

Arrayit Corp
Form 10-Q
November 15, 2010

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

Form 10-Q

Mark One)

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

For the Quarterly Period Ended September 30, 2010

Or

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

For the Transition Period From to

Commission File No. 001-16381

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

Nevada 76-0600966
(State of other jurisdiction of (I.R.S. Employer Identification No.)
incorporation)

524 East Weddell Drive Sunnyvale, CA 94089
(Address of Principal Executive Office) (Zip Code)

Registrant's telephone number, including area code: (408) 744-1331

Securities registered pursuant to Section 12 (b) of the Act: NONE

Securities registered pursuant to Section 12 (g) of the Act: Common Stock \$0.001 par value

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 periods that the registrant was

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required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input checked="" type="checkbox"/>
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(Do not check if a smaller reporting company)

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

There were 24,919,056 shares of the Registrant's common stock outstanding at November 15, 2010.

Form 10-Q
For the Quarterly Period Ended September 30, 2010

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This report contains trademarks and trade names that are the property of Arrayit Corporation and its subsidiaries, and of other companies, as indicated.

FORWARD-LOOKING STATEMENTS

Portions of this Form 10-Q, including disclosure under “Management’s Discussion and Analysis of Financial Position and Results of Operations,” contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), Section 21E of the Securities and Exchange Act of 1934, as amended (the “Exchange Act”), and the Private Securities Litigation Reform Act of 1995, as amended. These forward-looking statements are subject to risks and uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from the results, performance or achievements expressed or implied by the forward-looking statements. You should not unduly rely on these statements. Forward-looking statements involve assumptions and describe our plans, strategies, and expectations. You can generally identify a forward-looking statement by words such as may, will, should, expect, anticipate, estimate, believe, intend, contemplate or project. Factors, risks, and uncertainties that could cause actual results to differ materially from those in the forward-looking statements include, among others,

- our ability to raise capital,
- our ability obtain and retain customers,

- our ability to provide our products and services at competitive rates,
- our ability to execute our business strategy in a very competitive environment,

- our degree of financial leverage,
- risks associated with our acquiring and integrating companies into our own,

- risks related to market acceptance and demand for our services,
- the impact of competitive services,

- other risks referenced from time to time in our SEC filings.

With respect to any forward-looking statement that includes a statement of its underlying assumptions or bases, we caution that, while we believe such assumptions or bases to be reasonable and have formed them in good faith, assumed facts or bases almost always vary from actual results, and the differences between assumed facts or bases and actual results can be material depending on the circumstances. When, in any forward-looking statement, we or our management express an expectation or belief as to future results, that expectation or belief is expressed in good faith and is believed to have a reasonable basis, but there can be no assurance that the stated expectation or belief will result or be achieved or accomplished. All subsequent written and oral forward-looking statements attributable to us, or anyone acting on our behalf, are expressly qualified in their entirety by the cautionary statements. We do not undertake any obligations to publicly release any revisions to any forward-looking statements to reflect events or circumstances after the date of this report or to reflect unanticipated events that may occur.

PART I – FINANCIAL INFORMATION

ITEM 1.

ARRAYIT CORPORATION
CONSOLIDATED BALANCE SHEETS

	September 30, 2010	December 31, 2009
ASSETS		
Current Assets		
Cash	\$-	\$-
Accounts receivable, net of allowance for doubtful accounts of \$100,000	92,221	71,944
Inventory	237,871	241,436
Prepaid expenses	-	12,500
Total current assets	330,092	325,880
Property and equipment, net	47,763	68,688
Restricted cash	-	100,293
Deposits	18,924	18,924
Total current assets	\$396,779	\$513,785
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable and accrued liabilities	\$5,959,204	\$5,320,239
Bank overdraft	10,460	31,076
Due to related parties	591,333	459,116
Customer deposits	101,827	65,687
Notes payables, current portion including related parties	1,088,573	852,931
Total current liabilities	7,751,397	6,729,049
Notes payable, long term	100,367	180,656
Total liabilities	7,851,764	6,909,705
Commitments and contingencies	-	-
Stockholders' deficit		
Preferred stock, 20,000,000 authorized		
Preferred stock, Series 'A' 22,034 and 25,620 shares issued and outstanding	22	25
Preferred stock, Series 'C' 92,201 and 103,143 shares issued and outstanding	92	103
Common stock, \$0.001par value, voting, 480,000,000 shares authorized, 24,919,056 and 19,085,859 issued and outstanding	24,729	18,896
Additional paid-in capital	16,145,446	14,478,455
Accumulated deficit	(23,711,938)	(21,097,741)
Total Arrayit Corp's Stockholders' Equity (Deficit)	(7,541,649)	(6,600,262)
Non-controlling Interest		
Royalty interests	285,000	285,000
Less: Subscriptions receivable	(13,750)	(13,750)
Interest in subsidiaries earnings	(184,586)	(66,908)
Total Non-controlling interests	86,664	204,342
Total stockholders' deficit	(7,454,985)	(6,395,920)
Total liabilities and stockholders' deficit	\$396,779	\$513,785

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

ARRAYIT CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months ended September 30		Nine Months ended September 30	
	2010	2009	2010	2009
Total revenues	\$688,779	\$1,107,857	\$2,145,747	\$3,293,685
Cost of sales	263,942	730,307	1,101,129	2,332,512
Gross margin	424,837	377,550	1,044,618	961,173
Selling, general and administrative	582,954	342,331	2,990,442	1,030,519
Profit (loss) from operations	(158,117)	35,219	(1,945,824)	(69,346)
Research and development	(142,720)		(311,819)	
Gain (loss) on derivative liability	-	2,533,652	-	16,621,964
Gain (loss) on extinguishment of debt	-		-	(19,021,116)
Legal expense	(106,036)	(124,731)	(232,884)	(160,172)
Interest (expense)	(137,153)	(39,430)	(241,348)	(228,240)
Net loss	(544,026)	2,404,710	(2,731,875)	(2,856,910)
Less: net loss attributable to the noncontrolling interest	(69,920)	-	(117,678)	-
Net loss attributable to common shareholders	(474,106)	2,404,710	(2,614,197)	(2,856,910)
Profit (loss) per share - basic	\$(0.02)	\$0.70	\$(0.11)	\$(1.09)
Basic weighted average number of common shares	24,876,930	3,459,622	23,197,665	2,618,349
Profit (loss) per share - diluted	\$(0.02)	\$0.05	\$(0.11)	\$(1.09)
Diluted weighted average number of common shares	24,876,930	49,360,684	23,197,665	2,618,349

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

ARRAYIT CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the Nine Months Ended	
	2010	2009
Cash flows from operating activities:		
Net income	\$(2,731,875)	\$(2,856,910)
Adjustments to reconcile net income (loss) to net cash used for operating activities:		
Depreciation	22,957	10,500
Amortization	102,674	-
Loss on derivative liability	-	(16,621,964)
Loss on extinguishment of debt	-	19,021,116
Provision for bad debt		20,000
Stock paid for services	1,538,936	-
Changes in operating assets and liabilities		
Accounts receivable	(20,277)	(18,798)
Inventory	3,565	204,733
Prepays	12,500	-
Restricted cash	100,293	495
Accounts payable and accrued liabilities	638,965	178,874
Bank overdraft	(20,616)	22,079
Due to related parties	132,217	82,266
Customer deposits	36,140	(33,543)
Net cash provided by (used in) for operating activities	(184,521)	8,848
Cash flows from investing activities:		
Cash paid for purchase of fixed assets	(2,032)	(1,965)
Net cash provided by (used in) for investing activities:	(2,032)	(1,965)
Cash flows from financing activities:		
Proceeds from loans	147,326	180,124
Repayment of notes payable	(94,647)	(187,007)
Proceeds from option exercise	51,200	-
Proceeds from issuance of warrants	82,674	-
Net cash provided by (Used in) financing activities	186,553	(6,883)
Net increase in cash	-	-
Cash, beginning of period	-	-

Cash, end of period	\$-	\$-
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Supplemental cash flow information:

Cash paid for interest	\$75,714	\$84,417
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Cash paid for income taxes	\$-	\$-
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Shares issued for services	\$1,395,505	\$-
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Warrants issued for services	\$143,431	\$-
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The accompanying notes are an integral part of these consolidated financial statements

ARRAYIT CORPORATION
NOTES TO CONSOLIDATED UNAUDITED STATEMENTS
SEPTEMBER 30, 2010

NOTE 1 – ORGANIZATION AND BUSINESS OPERATIONS

Arrayit Corporation (the “Company” or “Arrayit”) is a Nevada Corporation, that entered into the life sciences in 1996. Arrayit is a leading edge developer, manufacturer and marketer of next-generation life science tools and integrated systems for the large scale analysis of genetic variation, biological function and diagnostics. Using Arrayit’s proprietary technologies, the Company provides a comprehensive line of products and services that currently serve the sequencing, genotyping, gene expression and protein analysis markets, and the Company expects to enter the market for molecular diagnostics.

Arrayit has earned respect as a leader in the health care and life sciences industries with its proven expertise in three key areas: the development and support of microarray tools and components, custom printing and analysis of microarrays for research, and the identification and development of diagnostic microarrays and tools for early detection of treatable disease states. As a result, Arrayit has provided tools and services to thousands of the leading genomic research centers, pharmaceutical companies, academic institutions, clinical research organizations, government agencies and biotechnology companies worldwide.

The Company’s patented tools and trade secrets provide researchers around the world with the performance, throughput, cost effectiveness and flexibility necessary to perform the billions of genetic tests needed to extract valuable medical information. The Company believes this information will enable researchers to correlate genetic variation and biological function, which will enhance drug discovery, drug development and clinical research, allowing diseases to be detected earlier and permitting better choices of drugs for individual patients.

Effective Thursday, March 19, 2009, the final steps of the business combination with Integrated Media Holdings, Inc. were completed and the Company’s common stock began trading on the OTC Bulletin Boards as “ARYC”. In addition, the Company changed its name to “Arrayit Corporation”, was reincorporated to Nevada from Delaware, and reverse-split its common stock and Series A Convertible Preferred stock in the ratio of one for thirty shares. The reverse split was only applicable to the Company’s Class “A” Preferred shares and its Common Shares. The Class “C” Preferred Shares were not affected by the reverse split. The reverse split had no effect upon the convertible debt “Oral Agreements” which fixed the amount of shares to be issued at 12,478,357 both pre and post split. As the March 19, 2009, Directors Resolution did not change the authorized share capital of the Company, the authorized number of Common Shares was reduced from 100,000,000 to 3,333,333. The Directors approved the reverse split to create a more orderly market for the trading of its Common Shares on the OTC BB.

On August 31, 2009, a majority of the stockholders provided written consent in lieu of a meeting to approve an increase in the authorized common shares of the Company from 3,333,333 to 480,000,000 and an increase in the authorized preferred shares of the Company from 166,667 to 20,000,000. A Certificate of Amendment to the Restated Certificate of Incorporation of the Company was filed on December 18, 2009. The forgoing was published in form DEF 14-C on November 18, 2009.

The effects of the Reverse Stock Split have been reflected retroactively in the accompanying consolidated financial statements and notes thereto for all periods presented.

Arrayit has a December 31 year end.

Arrayit's principal office is in Sunnyvale, California. Arrayit presently has ten employees.

Interim financial statements

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X, and, therefore, do not include all information and footnotes necessary for a complete presentation of financial position, results of operations, cash flows, and stockholders' equity in conformity with accounting principles generally accepted in the United States of America. In the opinion of management, all adjustments considered necessary for a fair presentation of the results of operations and financial position have been included and all such adjustments are of a normal recurring nature.

These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto contained in Arrayit's Annual Report filed with the SEC on Form 10-K. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the consolidated financial statements, which would substantially duplicate the disclosure contained in the audited financial statements for fiscal year 2009 as reported in Form 10-K, have been omitted.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND GOING CONCERN

Basis of Presentation

The accompanying Consolidated Financial Statements include the following majority-owned subsidiaries for all or a portion of the periods indicated, each of which has been consolidated since the date the Company acquired majority-voting control (collectively, the “Consolidated Subsidiaries”):

Subsidiary	Date of Incorporation	Business of Entity	Ownership
Arrayit Diagnostics, Inc.	June 2, 2009	Develops medical tests and through its partially owned subsidiaries markets these tests to the medical community. incorporating the technology and equipment developed by Arrayit Corporation	80% owned by Arrayit Corporation
Arrayit Diagnostics (Ovarian), Inc.	June 16, 2009	Markets a test for Ovarian Cancer incorporating the technology and equipment developed by Arrayit Corporation	80% owned by Arrayit Diagnostics, Inc.
Arrayit Diagnostics (Parkinson), Inc.	October 15, 2009	Markets a test for Parkinson’s Disease incorporating the technology and equipment developed by Arrayit Corporation	80% owned by Arrayit Diagnostics, Inc.

Summary of Significant Accounting Policies

Financial Reporting:

The Company prepares its financial statements in conformity with accounting principles generally accepted in the United States of America. Revenues and expenses are reported on the accrual basis, which means that income is recognized as it is earned and expenses are recognized as they are incurred.

Management further acknowledges that it is solely responsible for adopting sound accounting practices, establishing and maintaining a system of internal accounting control and preventing and detecting fraud. The Company's system of internal accounting control is designed to assure, among other items, that 1) recorded transactions are valid; 2) valid transactions are recorded; and 3) transactions are recorded in the proper period in a timely manner to produce financial statements which present fairly the financial condition, results of operations and cash flows of the Company for the respective periods being presented.

Use of Estimates

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

Cash and Cash Equivalents

Cash includes all cash and highly liquid investments with original maturities of three months or less. The Company maintains cash in bank deposit accounts which, at times, exceed federally insured limits. The Company has not experienced any losses on these accounts.

Investments in certificates of deposit with our bankers that contain prohibition on their redemption are treated as non-current assets and included in restricted cash.

Property and Equipment

Property and equipment are recorded at cost less accumulated depreciation. Depreciation and amortization on property and equipment are determined using the straight-line method over the three to five year estimated useful lives of the assets.

Impairment of Long-Lived Assets

Arrayit reviews its long-lived assets for impairment when events or changes in circumstances indicate that the book value of an asset may not be recoverable. Arrayit evaluates, at each balance sheet date, whether events and circumstances have occurred which indicate possible impairment. The Company uses an estimate of future undiscounted net cash flows of the related asset or group of assets over the estimated remaining life in measuring whether the assets are recoverable. If it is determined that an impairment loss has occurred based on expected cash flows, such loss is recognized in the statement of operations.

Inventory

Inventories are stated at the lower of cost or market, cost determined on the basis of FIFO.

Revenue recognition:

Overview

The Company recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed or determinable, and collectability is reasonably assured. In instances where final acceptance of the product or system is required, revenue is deferred until all the acceptance criteria have been met.

Product Sales

Product sales include sales of microarrays, reagents and related instrumentation. Microarray, reagent and instrumentation revenues are recognized when earned, which is generally upon shipment and transfer of title to the customer and fulfillment of any significant post-delivery obligations. Accruals are provided for anticipated warranty expenses at the time the associated revenue is recognized.

Services

Services revenue is comprised of equipment service revenue; revenue from custom microarray design fees; and scientific services revenue, which includes associated consumables.

Diagnostic Revenue

Revenue from medical testing and scientific services is recognized upon shipment of the reported results.

Other Income

The Company recognizes interest income as earned.

Shipping and Handling Costs

Shipping and handling costs billed to customers are recorded as revenue. Shipping and handling costs paid to vendors are recorded as cost of sales.

Fair Value of Financial Instruments

The Company follows accounting guidance relating to fair value measurements. This guidance establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels as follows:

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access as of the measurement date.

Level 2 – inputs other than quoted prices included within Level 1 that are directly observable for the asset or liability or indirectly observable through corroboration with observable market data.

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Level 3 – unobservable inputs for the asset or liability only used when there is little, if any, market activity for the asset or liability at the measurement date.

The asset or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the unobservable inputs.

The fair value of the Company's notes payable and derivative liability approximated stated value. The notes payable fair value was based on Level 2 inputs and the derivative liability fair value based on Level 3 inputs. See notes 10 and 11.

Allowance for Doubtful Accounts

The Company records an allowance for estimated losses on customer accounts. The allowance is increased by a provision for bad debts, which is charged to expense, and reduced by charge-offs, net of recoveries.

Patent Costs

Costs incurred with registering and defending patent technology are charged to expense as incurred.

Derivative Instruments

Derivatives were recorded on the balance sheet at fair value. These derivatives, including embedded derivatives, were separately valued and accounted for on our balance sheet.

Accounting guidance related to Accounting for derivative financial instruments indexed to and potentially settled in, a company's own stock, requires freestanding contracts that are settled in a company's own stock, including warrants to purchase common stock, to be designated as an equity instrument, asset or a liability. Under these provisions, a contract designated as an asset or a liability must be carried at fair value on a company's balance sheet, with any changes in fair value recorded in the company's results of operations. A contract designated as an equity instrument must be included within equity, and no fair value adjustments are required.

Following this guidance, we determined the conversion feature of our "SOV Cap" notes, Senior Secured Convertible Notes ("SSCN") and the warrants associated with the SSCN notes should be treated as separate derivative liabilities on our balance sheet under current liabilities. Unrealized changes in the value of these derivatives were recorded in the consolidated statement of operations as a gain or loss on derivative liabilities. Fair values of the derivative liability associated with the conversion features and warrants were determined using a Black-Scholes Model.

Income Taxes

Prior to February 21, 2008, the financial statements of TeleChem did not include a provision for Income Taxes because the taxable income of TeleChem was included in the Income Tax Returns of the Stockholders under the Internal Revenue Service "S" Corporation elections.

Upon completion of the February 21, 2008 transaction with IMHI as more fully described in Note 1, TeleChem ceased to be treated as an "S" Corporation for Income Tax purposes. Effective February 21, 2008, Arrayit Corporation became a Nevada "C" Corporation.

Deferred taxes are computed using the asset and liability method. Under the asset and liability method, deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred tax assets are not recognized unless it is more likely than not that the asset will be realized in future years.

Accounting for Uncertainty in Income Taxes

The Financial Accounting Standards Board has issued guidance on Accounting for Uncertainty in Income Taxes, FASB ASC 740, Income Taxes which prescribes a recognition threshold and a measurement attribute for the financial statement recognition and measurement of tax positions taken or expected to be taken in a tax return. For those benefits to be recognized, a tax position must be more likely than not to be sustained upon examination by taxing authorities. The amount recognized is measured as the largest amount of benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. Management has concluded that the Company has taken no uncertain tax positions that require adjustment to the financial statements to comply with the provisions of this guidance.

When applicable, the Company will include interest and penalties related to uncertain tax positions in income tax expense.

Earnings (Loss) per Common Share

The computation of basic earnings per common share is computed using the weighted average number of common shares outstanding during the period. The computation of diluted earnings per common share is based on the weighted average number of shares outstanding during the period plus common stock equivalents which would arise from the exercise of options and warrants outstanding using the treasury stock method and the average market price per share during the year. Options, warrants, convertible debt and convertible preferred stock which are common stock equivalents are not included in the diluted earnings per share calculations when their effect is anti-dilutive.

Stock-Based Compensation

The Company accounts for stock issued to employees, officers and directors in accordance with accounting standards for share-based payments which requires all new share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values.

Non-Controlling Interest

The Company accounts for the non-controlling interest in its two subsidiaries under ASC 810-10-45-16, Non-controlling Interest in a Subsidiary. This standard defines a non-controlling interest, previously called a minority interest, as the portion of equity in a subsidiary not attributable, directly or indirectly, to a parent. The standard requires, among other items, that a non-controlling interest be included in the consolidated statement of financial position within equity separate from the parent's equity; consolidated net income to be reported at amounts inclusive of both the parent's and non-controlling interest's shares and, separately, the amounts of consolidated net income attributable to the parent and non-controlling interest all on the consolidated statement of operations; and if a subsidiary is deconsolidated, any retained non-controlling equity investment in the former subsidiary be measured at fair value and a gain or loss be recognized in net income based on such fair value. Additionally, the standard defines a non-controlling interest as a financial instrument issued by a subsidiary that is classified as equity in the subsidiary's financial statements. A financial instrument issued by a subsidiary that is classified as a liability in the subsidiary's financial statements based on the guidance in other standards is not a controlling interest because it is not an ownership interest.

Royalty interests that entitle the holder to participate in future earnings and are not repayable are classified as non-controlling interests.

Deferred Offering Costs:

The Company may incur legal and accounting fees, as well as due diligence fees related to the preparation of our pending financing. Such costs are initially deferred until the offering is completed, at which time they are recorded as a reduction of gross proceeds from the offering, or expensed to operations if the offering is unsuccessful.

Nature and Classification of the Non-Controlling Interest in the Consolidated Financial Statements

Arrayit Corporation is the controlling interest of the affiliated group, since it maintains an investment in each of the operating entities. Arrayit Corporation has an 80% ownership investment in Arrayit Diagnostics, Inc., which in turn has an 80% interest in Arrayit Diagnostics (Ovarian), Inc., and Arrayit Diagnostics (Parkinson's), Inc. as of September 30, 2010 and December 31, 2009.

A non-controlling interest is the portion of the equity in a subsidiary not attributable, directly or indirectly, to a parent. A non controlling interest is the ownership held by owners other than the consolidating parent. The non-controlling interest is reported in the consolidated statement of financial position separately from the parent's equity, within the equity section of the balance sheet. The minority interest in the current year's income (loss) is segregated from the earnings (loss) attributable to the controlling parent. Minority ownership equity interest in the consolidating subsidiaries is increased by equity contributions and proportionate share of the subsidiaries earnings and is reduced by dividends, distributions and proportionate share of the subsidiaries incurred losses.

Recent Accounting Pronouncements

There were no new accounting pronouncements applicable to the Company's business during the quarter ended September 30, 2010.

The Company has reviewed all recently issued, but not effective, accounting pronouncements and does not believe the future adoption of any such pronouncements may be expected to cause a material impact on its financial condition or the results of its operations.

NOTE 3 – GOING CONCERN

The accompanying consolidated financial statements of the Company were prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has incurred significant net losses and negative cash from operations since it was a party to the Pediatrix legal dispute. At September 30, 2010, Arrayit had a working capital deficit of \$7,421,305, a stockholders' deficit of \$7,454,985, and recurring net losses. The Company currently devotes a significant amount of its resources on developing clinical protein biomarker diagnostic products and services, and it does not expect to generate substantial revenue until certain diagnostic tests are cleared by the United States Food and Drug Administration and commercialized. Management believes that current available resources will not be sufficient to fund the Company's planned expenditures over the next 12 months. The Company's ability to continue to meet its obligations and to achieve its business objectives is dependent upon, among other things, raising additional capital or generating sufficient revenue in excess of costs. At such time as the Company requires additional funding, the Company will seek to raise such additional funding from various possible sources, including, its parent company, the public equity market, private financings, sales of assets, collaborative arrangements and debt. If the Company raises additional capital through the issuance of equity securities or securities convertible into equity, stockholders will experience dilution, and such securities may have rights, preferences or privileges senior to those of the holders of common stock or convertible senior notes. If the Company raises additional funds by issuing debt, the Company may be subject to limitations on its operations, through debt covenants or other restrictions. If the Company obtains additional funds through arrangements with collaborators or strategic partners, the Company may be required to relinquish its rights to certain technologies or products that it might otherwise seek to retain. There can be no assurance that the Company will be able to raise additional funds, or raise them on acceptable terms. If the Company is unable to obtain financing on acceptable terms, it may be unable to execute its business plan, the Company could be required to delay or reduce the scope of its operations, and the Company may not be able to pay off its obligations, if and when they come due.

These factors create substantial doubt about Arrayit's ability to continue as a going concern. These consolidated financial statements do not include any adjustments relating to the recoverability or classification of recorded assets and liabilities or other adjustments that may be necessary should the Company not be able to continue as a going concern.

The ability of Arrayit to continue as a going concern is dependent on Arrayit generating cash from the sale of its common stock or obtaining debt financing and attaining future profitable operations. Management's plans include selling its equity securities and obtaining debt financing to fund its capital requirement and ongoing operations; however, there can be no assurance Arrayit will be successful in these efforts.

NOTE 4 – CASH AND RESTRICTED CASH

Cash on hand and bank overdrafts represent cash that may freely be used in the conduct of our business.

At December 31, 2009, restricted cash was comprised of a \$100,000 Certificate of Deposit and accrued interest of \$293, lodged with our bankers as security for a \$100,000 letter of deposit we were mandated to lodge with the Pennsylvania court as part of the Pediatrix legal action more fully described in Note 14. Upon finalization of the legal action, the letter of credit was returned and the bankers released the restrictions on the Certificate of Deposit.

NOTE 5 – ACCOUNTS RECEIVABLE SOLD WITH RECOURSE

Accounts receivable are shown net of an Allowance for Doubtful Accounts. As more fully explained in Note 6 below, receivable has been reduced by Accounts Receivable loans sold with recourse.

	September 30, 2010	December 31, 2009
Gross accounts receivable	\$ 571,551	\$ 431,420
Less:		
Allowance for doubtful accounts	(100,000)	(100,000)
Loan value of receivables sold with recourse (see note 6)	(379,331)	(259,476)
Total	\$ 92,221	\$ 71,944

NOTE 6 – ACCOUNTS RECEIVABLE SOLD WITH RECOURSE

Pursuant to an agreement dated July 5, 2007, the Company has sold some of its Accounts Receivable to a financial institution with full recourse. The financial institution retains a 15% portion of the proceeds from the receivable sales as reserves, which are released to the Company as the Receivables are collected. The maximum commitment under this facility is \$450,000, and is limited to receivables that are less than 31 days outstanding. The facility bears interest at prime plus 7%, currently 16% at September 30, 2010, and is secured by an unconditional guarantee of the Company and a first charge against the Accounts Receivable. At September 30, 2010, the balance outstanding under the recourse contracts was \$379,331 net of a hold back reserve of \$16,392 (December 31, 2009 - \$259,476 net of a hold back reserve of \$4,715). Because of the Company's credit policies, repossession losses and refunds in the event of default have not been significant and losses under the present recourse obligations are not expected to be significant, it is at least reasonably possible that the Company's estimate will change within the near term.

NOTE 7 – FIXED ASSETS

Property and equipment consisted of the following:

	September 30, 2010	December 31, 2009
Fixed Assets – Cost	\$ 347,139	\$ 345,107
Less:		
Accumulated Depreciation	(299,376)	(276,419)
Total	\$ 47,763	\$ 68,688

Depreciation expense totalled \$22,957 and \$10,500 respectively for the nine months ended September 30, 2010 and 2009; and \$7,653 and \$3,500 for the three months ended September 30, 2010 and 2009.

NOTE 8 – ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

Accounts payable and accrued liabilities, consisted of the following:

	September 30, 2010	December 31, 2009
ACCOUNTS PAYABLE		
Normal course of business	\$ 1,387,814	\$ 1,328,851
Pertaining to law suits	2,821,136	2,889,677
Total Accounts Payable	4,208,950	4,218,528
ACCRUED LIABILITIES		
Accrued salaries and wages	1,164,958	780,833
Judgement Interest	323,658	309,719
Other	261,638	11,159
Total Accrued Liabilities	1,750,254	1,101,711
TOTAL	\$ 5,959,204	\$ 5,320,239

NOTE 9 – DUE TO RELATED PARTIES

Pursuant to a consulting agreement with Dr. Mark Schena, the Company is obligated to pay a royalty of 5% of gross sales to him as a royalty for unfettered use of his patents and knowledge. Amounts outstanding at September 30, 2010 and December 31, 2009 of \$591,333 and \$459,116, respectively, are unsecured, non-interest bearing and due on demand.

NOTE 10 – DEBT MODIFICATION

In 2008, Cloud Capital entered into a formal custodial arrangement with 16 participants. Cloud has no discretionary power and acts solely as custodian taking direction from each participant. Each participant lodged a basket of securities with the custodian made up of common, convertible preferred and convertible debt at the time of the IMHI acquisition of TeleChem on February 21, 2008.

In January 2008, the Company entered into an oral agreement with each of the participants whereby the participant agreed to a fixed number of shares for their "basket" of securities. However, On February 20, 2009, the participants became discouraged with the efforts of the Company to complete the regulatory filings and requested that the original Oral Agreement be abrogated. The Company then came to a new Oral Agreement with each of the participants that included the following:

- (a) All prior agreements are now null and void. This includes both the predecessor Oral as well as the predecessor Written agreements.
- (b) The quantum of shares being made available to the 16 participants will be fixed at 12,509,357.
- (c) The 18,695 common shares, held by the participants, are issued and outstanding and will be not be affected by the new Oral Agreement.

(d) The 2,926,787 pre-split, (97,634 post-split) Series A Preferred Shares will be surrendered for cancellation without compensation by each of the participants.

(e) The debt of \$1,993,450 and estimated penalty and interest of \$1,555,750 for a total approximation of \$3,549,200 will be converted into 12,509,357 common shares, being a fixed number of common shares regardless of the interest and penalties that continue to accrue.

(f) Due to the lack of sufficient authorized capital only 2,712,500 common shares were available for conversion on March 13, 2009 and March 16, 2009.

(g) Interest and penalties cease to accrue on the debt and therefore no additional penalties or interest will become payable.

(h) The Oral Agreements constitute a formal waiver of any prior and future defaults on the underlying debt, thereby preventing the debt holders from asserting any rights and / or remedies they previously were entitled to under the written agreements.

It is the intention of the 16 debt holders and the Company that the debt will be converted into common shares, as soon as practical. Currently, the Company does not have sufficient authorized share capital to satisfy this obligation, and therefore the debt may not be converted. Management is not able to practically estimate when it will have sufficient authorized share capital as this lies outside the control of the Company.

For greater certainty and as outlined in Item (e) above, as a result of these Oral Agreements there will be no effect upon the Company of the continuing defaults or of any changes in interest rates. The Oral Agreements fix the number of shares to be issued upon conversion regardless of any additional interest and penalties, which may have been due under the originating documents that are now superseded by the Oral Agreements.

On March 13, 2009, the date of Debt Modification, the Company recorded a derivative liability of \$20,996,593 as a result of insufficient authorized shares to satisfy the debt settlement according to accounting standards for accounting for derivative instruments and hedging activities and revalued the liability by recording a loss on derivative liability of \$19,021,116.

The 97,634 Preferred Series "A" shares held by the Oral Agreement debt holders were cancelled subsequent to the debt settlement.

NOTE 11 – DEBT

	September 30, 2010	December 31, 2009
NOTES PAYABLE - ARRAYIT DIAGNOSTICS, INC.		
Notes payable, interest at 10%, which was due August 10, 2010 and is now past due, secured by 200,000 shares out of the Company's common stock, pledged to the private lender without compensation as follows: 100,000 common shares provided by the Company's chief financial officer; 50,000 common shares provided without compensation by a minority shareholder in Arrayit Diagnostics; and a call option call to acquire an additional 50,000 common shares currently held by a minority shareholder in Arrayit Diagnostics.	\$ 50,000	\$ -
NOTES PAYABLE - ARRAYIT CORP.		
Notes payable, interest at 10%, which was due August 10, 2010 and is now past due, secured by 1,000,000 shares out of the Company's common stock, pledged to the private lender without compensation by the Company's Chairman. The terms also called for the lender to withhold proceeds of \$20,000 as a debt origination fee and the issuance of 200,000 warrants issuable for shares of common stock at \$1.00 per share. The annual effective interest rate for this loan is estimated to be 239.2%	200,000	-
LESS: Unamortized loan fee and discount in connection with the obtaining of the loan	-	-
	200,000	-
Notes payable to Wells Fargo, payable in 60 monthly installments of \$8,572 including interest at bearing interest at Prime plus 2.75%, through November 2012. Secured by Equipment, Inventory, Accounts, Instruments, Chattel Paper and General Intangibles of TeleChem International, Inc. Unconditional Guarantees by some of the Company's Class "C" shareholders and unconditional limited guarantees by those shareholders' spouses. Guarantee secured by two residential properties and cash collateral of \$276,000.	187,239	261,126
Notes payable, interest at 8%, unsecured due on demand from Arrayit creditors	40,637	42,711
Notes payable, interest at 8%, unsecured due on demand from the former TeleChem shareholders and their families.	711,064	729,750
	1,138,940	1,033,587
Notes payable including related parties	\$ 1,188,940	\$ 1,033,587
Short Term Debt	\$ 1,088,573	\$ 852,931
Long Term Debt	100,367	180,656
Notes payable including related parties	\$ 1,188,940	\$ 1,033,587

Scheduled maturities of notes payable for years succeeding September 30, 2010 are as follows:

Year	Amount
2010	\$ 1,088,573
2011	69,663
2012	30,704
Total	\$ 1,188,940

Derivative Liabilities

Convertible Debt – SovCap

The Company, upon the execution of the reverse merger with IMHI, become obligated for convertible debt of \$3,549,200 (see Note 10) which on March 13, 2009 become subject to a series of 16 Oral Agreements. The debt, as detailed in Note 10, was shown as a derivative, subsequent to the establishment of the Oral Agreements for the Company's interim reporting periods ending March 31, June 30 and September 30, 2009. Upon the increase in the Company's authorized common share capital, on December 10, 2009, the balance of the debt was converted. The continuity of the convertible loan for the year ended December 31, 2009 is as follows:

	Shares Issued	Original Debt	Accrued Interest	Total Debt
December 31, 2008		\$ 1,993,450	\$ 1,555,750	\$ 3,549,200
Conversions:				
March 13, 2009	1,140,000	(134,799)	(105,201)	(240,000)
March 16, 2009	1,572,500	(321,551)	(250,949)	(572,500)
December 11, 2009	9,765,857	(1,537,100)	(1,199,600)	(2,736,700)
September 30, 2010 and December 31, 2009	12,478,357	\$ -	\$ -	\$ -

Warrants

With the increase in authorized share capital on December 10, 2009, the Company now has sufficient shares to settle any and all outstanding common stock equivalent instruments. The previously recognized derivative was accordingly transferred to Additional Paid in Capital.

During the quarter ended June 30, 2010 the Company issued 150,000 share purchase warrants, expiring on April 25, 2012, exercisable at \$1.00 and issued 200,000 share purchase warrants also exercisable at \$1.00, expiring on May 12, 2012

Options

On October 1, 2009, the Company granted 450,000 options to the President of Arrayit Diagnostics, Inc. at an exercise price of \$0.32. The \$229,000 fair value of these options was recorded as an expense on that date.

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On September 30, 2010, the Company granted 200,000 options to the President of Arrayit Diagnostics, Inc. at an exercise price of \$0.20. The \$40,000 fair value of these options was recorded as an expense on that date.

NOTE 12 – ROYALTY OBLIGATIONS

(a) Advisory Agreement

Under paragraph 2 (b) of an Advisory Agreement dated August 11, 2009 between Arrayit Diagnostics, Inc. and a limited liability partnership, controlled by parties that are also shareholders in Arrayit Corporation, there is a contractual obligation to pay a Royalty of twenty percent (20%) of the net sales of Arrayit Diagnostics, Inc., and its subsidiaries, which includes the Company. “Net Sales” means the gross selling price by the Company and sub-licensees for the sale of any product or products, less trade discounts allowed, credits for claims or allowances, commissions, refunds, returns and recalls.

The term of the Advisory Agreement is five years. The royalties and ownership provisions are in perpetuity.

The entitlement to royalties under the Advisory Agreement is decreased by obligation to pay royalties to other advisors and investors. With respect to the revenue generated by Arrayit Diagnostics (Ovarian), Inc. as described in (b) below, the Company is obligated to pay a 0.95% royalty to purchasers of royalty interests, thereby reducing the Company’s obligation to the advisor by a similar amount, resulting in a net royalty obligation to the advisor of 19.05% on revenue generated by our Ovarian subsidiary.

During the nine and three months ended September 30, 2010 and 2009, there were no revenues earned and hence no obligation to pay any royalties.

(b) Royalty Interests – ARRAYIT DIAGNOSTICS (OVARIAN), INC.

Third party investors purchased royalty interests in the amount of \$285,000 in Arrayit Diagnostics (Ovarian), Inc. in return for a zero decimal nine five percent (0.95%) royalty on net sales of the Ovarian test. Amounts received with respect to these royalty interests are shown as Non-Controlling Interests on the Balance Sheet, as there are no terms of repayment of the royalty interests.

During the nine and three months ended September 30, 2010 and 2009, there were no revenues earned and hence no obligation to pay any royalties.

(c) Wayne State University – ARRAYIT DIAGNOSTICS (OVARIAN), INC.

Under terms of a biomarker license agreement between Wayne State University and the Company, effective December 7, 2009, the Company is obligated to pay the University royalties of five percent (5%) of net sales. In addition the license agreement provides for lump sum payments to be made as milestone events are achieved.

During the nine and three months ended September 30, 2010 and 2009, there were no revenues generated and hence no obligation to pay any amounts to Wayne State University.

(d) The Parkinson’s Institute – ARRAYIT DIAGNOSTICS (PARKINSON’S), INC.

Pursuant to an agreement dated February 9, 2009 between the Company, and The Parkinson's Institute, a California Corporation, Arrayit Diagnostics (Parkinson’s), Inc., is obligated to make payments, of five percent (5%) of gross earnings generated from research derived from the biological specimens from Parkinson's disease patients and control

patients provided by the Parkinson's Institute.

During the nine and three months ended September 30, 2010 and 2009, there were no revenues generated and hence no obligation to pay any amounts to the Parkinson's Institute.

NOTE 13 - STOCKHOLDERS' EQUITY (DEFICIT)

TOTAL ARRAYIT CORPORATION STOCKHOLDERS' EQUITY (DEFICIENCY)										NON-CONT		
Description	Preferred Series A		Preferred Series C		Common Stock		Additional Paid In Capital		Retained Earnings	Total	Royalty Interest	Subsidiary Receivable
	Number	Dollar	Number	Dollar	Number	Dollar						
Balance, December 31, 2009	25,620	25	103,143	103	19,085,859	18,896	14,478,455	(21,097,741)	(6,600,262)	285,000	(1)	
Convert Preferred A to Common	(3,586)	(3)	-	-	13,177	13	(10)	-	-	-	-	-
Convert Preferred C to Common	-	-	(10,942)	(11)	3,830,010	3,830	(3,819)	-	-	-	-	-
Issuance of shares for services	-	-	-	-	1,830,010	1,830	1,393,675	-	1,395,505	-	-	-
Issuance of shares on exercise of options	-	-	-	-	160,000	160	51,040	-	51,200	-	-	-
Issuance of warrants for services	-	-	-	-	-	-	143,431	-	143,431	-	-	-