13,797
Furniture and fixtures	380	354
	31,764	31,191
Less accumulated depreciation and amortization	(15,835)	(14,067)
Construction in-progress	783	672
Equipment and leasehold improvements, net	$ 16,712	$ 17,796

(1) Includes $373,000 and $314,000 of equipment under capital lease at March 31, 2017 and 2016 respectlively, with accumulated amortization of $106,000 and $41,000, respectively.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets may not be recoverable. No such event occurred during the fiscal years ended March 31, 2017, 2016 and 2015. The Company recognized a loss on disposal of equipment, leasehold improvements and intangible assets in the amount of $63,000, $11,000 and $96,000 in fiscal 2017, 2016 and 2015 respectively. Depreciation and amortization expense was $1,978,000, $1,520,000 and $1,243,000 for the years ended March 31, 2017, 2016 and 2015, respectively

The Company has capitalized interest in the amount of $0, $173,000 and $228,000 for the fiscal years ended March 31, 2017, 2016 and 2015, respectively.

Note 4 Notes Payable

On August 30, 2016, the Revolving Credit Agreement (the "Credit Agreement"), which the Company and First Foundation Bank ("the Bank") entered into on June 3, 2016, became effective after the Company and the Bank received the necessary approvals from the State of Hawaii to secure the lien on the Company's leasehold property in Kona, Hawaii. The Credit Agreement allows the Company to borrow up to $2,000,000 on a revolving basis. Borrowings under the Credit Agreement bear interest at the Wall Street Journal prime rate (4.00% at March 31, 2017) + 2%, floating. The Credit Agreement's initial term expires on August 30, 2017, and the term may be extended at the Bank's sole discretion. The Credit Agreement includes various covenants as defined in the Credit Agreement. The Credit Agreement also contains standard acceleration provisions in the event of a default by the Company. Proceeds from the revolving line were used to repay a $600,000 short-term loan from First Foundation Bank. At March 31, 2017, the Company had borrowed $611,000 under the Credit Agreement and had $1,389,000 available on the line.

The Credit Agreement grants the Bank the following security interests in the Company's property: (a) a lien on the Company's leasehold interest in its Kona facility; (b) an assignment of the Company's interest in leases and rents on its Kona facility; and (c) a security interest in all fixtures, furnishings and equipment related to or used by the Company at the Kona facility. Each security interest is further subject to the terms of the Credit Agreement.

Note 5 Accrued Expenses

Components of accrued expenses as of March 31, 2017 and 2016 are as follows:

	2017	2016
	(in thousands)	
Wages, commissions, bonus and profit sharing	$ 793	$ 972
Use tax	—	140
Customer rebates	—	74
Rent and utilities	69	49
Other accrued expenses	151	195
Total accrued expenses	$ 1,013	$ 1,430

Note 6 Long-Term Debt

Long-term debt consists of the following as of March 31, 2017 and 2016 as follows:

	2017	2016
	(in thousands)	
Long-term debt	$ 7,139	$ 7,972
Less current maturities	(623)	(574)
Long-term debt, excluding current maturities	6,516	7,398
Less unamortized debt issuance costs	(267)	(304)
Total long-term debt, net of current maturities and unamortized debt issuance costs	$ 6,249	$ 7,094

Term Loans

The Company executed a loan agreement with a lender providing for $2,500,000 in aggregate credit facilities (the "2015 Loan") secured by substantially all the Company's assets, pursuant to a Term Loan Agreement dated July 30, 2015 (the "2015 Loan Agreement"). The 2015 Loan Agreement is evidenced by a promissory note in the amount of $2,500,000, the repayment of which is partially guaranteed under the provisions of a United States Department of Agriculture ("USDA") Rural Development Guarantee program. The proceeds of the 2015 Loan were used to pay off a $500,000 short term note payable that matured on September 18, 2015, acquire new processing equipment and leasehold improvements at the Company's Kona, Hawaii facility.

The provisions of the 2015 Loan require the payment of principal and interest until its maturity on September 1, 2022, the obligation fully amortizes over seven (7) years. Interest on the 2015 Loan accrues on the outstanding principal balance at an annual variable rate equal to the published Wall Street Journal prime rate (4.00% at March 31, 2017) plus 2.0% and is adjustable on the first day of each calendar quarter and fixed for that quarter. At no time shall the annual interest rate be less than 6.00%. The 2015 Loan has a prepayment penalty of 5% for any prepayment made prior to the first anniversary of the date of the 2015 Loan Agreement, which penalty is reduced by 1% each year thereafter until the fifth anniversary of such date, after which there is no prepayment penalty. The balance under the 2015 Loan was $2,049,000 and $2,354,000 at March 31, 2017 and 2016, respectively.

The 2015 Loan includes a one-time origination and guaranty fee totaling $113,900 and an annual renewal fee payable in the amount of 0.50% of the USDA guaranteed portion of the outstanding principal balance as of December 31 of each year, beginning December 31, 2015. The USDA has guaranteed 80% of all amounts owing under the 2015 Loan. The Company is subject to financial covenants and customary affirmative and negative covenants.

The Company executed a loan agreement with a lender providing for $5,500,000 in aggregate credit facilities (the "Loan") secured by substantially all the Company's assets, including a mortgage on the Company's interest in its lease at the National Energy Laboratory of Hawaii Authority, pursuant to a Term Loan Agreement dated August 14, 2012 (the "Loan Agreement"). The Loan Agreement is evidenced by promissory notes in the amounts of $2,250,000 and $3,250,000, the repayment of which is partially guaranteed under the provisions of a USDA Rural Development Guarantee. The proceeds of the Loan have been used to acquire new processing equipment and leasehold improvements at its Kona, Hawaii facility.

The provisions of the Loan required the payment of interest only for the first 12 months of the term; thereafter, and until its maturity on August 14, 2032, the obligation fully amortizes over nineteen (19) years. Interest on the Loan accrues on the outstanding principal balance at an annual variable rate equal to the published Wall Street Journal prime rate (4.00% at March 31, 2017) plus 1.0% and is adjustable on the first day of each calendar quarter and fixed for that quarter. At no time shall the annual interest rate be less than 5.50%. The Loan has a prepayment penalty of 5% for any prepayment made prior to the first anniversary of the date of the Loan Agreement, which penalty is reduced by 1% each year thereafter until the fifth anniversary of such date, after which there is no prepayment penalty. The balance under this Loan was $4,854,000 and $5,049,000 at March 31, 2017 and 2016, respectively. Proceeds from the Loan were classified as restricted cash until drawn upon to acquire new processing equipment and leasehold improvements.

The Loan included a one-time origination and guaranty fees totaling $214,500 and an annual renewal fee payable in the amount of 0.25% of the USDA guaranteed portion of the outstanding principal balance as of December 31 of each year, beginning December 31, 2012. The USDA has guaranteed 80% of all amounts owing under the Loan. The Company is subject to financial covenants and customary affirmative and negative covenants.

The Company's current ratio of 1.92 to 1 and 1.97 to 1 as of March 31, 2017 and 2016, respectively, fell short of the bank's requirement of 2.10 to 1; however, the Company has received a letters from its bank stating that they found the Company to be in compliance with this and all other financial covenants as of March 31, 2017 and 2016, and do not consider these shortfalls to be a defaults under the Loan Agreements.

Capital Leases

In August 2016, the Company executed a capital lease agreement with Thermo Fisher Financial providing for $52,000 in equipment, secured by the equipment financed. The capital lease matures in May 2019 and is payable in 36 equal monthly payments. The interest rate under this capital lease is 12.90%. The balance under this lease was $43,000 and $0 at March 31, 2017 and 2016, respectively.

In February 2016, the Company executed a capital lease agreement with Bank of the West providing for $51,000 in equipment, secured by the equipment financed. The capital lease matures in March 2021 and is payable in 60 equal monthly payments. The interest rate under this capital lease is 4.18%. The balance under this lease was $42,000 and $50,000 at March 31, 2017 and March 31, 2016, respectively.

In July 2015, the Company executed a capital lease agreement with Huntington Technology Finance providing for $174,000 in equipment, secured by the equipment financed. The capital lease matures in July 2020 and is payable in 60 equal monthly payments. The interest rate under this capital lease is 6.57%. The balance under this lease was $121,000 and $152,000 at March 31, 2017 and March 31, 2016, respectively.

In March 2015, the Company executed a capital lease agreement with Thermo Fisher Financial providing for $86,000 in equipment, secured by the equipment financed. The capital lease matures in March 2018 and is payable in 36 equal monthly payments. The interest rate under this capital lease is 6.5%. The balance under this lease was $30,000 and $59,000 at March 31, 2017 and 2016, respectively.

Future principal payments under the loan and capital lease agreements as of March 31, 2017 are as follows:

Year ending March 31	**(in thousands)**
2018	$ 623
2019	628
2020	647
2021	655
2022	668
Thereafter	3,918
Total principal payments	$ 7,139

Note 7 Leases

The Company's principal facility and its corporate headquarters are located at the Natural Energy Laboratory of Hawaii Authority ("NELHA") at Keahole Point in Kailua-Kona, Hawaii. The property is leased from the State of Hawaii under a 40-year commercial lease expiring in 2035. Under the terms of the existing NELHA lease, the Company could be required to remove improvements at the end of the lease term. Under generally accepted accounting principles in the United States, an entity should recognize the fair value of a liability for an asset retirement obligation in the period in which the retirement obligation is incurred, if a reasonable estimate of fair value can be made. If such an estimate cannot be made in the period the asset retirement obligation is incurred, the liability should be recognized when the fair value can be reasonably estimated. Based on communications with NELHA, management does not believe the projected cost for such removal to be material to the consolidated financial statements, or likely, given historical practices. However, conditions could change in the future. It is not possible to predict such changes or estimate any impact thereof.

The Company leases facilities, equipment and land under operating leases expiring through 2035. The land lease provides for contingent rentals in excess of minimum rental commitments based on a percentage of the Company's sales. Contingent rental payments for the years ended March 31, 2017, 2016 and 2015 were $80,000, $65,000 and $67,000, respectively.

Future minimum lease payments under non-cancelable operating leases at March 31, 2017 are as follows:

Year ending March 31	**(in thousands)**
2018	$ 615
2019	617
2020	624
2021	533
2022	531
Thereafter	4,290
Total minimum lease payments	$ 7,210

Rent expense, including contingent rent, under operating leases amounted to $605,000, $622,000 and $626,000 for the years ended March 31, 2017, 2016 and 2015, respectively.

Note 8 Other Commitments and Contingencies

The Company was previously a party to a litigation action initiated by Meridian OHC Partners, LP ("Meridian") in the United States District Court, District of Nevada. As disclosed in the Company's Form 8-K filed with the Securities and Exchange Commission on February 16, 2017, the court granted the Company's motion to dismiss the lawsuit on January 23, 2017, but granted Meridian a 20-day period to file an amended complaint. On February 13, 2017, Meridian filed an amended complaint in which the Company was not named as a defendant. As a result, the Company is no longer a party to the Meridian lawsuit. The lawsuit has continued against other defendants.

On April 6, 2017, the Company and Brent D. Bailey, the Company's former Chief Executive Officer, entered into a Settlement Agreement (the "Settlement Agreement") resolving all disputes between the Company and Mr. Bailey with respect to that certain Separation Agreement and Release of Claims, dated March 31, 2016 (the Separation Agreement"). In accordance with the terms of the Settlement Agreement, the Company paid $100,000 to Mr. Bailey in April 2017. The Company has also agreed to make twelve monthly payments to Mr. Bailey in the amount of $18,750 each, with the first payment made May 15, 2017. The Settlement Agreement now constitutes the entire agreement between the Company and Mr. Bailey and, other than the payments of up to $325,000 to be made to Mr. Bailey under the Settlement Agreement, the Company has no further obligations to provide him with any severeance payments, healthcare benefits or share grants. In connection with the Settlement Agreement, the Company increased the severance obligation payable to Mr. Bailey and reduced stockholders equity by $140,000 to reflect the increase in payments required to eliminate the Company's obligation to issue a second tranche of 77,500 shares of the Company's common stock to Mr. Bailey pursuant to the original Separation Agreement.

As of March 31, 2017, the Company has entered into purchase obligations of $406,000, including agreements to purchase goods or services that are enforceable, are legally binding and specify all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction. Purchase obligations do not include agreements that are cancelable without penalty.

Note 9 Share-Based Compensation

As of March 31, 2017, the Company had two equity-based compensation plans: the 2016 Equity Incentive Plan (the 2016 Plan) and the 2014 Independent Director Stock Option and Restricted Stock Grant Plan (the "2014 Directors Plan"). The Company has also issued stock options, which remain outstanding as of March 31, 2017, under two equity-based compensation plans which have expired according to their terms: the 2005 Stock Option Plan (the "2005 Plan") and the 2004

Independent Director Stock Option and Stock Grant Plan (the "2004 Directors Plan"). These plans allowed the Company to award stock options and shares of restricted common stock to eligible employees, certain outside consultants and independent directors. No additional awards will be issued under the 2005 Plan or the 2004 Directors Plan.

On August 25, 2016, the Company's shareholders approved the 2016 Plan as a successor to the 2005 Plan, authorizing the Board of Directors to provide incentive to the Company's officers, employees and certain independent consultants through equity based compensation in the form of stock options, restricted stock, restricted stock units, stock appreciation rights and other stock based awards (together, "Stock Awards") and performance shares and performance units (together, "Performance Awards"). Awards under the 2016 Plan are limited to the authorized amount of 1,300,000 shares, up to 600,000 of which are available for issuance in connection with Performance Awards and Stock Awards. As of March 31, 2017, there were 1,275,000 shares available for grant under the 2016 Plan.

On August 28, 2014, the Company's shareholders approved the 2014 Directors Plan authorizing the Board of Directors to provide incentive to the Company's independent directors through equity based compensation in the form of stock options and restricted stock. Awards under the 2014 Directors Plan are limited to the authorized amount of 350,000 shares. As of March 31, 2017, there were 289,124 shares available for grant under the 2014 Directors Plan.

The following table presents shares authorized, available for future grant and outstanding under each of the Company's plans:

	As of March 31, 2017		
	Authorized	**Available**	**Outstanding**
2016 Plan	1,300,000	1,275,000	25,000
2014 Directors Plan	350,000	289,124	12,000
2005 Plan	—	—	479,000
2004 Directors Plan	—	—	12,000
Total	1,650,000	1,564,124	528,000

Stock Options

All stock option grants made under the equity-based compensation plans were issued at exercise prices no less than the Company's closing stock price on the date of grant. Options under the 2005 Plan and 2014 Directors Plan were determined by the Board of Directors or the Compensation Committee of the Board of Directors in accordance with the provisions of the respective plans. The terms of each option grant include vesting, exercise, and other conditions are set forth in a Stock Option Agreement evidencing each grant. No option can have a life in excess of ten (10) years. The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes option-pricing model. The model requires various assumptions, including a risk-free interest rate, the expected term of the options, the expected stock price volatility over the expected term of the options, and the expected dividend yield. Compensation expense for employee stock options is recognized ratably over the vesting term. Compensation expense recognized for options issued under the 2005 Plan was $148,000, $581,000 and $663,000 for the years ended March 31, 2017, 2016 and 2015, respectively. Compensation expense recognized for restricted stock and stock options issued under the 2014 Directors Plan and the 2004 Directors Plan was $84,000, $84,000 and $78,000 for the three years ended March 31, 2017, 2016 and 2015, respectively. All stock-based compensation has been classified as general and administrative expense in the consolidated statement of operations.

A summary of option activity under the Company's stock plans for the years ended March 31, 2017, 2016 and 2015 is presented below:

Option Activity	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding at March 31, 2014	1,469,306	$ 4.04	7.3	$ 2,034,303
Granted	45,000	4.72		
Exercised	(60,200)	3.58		
Forfeited	(20,890)	4.28		
Outstanding at March 31, 2015	1,433,216	$ 4.08	6.4	$ 6,221,909
Granted	6,000	5.91		
Exercised	(21,800)	3.26		
Forfeited	(732,416)	3.59		
Outstanding at March 31, 2016	685,000	$ 4.65	5.7	$ 566,323
Granted	6,000	4.08		
Exercised	(18,000)	2.77		
Forfeited	(170,000)	6.44		
Outstanding at March 31, 2017	503,000	$ 4.10	4.7	$ 145,946
Exercisable at March 31, 2017	483,500	$ 4.07	4.6	$ 145,946

The aggregate intrinsic value in the table above is before applicable income taxes and represents the excess amount over the exercise price optionees would have received if all options had been exercised on the last business day of the period indicated, based on the Company's closing stock price of $3.85, $4.98, $8.42 and $5.24 at March 31, 2017, 2016, 2015 and 2014 respectively. The total intrinsic value of stock options exercised during fiscal years 2017, 2016 and 2015 were $23,000, $58,000 and $167,000, respectively.

A summary of the Company's non-vested options for the year ended March 31, 2017 is presented below:

Nonvested Options	Shares	Weighted Average Grant-Date Fair Value
Nonvested at March 31, 2016	171,250	$ 3.75
Granted	6,000	0.83
Vested	(103,250)	3.21
Forfeited	(54,500)	4.73
Nonvested at March 31, 2017	19,500	$ 2.93

The weighted average grant-date fair value of stock options granted during fiscal years 2017, 2016 and 2015 was $5,000, $7,000 and $123,000, respectively. The total grant-date fair values of stock options that vested during fiscal years 2017, 2016 and 2015 were $332,000, $651,000 and $809,000, respectively.

The following table summarizes the weighted average characteristics of outstanding stock options as of March 31, 2017:

	Outstanding Options			Exercisable Options	
Range of Exercise Prices	**Number of Shares**	**Remaining Life (Years)**	**Weighted Average Exercise Price**	**Number of Shares**	**Weighted Average Exercise Price**
$1.60 - $3.70	125,920	3.0	$ 2.74	125,920	$ 2.74
$3.71 - $4.42	197,580	4.6	$ 3.83	197,580	$ 3.83
$4.43 - $5.40	95,000	6.2	$ 5.00	75,500	$ 5.04
$5.41 - $7.08	84,500	5.6	$ 5.77	84,500	$ 5.77
Total stock options	503,000	4.7	$ 4.10	483,500	$ 4.07

The range of fair value assumptions related to options granted during the years ended March 31, 2017, 2016 and 2015 were as follows:

	2017	**2016**	**2015**
Exercise Price	$ 4.08	$ 5.91	$ 4.72
Volatility	51.13%	50.00%	64.00%
Risk Free Rate	0.60%	0.22%	1.74%
Vesting Period (in years)	0.5	0.5	3
Forfeiture Rate	0.00%	0.00%	4.51%
Expected Life (in years)	1.00	1.00	5.73
Dividend Rate	0%	0%	0%

As of March 31, 2017, total unrecognized stock-based compensation expense related to all unvested stock options was $25,000, which is expected to be expensed over a weighted average period of 0.5 years.

Restricted Stock Units ("RSUs")

RSUs are service-based awards granted to eligible employees under our 2016 Plan.

On March 31, 2017, 25,000 restricted stock units ("RSUs") were awarded to the CEO. This award is valued at $3.85 per share, the closing market price of Cyanotech common stock on the grant date, and vest over a period of three years.

On April 5, 2017, 28,074 RSUs were awarded to employees of the Company. This award is valued at $3.92 per share, the closing market price of Cyanotech common stock on the grant date, and vests over a period of three years.

The following table summarizes information related to awarded RSUs:

Nonvested Restricted Stock Units	**Shares**	**Weighted Average Grant Price**
Nonvested restricted stock units at March 31, 2016	—	$ —
Granted	25,000	$ 3.85
Vested	—	$ —
Exercised	—	$ —
Forfeited	—	$ —
Nonvested restricted stock units at March 31, 2017	25,000	$ 3.85

As of March 31, 2017, total unrecognized stock-based compensation expense related to unvested restricted stock units was $96,250.

Note 10 Common and Preferred Stock

The Company has authorized a total of sixty million shares of which fifty million shares are authorized common stock and ten million shares are authorized preferred stock. None of the preferred stock was issued or outstanding at March 31, 2017 and 2016. Under the terms of the Company's Amended and Restated Articles of Incorporation, the Board of Directors is authorized to determine or alter the rights, preferences, privileges and restrictions of the Company's authorized but unissued shares of preferred stock.

Note 11 Earnings (Loss) Per Share

Basic earnings (loss) per share is computed on the basis of the weighted average number of common shares outstanding. Diluted earnings per share is computed on the basis of the weighted average number of common shares outstanding plus the potentially dilutive effect of outstanding stock options using the treasury stock method.

Reconciliations between the numerator and the denominator of the basic and diluted loss per share computations for the years ended March 31, 2017, 2016 and 2015 are as follows:

	Net Loss (Numerator)	Shares (Denominator)	Per Share Amount
	(in thousands, except per share amounts)		
Year ended March 31, 2017:			
Basic and diluted loss per share	$ (1,215)	5,658	$ (0.21)
Year ended March 31, 2016:			
Basic and diluted loss per share	$ (4,395)	5,581	$ (0.79)
Year ended March 31, 2015:			
Basic and diluted loss per share	$ (24)	5,517	$ (0.00)

Basic and diluted per share amounts are the same in periods of a net loss, because common share equivalents are anti-dilutive when a net loss is recorded. Diluted earnings per share does not include the impact of common stock options totaling 6,000, 58,000 and 634,000 for the fiscal years ending March 31, 2017, 2016 and 2015, respectively, as the effect of their inclusion would be anti-dilutive. Restricted stock units become dilutive within the period granted and remain dilutive until the units vest and are issued as common stock. Diluted earnings per share does not include the impact of restricted stock units totaling 25,000 for the fiscal year ending March 31, 2017, as the effect of their inclusion would be anti-dilutive.

Note 12 Profit Sharing Plan and 401k Plan

The Company sponsors a profit sharing plan for all employees not covered under a separate management incentive plan. Under the profit sharing plan, a percentage determined by the Board of Directors of pre-tax profits on a quarterly basis may be allocated to non-management employees at management's discretion. The profit sharing bonus may be distributed all in cash on an after-tax basis or distributed half in cash (on an after-tax basis) and the remainder deposited in an employee's 401(k) account on a pre-tax basis. Employees may also make voluntary pre-tax contributions to their 401(k) accounts. Compensation expense under this plan was approximately $4,000, $0 and $46,000 for the fiscal years ended March 31, 2017, 2016 and 2015, respectively. Additionally, the Company makes a retirement contribution to all employees individual 401(k) accounts equal to two percent of each employee's base pay for each bi-weekly pay period on a pre-tax basis. Retirement expense under this plan was approximately $139,000, $147,000 and $113,000 for fiscal years ended March 31, 2017, 2016 and 2015, respectively.

Note 13 Product Line and Geographic Information

Net sales by product line for the years 2017, 2016 and 2015 are as follows:

	2017	2016	2015
		(in thousands)	
Net sales:			
Natural astaxanthin products			
BioAstin®	$ 19,357	$ 19,829	$ 22,087
Spirulina products			
Spirulina Pacifica®	12,685	12,011	11,722
	$ 32,042	$ 31,840	$ 33,809

Net sales by geographic region for the years 2017, 2016 and 2015 are as follows:

	2017		2016 (dollars in thousands)		2015	
Net sales(1):						
United States	$ 22,978	72%	$ 22,711	71%	$ 24,049	71%
Asia / Pacific	4,017	13%	4,130	13%	3,149	8%
Europe	3,652	11%	2,990	9%	4,302	13%
Other	1,395	4%	2,009	7%	2,309	8%
	$ 32,042	100%	$ 31,840	100%	$ 33,809	100%

(1) Net sales are attributed to countries based on location of customer.

Note 14 Income Taxes

Income tax expense for the years ended March 31, 2017, 2016 and 2015 consisted of:

	2017	2016 (in thousands)	2015
Current:			
Federal	$ (2)	$ (1)	$ (12)
State	(3)	23	(78)
Total current benefit (expense)	(5)	22	(90)
Deferred:			
Federal	—	(3,027)	(170)
State	—	(323)	7
Total deferred expense	—	(3,350)	(163)
Income tax expense	$ (5)	$ (3,328)	$ (253)

The following table reconciles the amount of income taxes computed at the federal statutory rate of 34%, for all periods presented, to the amount reflected in the Company's consolidated statements of operations for the years ended March 31, 2017, 2016 and 2015:

	2017	2016 (in thousands)	2015
Tax provision at federal statutory income tax rate	$ 411	$ 363	$ (78)
Stock based compensation	(281)	(128)	(108)
Increase in valuation allowance	(158)	(3,564)	—
State income taxes benefit (expense), net of federal income tax effect	49	25	(49)
State rate adjustment	(1)	1	(4)
Other, net	(25)	(25)	(14)
Income tax expense	$ (5)	$ (3,328)	$ (253)

The tax effects of temporary differences related to various assets, liabilities and carry forwards that give rise to deferred tax assets and deferred tax liabilities as of March 31, 2017 and 2016 are as follows:

	2017	2016
	(in thousands)	
Deferred tax assets:		
Net operating loss carry forwards	$ 4,325	$ 3,862
Inventory	405	3
Compensation accrual	187	535
Tax credit carry forwards	147	147
Other	40	72
Gross deferred tax assets	5,104	4,619
Less valuation allowance	(3,722)	(3,564)
Net deferred tax assets	1,382	1,055
Deferred tax liability- Depreciation and amortization	(1,382)	(1,055)
Net deferred tax assets	$ —	$ —

In assessing the valuation allowance for deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. Ultimately, the realization of deferred tax assets will depend on the existence future taxable income during the periods. In making this assessment, management considers past operating results, the scheduled reversal of deferred tax liabilities, estimates of future taxable income and tax planning strategies.

In fiscal 2016, the Company recorded a $3,564,000 valuation allowance against deferred tax assets. The Company concluded that a valuation allowance was appropriate in light of the significant negative evidence, which was objective and verifiable, primarily the cumulative losses in recent years. While the Company's long-term financial outlook remains positive, the Company concluded that its ability to rely on its long-term outlook as to future taxable income was limited due to the relative weight of the negative evidence from its recent cumulative losses. The Company's conclusion regarding the need for a valuation allowance against its deferred tax assets could change in the future based on improvements in operating performance, which may result in the full or partial reversal of the valuation allowance.

At March 31, 2017, the Company has net operating loss carry forwards and tax credit carry forwards available to offset future federal income tax as follows (in thousands):

Expires March 31,	Net Operating Losses	Research and Experimentation Tax Credits
2020	$ —	$ 8
2021	—	2
2022	2,839	—
2023	1,863	1
2026	159	—
2027	2,665	1
2028	1,612	16
2031	389	—
2032	44	—
2033	76	—
2034	392	—
2035	18	—
2037	1,705	—
	$ 11,762	$ 28

In addition, at March 31, 2017, the Company has alternative minimum tax credit carry forwards of approximately $120,000 available to reduce future federal regular income taxes over an indefinite period.

At March 31, 2017, the Company has state tax net operating loss carry forwards available to offset future California state taxable income of $1,040,000. These carry forwards expire March 31, 2037. At March 31, 2017, the Company has state tax net operating loss carry forwards available to offset future Hawaii state taxable income of $6,289,000. These carry forwards expire March 31, 2030 through 2037.

The following represents the open tax years and jurisdictions that the Company used in its evaluation of tax positions:

Open tax years ending March 31,	Jurisdiction
2014 - 2017	U.S. Federal
2014 - 2017	State of Hawaii
2013 - 2017	State of California

Note 15 Selected Quarterly Financial Data (Unaudited)

	First Quarter(1)	Second Quarter(1)	Third Quarter(1)	Fourth Quarter (1)(2)	Year
		(in thousands, except per share data)			
2017					
Net sales	$ 7,322	$ 9,862	$ 7,605	$ 7,253	$ 32,042
Gross profit	2,821	3,885	2,857	2,661	12,224
Net income (loss)	(691)	99	(349)	(274)	(1,215)
Net income (loss) per share					
Basic and diluted	(0.12)	0.02	(0.06)	(0.05)	(0.21)
2016					
Net sales	$ 7,594	$ 8,516	$ 7,534	$ 8,196	$ 31,840
Gross profit	2,924	3,100	3,084	2,758	11,866
Net income (loss)	(105)	14	(250)	(4,054)	(4,395)
Net income (loss) per share					
Basic and diluted	(0.02)	0.00	(0.04)	(0.73)	(0.79)

(1) The first, second, third and fourth quarters of 2017 include abnormal costs of $28,000, $73,000, $148,000 and $5,000, respectively. The first, second and third quarters of 2016 include abnormal costs of $214,000, $308,000 and $21,000, respectively.

(2) Net loss and net loss per share for the fourth quarter of fiscal 2016 includes the provision of a valuation allowance of $3.6 million against our deferred tax assets.

Item 9A. Controls and Procedures

Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our chief executive officer ("CEO") and chief financial officer ("CFO"), we have evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15(d)-15(e) of the Exchange Act as of the end of the period covered by this Report. Based on that evaluation, our CEO and CFO have concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in reports we file or submit under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (2) accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosures.

Management's Report on Internal Control over Financial Reporting.

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our management evaluated the effectiveness of our internal control over financial reporting as of March 31, 2017. This assessment was based on the framework in 1992 Internal Control—Integrated Framework, issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on our assessment, using those criteria, management concluded that our internal control over financial reporting was effective as of March 31, 2017.

Changes in Internal Control over Financial Reporting.

During Fiscal 2017, the Company implemented additional training programs for the personnel responsible for reviewing customer purchase orders in order to clarify and confirm transfer of title and risk of loss when customer purchase orders terms are vague or missing, including appropriate review and approval procedures as well as additional quarter end closing and review procedures to confirm delivery dates for all FOB Destination shipments.

There have not been any other changes in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act) during the fourth fiscal quarter that our certifying officers concluded materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Limitations on the Effectiveness of Controls.

Our management, including our Chief Executive Officer and Chief Financial Officer, do not expect that our disclosure controls and procedures will prevent all errors and all fraud. A control system no matter how well designed and implemented, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues within a company are detected. The inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistakes. Controls can also be circumvented by the individual acts of some persons, or by collusion of two or more people. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Item 9B. Other Information

Not applicable

PART III

Item 10. Directors, Executive Officers of the Registrant and Corporate Governance

Information with respect to Directors may be found under captions “Proposal One: Election of Directors,” “Board Meetings and Committees,” “Director Compensation,” “Security Ownership of Certain Beneficial Owners and Management: and “Compliance with Section 16(a) of the Exchange Act” contained in Cyanotech’s definitive 2017 Proxy Statement. Information on Executive Officers may be found under the caption “Executive Officers” contained in Cyanotech’s definitive 2017 Proxy Statement.

We have adopted the Cyanotech Code of Ethics for our officers and employees. We have also adopted the Board of Directors Code of Conduct. Both Codes are publicly available on our website at *www.cyanotech.com*. If we make any substantive amendments to or grant any waiver from such Codes relating to our Chief Executive Officer, Chief Financial Officer or Controller, we will disclose the nature of such amendment in a report on Form 8-K and amend the website disclosure.

Item 11. Executive Compensation

The information required by this Item is incorporated herein by reference from the sections captioned “Executive Compensation and Other Information,” “Equity Compensation Plan Information” and “Option Grants in Fiscal Year 2017,” contained in Cyanotech’s definitive 2017 Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The security ownership information required by this Item is incorporated herein by reference from the sections captioned “Equity Compensation Plan Information” and “Security Ownership of Certain Beneficial Owners and Management” contained in Cyanotech’s definitive 2017 Proxy Statement.

Item 13. Certain Relationships and Related Transactions, and Director Independence

The information required by this Item, if any, is incorporated herein by reference from the sections captioned “Related Party Transactions” contained in Cyanotech’s definitive 2017 Proxy Statement.

Item 14. Principal Accountant Fees and Services

Information concerning principal accountant fees and services appears under the heading “Independent Registered Public Accounting Firm’s Fees” in Cyanotech’s definitive 2017 Proxy Statement.

PART IV

Item 15. Exhibits and Financial Statement Schedule

(a) Financial Statements and Schedule

(1) The following Financial Statements of Cyanotech Corporation and subsidiary and the Report of Independent Registered Public Accounting Firm are included in Item 8 of this report:

(2) The following financial statement schedule is included in this report on the pages indicated below:

Financial statement schedules not listed above have been omitted since they are either not required, not applicable or the information is included in the consolidated financial statements or notes thereto.

(b) Exhibit Listing

Exhibit Number	Document Description
3.1	Restated Articles of Incorporation (Incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q, filed November 9, 2012, File No. 0-14602).
3.2	Amended and Restated Bylaws (Incorporated by reference to Exhibit 3.2 to the Company's Report on Form 8-K filed January 13, 2010, File No. 0-14602)
4.1	Specimen Common Stock (Incorporated by reference to Exhibit 4.1 to the Company's Annual Report on Form 10-K for the year ended March 31, 2007, File No. 0-14602)
10.1	Sub-Lease Agreement between the Company and Natural Energy Laboratory of Hawaii Authority dated December 29, 1995 (Incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-QSB for the quarter ended December 31, 1995, File No. 0-14602)
10.2	Supplemental Agreement effective February 1, 2012 to amend the Sub-Lease Agreement described in Exhibit 10.1 herein, (Incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated March 9, 2012, File No. 0-14602).
10.3	2004 Independent Director Stock Option and Restricted Stock Grant Plan, amended and restated November 8, 2011 (Incorporated by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q dated November 14, 2011 for the quarter ended September 30, 2011, File No. 0-14602).
10.4	2005 Stock Option Plan, amended August 29, 2011 (Incorporated by reference to Exhibit 10.2 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2011, File No. 0-14602).
10.5	Settlement Agreement, by and between Brent D. Bailey and the Company, dated April 6, 2017 (Incorporated by reference as Exhibit 10.1 to the Company's Report on Form 8-K filed on April 11, 2017, File No. 0-14602)
10.6	Term Loan Agreement between Pacific Rim Bank ("Pacific Rim") and both the Company and Nutrex Hawaii, Inc. ("Nutrex"); Promissory Notes in favor of Pacific Rim in the amounts of $2,250,000 and $3,250,000, issued by the Company and Nutrex, dated September 7, 2012; Mortgage, Security Agreement and Financing Statement between the Company and Pacific Rim; Assignment of Lessor's Interest in Leases and Rents between the Company and Pacific Rim; Security Agreement and UCC Financing Statement between the Company and Pacific Rim; United States Department of Agriculture Rural Development ("USDA") Conditional Commitments; Hazardous Substances Certificate and Indemnity Agreement; Assignment of Construction Contract between the Company and No'Eau Construction LLC; Sublessor's Consent to Mortgage of Sublease K-4; Estoppel Certificate and Subordination Agreement, given by the Natural Energy Laboratory of Hawaii Authority, State of Hawaii, as Sublessor; Security Agreement and UCC Financing Statement between Nutrex and Pacific Rim. (Incorporated by reference as Exhibit 4.1 to the Company's Report on Form 10-Q filed on November 9, 2012, File No. 0-14602)
10.7	Term Loan Agreement between First Foundation Bank ("First Foundation") and both the Company and Nutrex; Promissory Note in favor of First Foundation in the amount of $2,500,000, issued by the Company and Nutrex, dated July 30, 2015; Mortgage, Security Agreement and Financing Statement between the Company and First Foundation; Assignment of Lessor's Interest in Leases and Rents between the Company and First Foundation; Security Agreement and UCC Financing Statement between the Company and First Foundation; Security Agreement and UCC Financing Statement between Nutrex and First Foundation; USDA Conditional Commitments; Hazardous Substances Certificate and Indemnity Agreement; Sublessor's Consent to Mortgage of Sublease K-4; Estoppel Certificate and Subordination Agreement. (Incorporated by reference as Exhibit 4.1through 4.9 to the Company's Report on Form 10-Q filed on November 12, 2015, File No. 0-14602)
10.8	2014 Independent Director Stock Option and Restricted Stock Grant Plan (Incorporated by reference to the Company's Definitive Proxy Statement filed July 18, 2014, File No. 0-14602)
10.9	2016 Equity Incentive Plan (Incorporated by reference to the Company's Definitive Proxy Statement filed July 15, 2016, File No. 0-14602).
10.10	Revolving Credit Agreement, by and between First Foundation Bank and the Company, dated June 3, 2016. (Incorporated by reference to the Company's Current Report on Form 8-K filed August 30, 2016, File No. 0-14602).
21.1	Subsidiaries of the Company (Incorporated by reference to Exhibit 21.1 to the Company's Annual Report on Form 10-K for the year ended March 31, 2012, File No. 0-14602)
23.1*	Consent of Independent Registered Public Accounting Firm signed June 22, 2017—Grant Thornton LLP
31.1*	Certifications of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 signed as of June 22, 2017.
31.2*	Certifications of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 signed as of June 22, 2017.
32.1*	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 signed as of June 22, 2017.
99.1*	Press Release dated June 22, 2017
101	The following financial information from our Annual Report on Form 10-K for fiscal year ended March 31, 2017, filed with the SEC on June 22, 2017, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets at March 31, 2017 and 2016, (ii) the Consolidated Statements of Operations for the years ended March 31, 2017, 2016 and 2015, (iii) the Consolidated Statements of Stockholders' Equity for the years ended March 31, 2017, 2016 and 2015, (iv) the Consolidated Statements of Cash Flows for the years ended March 31, 2017 and 2016, and (v) Notes to Consolidated Financial Statements.
*	Included herewith. Other exhibits were filed as shown above.

Schedule II

Cyanotech Corporation and Subsidiary
Valuation and Qualifying Accounts

Years Ended March 31, 2017, 2016 and 2015
(in thousands)

Description	Balance at Beginning of Year	Additions: Charged to Costs and Expense	Additions: Charged to Other Accounts	Deductions	Balance at End of Year
Allowance for Doubtful Accounts:					
2017	$ 136	—	—	87	$ 49
2016	$ 6	130	—	—	$ 136
2015	6	—	—	—	6

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, on the 22th day of June, 2017.

CYANOTECH CORPORATION

By: /s/ Gerald R. Cysewski
Gerald R. Cysewski
President and Chief Executive Officer; Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signatures	Title	Date
/s/ Gerald R. Cysewski, PH.D. Gerald R. Cysewski	President and Chief Executive Officer; Director	June 22, 2017
/s/ Jole Deal Jole Deal	Chief Financial Officer, Vice President—Finance and Administration, Secretary and Treasurer (Principal Financial and Accounting Officer)	June 22, 2017
/s/ Michael A. Davis Michael A. Davis	Chairman of the Board	June 22, 2017
/s/ Walter B. Menzel Walter B. Menzel	Director	June 22, 2017
/s/ David M. Mulder David M. Mulder	Director	June 22, 2017
/s/ David L. Vied David L. Vied	Director	June 22, 2017
/s/ Nancy E. Katz Nancy Katz	Director	June 22, 2017

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*	Included herewith. Other exhibits were filed as shown above.

Forward-Looking Information

Certain statements herein set forth management's intentions, plans, beliefs, expectations or predictions of the future based on current facts and analyses.

Actual results may differ materially due to a variety of factors including reduced product demand, price competition, government action and weather conditions. Additional information on factors that may affect the Company and cause actual results to differ from current expectations can be found in Cyanotech's filings with the Securities and Exchange Commission.

Market for Common Equity and Related Stockholder Matters

The Company's common stock is listed and traded on the NASDAQ Capital Market under the symbol "CYAN". The closing price of our common stock was $3.38 as of June 20, 2017. The approximate number of holders of record of our common stock was 400.

The high and low selling prices as reported by NASDAQ were as follows:

Fiscal 2017

Common stock price per share:

Q End	June 30	Sept 30	Dec 31	March 31
High	$5.65	$5.36	$4.30	$4.70
Low	$4.76	$3.43	$3.60	$3.70

Fiscal 2016

Common stock price per share:

Q End	June 30	Sept 30	Dec 31	March 31
High	$10.25	$9.63	$6.08	$5.41
Low	$8.75	$5.73	$5.10	$3.89

The Company is prohibited from declaring any common stock dividends without the prior written consent of a lender per the conditions of an existing term loan agreement with such lender. The Company has never declared or paid cash dividends on its common stock. We currently intend to retain all of our earnings for use in the business and do not anticipate paying any cash dividends on common stock in the foreseeable future.

Cyanotech Corporation's annual report to the Securities and Exchange Commission on Form 10-K, including financial statements and financial statement schedules, for the most recent fiscal year accompany these proxy materials. Additional copies may be obtained by downloading from the Company's website (www.cyanotech.com), including Exhibits to the Form 10-K. Paper copies of the four (4) Exhibits identified in the Form 10-K, Item 15 (b) with an asterisk (*) will be furnished upon request from persons making a good faith representation that they were a beneficial owner of the Company's securities on June 26, 2017, and upon payment to the Company of its reasonable expenses for furnishing such copies which will be the lesser of $60 per set or $0.68 per page for those requesting less than a full set. Such written requests should be addressed to:

Jolé E. Deal
Cyanotech Corporation
73-860 Makako Bay Drive, Kailua-Kona, HI 96740.

OFFICERS

Gerald R. Cysewski, Ph.D.
President and CEO,
Chief Scientific Officer and Founder

Jolé E. Deal
Chief Financial Officer, Vice President of Finance and Administration, Secretary and Treasurer

Gerry Watts
Chief Operations Officer

Glenn D. Jensen
Vice President of Manufacturing and Infrastructure

Jennifer M. Johansen
Vice President of Quality and Regulatory Affairs

DIRECTORS

Michael A. Davis [3]
Principal
Ebb and Flow Ventures

Nancy E. Katz [1, 3]
CEO
NKI Consulting

David M. Mulder [1]
EVP and Chief Financial Officer,
Reiter Affiliated Companies

Walter B. Menzel [1, 2]
President
WM Group

David L. Vied [2, 3]
Global Sector Leader, Medical Devices & Diagnostics, Korn Ferry

Gerald R. Cysewski, Ph.D.
President and CEO,
Chief Scientific Officer,
Cyanotech Corporation

1 Member of Audit Committee
2 Member of Compensation Committee
3 Member of the Nominating and Corporate Governance Committee

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Jolé E. Deal
Chief Financial Officer
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TRANSFER AGENT AND REGISTRAR

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ADDITIONAL INFORMATION

Copies of Cyanotech's news releases and financial statements are available at our website: http://www.cyanotech.com

NOTICE OF ANNUAL MEETING

The 2017 Annual Meeting of Stockholders will be held on Thursday, August 24, 2017, at 3:00 P.M. Hawaii Standard Time at the Waikoloa Beach Marriott, 69-275 Waikoloa Beach Dr, Waikoloa, HI, USA, 96738 or such other date and time as may be properly determined and communicated to eligible meeting participants.

CORPORATE HEADQUARTERS

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WHOLLY-OWNED SUBSIDIARIES

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