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PURE BIOSCIENCE
Form 10QSB
December 15, 2003

U.S. Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the period ended October 31, 2003

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 [No Fee Required]
For the transition period from _____ to _____

Commission File number 0-21019

PURE Bioscience

(Name of small business issuer in its charter)

California

33-0530289

(State or other jurisdiction of
incorporation or organization)

(IRS Employer Identification No.)

1725 Gillespie Way, El Cajon, California 92020

(Address of principal executive offices)

619 596 8600

Issuer's telephone number

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

State the number of shares outstanding of each of the issuer's classes of common equity as of the latest practicable date: 13,484,088 as of December 12, 2003.

INNOVATIVE MEDICAL SERVICES

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PART 1 ITEM 1 Financial Statements

CONSOLIDATED BALANCE SHEETS

| | (Unaudited) October 31 2003 ---- | July 31 2003 ---- |
|--|---|-------------------------|
| ASSETS | | |
| Current Assets | | |
| Cash and cash equivalents | \$ 145,827 | \$ 251,087 |
| Accounts receivable, net of allowance for doubtful accounts of \$ 63,500 at October 31, 2003 and \$63,500 at July 31, 2003 | 256,484 | 163,895 |
| Due from officers and employees | -- | 61 |
| Trust deed receivable | 2,035,000 | -- |
| Inventories | 112,537 | 119,237 |
| Prepaid expenses | 3,000 | 6,655 |
| | ----- | ----- |
| Total current assets | 2,552,848 | 540,935 |
| | ----- | ----- |
| Property, Plant and Equipment | | |
| Property, plant and equipment | 221,554 | 249,024 |
| | ----- | ----- |
| Total property, plant and equipment | 221,554 | 249,024 |
| | ----- | ----- |
| Noncurrent Assets | | |
| Deposits | 9,744 | 9,341 |
| Patents and licenses | 2,479,769 | 2,475,280 |
| | ----- | ----- |
| Total noncurrent assets | 2,489,513 | 2,484,621 |

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| | | |
|--|--------------|--------------|
| Assets of the water division held for resale | 337,850 | 352,423 |
| | ----- | ----- |
| Total assets | \$ 5,601,765 | \$ 3,627,002 |
| | ===== | ===== |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current Liabilities | | |
| Accounts payable | \$ 980,762 | \$ 1,079,128 |
| Accrued liabilities | 180,334 | 114,523 |
| Notes payable | 645,385 | 180,513 |
| Loans from shareholders | 600,000 | 600,000 |
| | ----- | ----- |
| Total current liabilities | 2,406,481 | 1,974,164 |
| | ----- | ----- |
| Liabilities of the water division held for resale | 45,083 | 36,165 |
| | ----- | ----- |
| Stockholders' Equity | | |
| Class A common stock, no par value: authorized 50,000,000 shares, issued and outstanding 13,604,088 at October 31, 2003 and 10,594,088 at July 31, 2003 | 16,948,203 | 14,758,203 |
| Warrants: issued and outstanding 1,037,429 warrants | 788,473 | 788,473 |
| Accumulated deficit | (14,586,475) | (13,930,003) |
| | ----- | ----- |
| Total stockholders' equity | 3,150,201 | 1,616,673 |
| | ----- | ----- |
| Total liabilities and stockholders' equity | \$ 5,601,765 | \$ 3,627,002 |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

| | For the Three Months Ended | |
|---------------|----------------------------|-----------|
| | October 31 | |
| | 2003 | 2002 |
| | ---- | ---- |
| Net revenues | \$ 39,293 | \$ 36,683 |
| Cost of sales | 28,333 | 26,267 |
| | ----- | ----- |

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| | | |
|--|--------------|--------------|
| Gross profit | 10,960 | 10,416 |
| | ----- | ----- |
| Selling expenses | 46,697 | 150,200 |
| General and administrative expenses | 328,432 | 316,946 |
| Research and development | 376,941 | 173,068 |
| | ----- | ----- |
| Total operating costs | 752,070 | 640,214 |
| | ----- | ----- |
| Loss from operations | (741,110) | (629,798) |
| | ----- | ----- |
| Other income and (expense): | | |
| Interest income | 32,329 | 1,329 |
| Interest Expense | (73,102) | (17,470) |
| Other | (1,095) | -- |
| | ----- | ----- |
| Total other income (expense) | (41,868) | (16,141) |
| | ----- | ----- |
| Loss from continuing operations | (782,978) | (645,939) |
| | ----- | ----- |
| Discontinued operations: | | |
| Income from discontinued operations | 126,506 | 167,115 |
| | ----- | ----- |
| Net loss | \$ (656,472) | \$ (478,824) |
| | ===== | ===== |
| Net loss per common share, basic and diluted | | |
| Continuing operations | \$ (0.06) | \$ (0.07) |
| Discontinued operations | 0.01 | 0.02 |
| | ----- | ----- |
| Net loss | \$ (0.05) | \$ (0.05) |
| | ===== | ===== |

| | (Unaudited) Three Months Ended October 31 2003 | Year Ended July 31 2003 |
|---|--|----------------------------------|
| ----- | | |
| CONSOLIDATED STATEMENTS OF ACCUMULATED DEFICITS | | |
| | ----- | ----- |
| Balance, beginning of period | \$ (13,930,003) | \$ (10,646,014) |
| Net income (loss) | (656,472) | (3,283,989) |
| | ----- | ----- |
| Balance, end of period | \$ (14,586,475) | \$ (13,930,003) |
| | ===== | ===== |

The accompanying notes are an integral part of these financial statements

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CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

| | For the Three Months Ended October 31 | |
|--|--|--------------|
| | 2003 | 2002 |
| | ---- | ---- |
| Cash flows from operating activities | | |
| Net loss | \$ (656,472) | \$ (478,825) |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Amortization | 40,511 | 38,037 |
| Depreciation | 27,473 | 30,187 |
| Services and interest paid for with stock and warrants | 74,872 | -- |
| Income from discontinued operations | (126,506) | (167,115) |
| Changes in assets and liabilities: | | |
| (Increase) decrease in accounts receivable | (92,588) | (56,264) |
| (Increase) decrease in due from officers and employees | 61 | 22,980 |
| (Increase) decrease in prepaid expense | 3,655 | 64,996 |
| (Increase) decrease in inventory | 6,699 | 57,903 |
| (Increase) decrease in deposits | (403) | (387) |
| Increase (decrease) in accounts payable | (98,366) | 102,017 |
| Increase (decrease) in accrued liabilities | 65,808 | 7,851 |
| | ----- | ----- |
| Net cash provided (used) by operating activities | (755,256) | (378,620) |
| | ----- | ----- |
| Cash flows from investing activities | | |
| Purchase of patents and licenses | (45,000) | (4,740) |
| Purchase of property, plant and equipment | -- | (8,928) |
| | ----- | ----- |
| Net cash (used) in investing activities | (45,000) | (13,668) |
| | ----- | ----- |
| Cash flows from financing activities | | |
| Proceeds from debt obligations | -- | 100,000 |
| Proceeds from sale of common stock | 545,000 | 76,950 |
| | ----- | ----- |
| Net cash provided by financing activities | 545,000 | 176,950 |
| | ----- | ----- |
| Cash flows from discontinued operations | 149,996 | 185,616 |
| | ----- | ----- |
| Net increase (decrease) in cash and cash equivalents | (105,260) | (29,722) |
| | ----- | ----- |
| Cash and cash equivalents at beginning of period | 251,087 | 151,257 |
| | ----- | ----- |

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| | | |
|---|--------------|------------|
| Cash and cash equivalents at end of period | \$ 145,827 | \$ 121,535 |
| | ===== | ===== |
| Supplemental disclosures of cash flow information | | |
| Cash paid for interest | \$ 43,230 | \$ 17,470 |
| Noncash investing and financing activities: | | |
| Value of shares issued in exchange for services | \$ 45,000 | \$ 139,650 |
| Value of options issued in exchange for services | \$ -- | \$ 59,805 |
| Trust Deed received in exchange for stock | \$ 2,035,000 | |

The accompanying notes are an integral part of these financial statements

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NOTES TO FINANCIAL STATEMENTS

Note 1. Financial Statements

The financial statements included herein have been prepared by PURE Bioscience (the Company) without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in the financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted as allowed by such rules and regulations, and PURE Bioscience believes that the disclosures are adequate to make the information presented not misleading. It is suggested that these financial statements be read in conjunction with the July 31, 2003 audited financial statements and the accompanying notes thereto. While management believes the procedures followed in preparing these financial statements are reasonable, the accuracy of the amounts are in some respects dependent upon the facts that will exist and procedures that will be accomplished by PURE Bioscience later in the year. The results of operations for the interim periods are not necessarily indicative of the results of operations for the full year.

The management of the Company believes that the accompanying unaudited financial statements contain all adjustments (including normal recurring adjustments) necessary to present fairly the operations and cash flows for the periods presented.

Note 2. Business Segment and Sales Concentrations

In accordance with the provisions of SFAS No. 131, certain information is disclosed based on the way management organizes financial information for making operating decisions and assessing performance. In determining operating segments, the Company reviewed the current management structure reporting to the chief operating decision-maker ('CODM') and analyzed the reporting the CODM receives to allocate resources and measure performance.

The Company's business activities are divided, managed and conducted in two basic business segments, the Water Treatment segment and the Bioscience segment. These two segments were determined by management based upon the inherent differences in the end use of the products, the inherent differences in the value added processes made by the Company, the differences in the regulatory requirements and the inherent differences in the strategies required to

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successfully market finished products. The Water Treatment segment includes Commercial Water and Residential Retail products and the Nutripure Water Dealer program. The Water Treatment division has been discontinued (Note 6). Bioscience includes Axenohl (Silver Ion Technology) and the Innovex line of pest control products.

Segment information is presented in accordance with SFAS 131, Disclosures about Segments of an Enterprise and Related Information. This standard is based on a management approach, which requires segmentation based upon the Company's internal organization and disclosure of revenue and operating income based upon internal accounting methods. The Company's financial reporting systems present various data for management to run the business, including internal profit and loss statements prepared on a basis not consistent with U.S. generally accepted accounting principles.

| FOR THE THREE MONTHS ENDED OCTOBER 31, 2002 | Water Treatment (Discontinued) | Bioscience | Reconc Amou |
|--|--------------------------------------|------------------|----------------|
| Revenues | | | |
| Commercial Water Treatment | | | |
| Fillmaster Products | \$ 304,500 | \$ - | \$ - |
| Replacement Filters (Includes CSP 2000) | 153,200 | - | - |
| Residential Water Treatment | 128,200 | - | - |
| Water Dealer Program | 107,500 | - | - |
| Silver Ionization | - | - | - |
| Pesticide | - | 36,700 | - |
| Total Revenues | \$ 693,400 | \$ 36,700 | \$ - |
| Operating Income/(Loss) | \$ 167,100 | \$ (268,100) | \$ (37,000) |
| Segment Assets | \$ 1,303,200 | \$ 1,873,300 | - |

| FOR THE THREE MONTHS ENDED OCTOBER 31, 2003 | Water Treatment (Discontinued) | Bioscience | Reconc Amou |
|--|--------------------------------------|------------------|----------------|
| Revenues | | | |
| Commercial Water Treatment | | | |
| Fillmaster Products | \$ 236,000 | \$ - | \$ - |
| Replacement Filters (Includes CSP 2000) | 184,200 | - | - |
| Residential Water Treatment | 26,000 | - | - |
| Water Dealer Program | 21,000 | - | - |
| Silver Ionization | - | 8,600 | - |
| Pesticide | - | 30,700 | - |
| Total Revenues | \$ 467,200 | \$ 39,300 | \$ - |
| Operating Income/(Loss) | \$ 126,500 | \$ (167,200) | \$ (61,000) |
| Segment Assets | \$ 340,700 | \$ 2,639,200 | - |

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Significant customers primarily consisted of domestic retail chain pharmacies. Sales concentrations to major chain stores were approximately \$322,300 and export sales were \$13,700 for the quarter ended October 31, 2003. Sales concentrations to major chain stores were approximately \$375,100 and export sales were \$2,400 for the three months ended October 31, 2002. No customer accounted for more than 10% of consolidated sales.

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Note 3. Common Stock

In August of 2003 the Company completed a financing arrangement which included the acquisition of a \$2,000,000 Trust Deed receivable and \$35,000 related accrued interest and issuing a \$435,000 note payable resulting in a net increase of \$1,600,000 in equity during the period. This note receivable is in exchange for the issuance of 2,000,000 shares (at fair value of \$0.80 per share) of the Company's common stock to a party unrelated to the Company, and that is fully secured by specific assets other than the equity instruments granted.

On August 25, 2003, 60,000 shares were issued in exchange for attorney fees related to the acquisition of the Axenohl patent. The shares were issued at fair value of \$0.75 per share. Also during the quarter ended October 31, 2003 the Company conducted three private placements in which it issued 950,000 shares of common stock at prices that range from \$0.50 to \$0.75 per share for a total of \$545,000 with a weighted average price of \$0.57 per share.

Note 4. Recent Accounting Pronouncements

In November 2002, the FASB issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others". Interpretation 45 is effective for financial statements of interim or annual periods fiscal years ending after December 15, 2002 and requires the following disclosures of the Company's product warranties:

The Company provides a standard warranty of two years for replacement parts on all Fillmaster systems sold. Most of the Company's chain customers have entered into multi-year contracts for the Customer Service Plan 2000. The CSP 2000 provides an extended warranty on all PURE Bioscience pharmacy products; significant discounts on maintenance item costs; annual software upgrades for the Fillmaster 1000e and Scanmaster; automatic replacement filter shipments; and simplified, annual invoicing. When the customer buys a dispenser on the Customer Service Plan 2000 they agree to pay a fixed annual fee that covers replacement filters and parts. The Company monitors the costs of providing replacement parts other than filters. This cost has remained steady and is computed as a percentage of related revenues. The following is a summary of changes in the Company's product warrantee liability.

| | Beginning Liability | Expense Incurred | Warran Paymen |
|-------------------------------------|------------------------|---------------------|------------------|
| | ----- | ----- | ----- |
| Three months ended October 31, 2002 | \$ 41,445 | \$ 2,612 | \$ 1,3 |
| Three months ended October 31, 2003 | \$ 42,430 | \$ 2,903 | \$ 3,0 |
| | ----- | ----- | ----- |

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Note 5. Reclassifications

Certain reclassifications have been made to previously reported statements to conform to the Company's current financial statement format.

Note 6. Sale of Water Treatment Division and Discontinued Operations

On October 29, 2003, PURE Bioscience and subsidiaries ("PURE") announced that it had entered into an agreement (the "Agreement For The Purchase and Sale of Assets") to sell substantially all of the assets and certain related liabilities of the water treatment division, including substantially all of the related machinery, equipment, inventory, work in process, licenses, customer lists and certain intellectual property and certain agreements and contracts to Data Recovery Continuum, Inc. (DRCI). The Company will realize a gain on the sale of approximately \$2,000,000 after federal and California income taxes.

If the proposed transaction is consummated, DRCI will pay \$2.75 million in cash at the closing. DRCI will also pay an additional \$250,000 six months later and another \$1,000,000 one year after closing after the Nutripure 2000 Countertop water purifier reaches certain agreed upon volume and sales projections in connection with a rollout program with a large general merchandise retailer. In the event the sales of Nutripure products do not achieve the projected levels the additional payment amounts will be reduced on a pro rata basis. Also at closing DRCI has agreed to deposit an additional \$2.0 million into escrow to purchase the Company's Trust Deed receivable at face value, PURE Bioscience will incur no gain or loss on this portion of the agreement. The Trust Deed was acquired in August of 2003 in exchange for 2,000,000 unregistered shares of PURE common stock.

In accordance with SFAS 144, the assets and liabilities of the water division are classified as held for sale and are presented separately in the balance sheet. In addition, the results of operations from the water division have been reported as discontinued operations, and were historically shown as the Company's water treatment segment for financial reporting.

Components of the results of discontinued operations are:

| | Three Months Ended October 31, 2003 | Three Months Ended October 31, 2002 |
|----------------|--|--|
| | ----- | ----- |
| Net revenues | \$ 467,000 | \$ 693,400 |
| Cost of Sales | 209,500 | 418,300 |
| Other Expenses | 131,000 | 108,000 |
| | ----- | ----- |
| Total | \$ 126,500 | \$ 167,100 |
| | ----- | ----- |

Assets and liabilities of the water division held for sale include:

| | October 31, 2003 |
|--------------------------------------|------------------|
| | ----- |
| Inventories and other current assets | \$ 171,100 |
| Property, plant and equipment | 166,700 |
| | ----- |
| Total | 337,800 |
| | ----- |
| Accrued liabilities | 45,100 |
| | ----- |

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Net assets and liabilities of the water division held for sale: \$ 292,700

The interim financial statements include all adjustments, which in the opinion of management, are necessary in order to make the financial statements not misleading.

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ITEM 2

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the audited and unaudited financial statements of PURE Bioscience.

OVERVIEW

PURE Bioscience (formerly Innovative Medical Services) began as a provider of pharmaceutical water purification products. Although our current revenues are still primarily from the pharmacy industry, we have expanded from our niche pharmacy market into other, broader markets with new, proprietary bioscience products based upon our silver ion bioscience technologies and boric acid based pesticide technologies. Because of this business development evolution, in September 2003, shareholders approved a name change from Innovative Medical Services to PURE Bioscience. In November 2003, we announced that we signed a definitive agreement to sell our water treatment business to Data Recovery Continuum, Inc., a Delaware corporation based in California, for \$2.75 million in cash plus up to \$1.25 million in deferred payments over the next year. We are also selling to Data Recovery Continuum, Inc. (DRCI) our \$2.0 million Note and Deed of Trust asset for face value. Total combined cash proceeds from the transaction will be \$4.75 million to \$6.0 million to PURE Bioscience. Upon completion of the transaction, we emerge as a focused bioscience company that is debt-free, and we believe that we will be capitalized sufficiently to commercialize our powerful, least toxic and environmentally friendly technologies including our Axenohl(R) antimicrobial technology. Completion of the transaction is subject to approval by PURE Bioscience shareholders. On November 25, 2003, we filed a proxy statement with the Securities and Exchange Commission detailing the proposed sale. A definitive proxy statement will be sent to shareholders of PURE Bioscience seeking their approval of the transaction.

Water Treatment Division (Discontinued Operation) The Fillmaster(R) pharmaceutical water purification, dispensing and measuring products include the Pharmapure(R) water purification system, the FMD 550 dispenser, the patented Fillmaster 1000e computerized dispenser and the patented Scanmaster(TM) bar code reader. We also market proprietary National Sanitation Foundation certified replacement filters for the Fillmaster Systems. Our Nutripure(R) line of water treatment and filtration systems includes a line of Nutripure whole-house water softening systems, a line of Nutripure reverse osmosis point-of-use systems, the Nutripure 2000 countertop water filtration system and the Nutripure Sport filtered sport bottle. Results from this division are shown separately as "Discontinued Operation."

Bioscience Division Our bioscience division features a patented, aqueous disinfectant called Axenohl(R) (silver dihydrogen citrate). Based on the EPA toxicity categorization of antimicrobial products that ranges from Category I (high toxicity) down to Category IV, Axen, with its combination of the biocidal

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properties of ionic silver and citric acid, is an EPA Category IV antimicrobial for which precautionary labeling statements are normally not required. This compares with Category II warning statements for most leading brands of antimicrobial products.

The initial EPA registration for use of Axenohl and Axen (12-parts per million formula) as hard surface disinfectants was issued in 2001. In March 2003, we received Environmental Protection Agency (EPA) registration for our new Axen-30(R) formulated Category IV hard surface disinfectant product for commercial, industrial and consumer applications. Axen-30 is a 30-part per million (ppm) use-dilution formula of our patented antimicrobial technology, Axenohl.

The recent EPA approval allows us to expand the existing Axen efficacy claims as a hard surface disinfectant to include a 30 second kill time and a 24 hour residual kill on standard indicator bacteria, a 2 minute kill time on some resistant strains of bacteria including MRSE and VRE, 10 minute kill time on fungi, 30 second kill time on HIV Type I, and 10 minute kill time on other viruses. These claims distinguish the efficacy of Axen-30 from many of the leading commercial and consumer products currently on the market, while maintaining lower toxicity ratings.

In September 2003, we announced the first significant commercialization of our hard surface disinfectant, Axen-30, which is sold by EnvirOx L.L.C. of Danville, Illinois, as Critical Care(TM), a new commercial disinfectant-fungicide-virucide.

We plan to pursue additional EPA and FDA regulatory approvals for other applications. Additional possible uses for this product include wound care, topical infection care, personal disinfecting retail products, food processing, and food safety applications which may require FDA approvals, as well as municipal water treatment and point-of-use/point-of-entry water treatment products, which may require additional EPA approvals.

Also in September 2003, we announced an agreement with Therapeutics, Inc., a drug development company based in La Jolla, California, for the development and commercialization of Food and Drug Administration (FDA) regulated Axenohl-based products. Therapeutics, Inc. will fund and direct all development activities and FDA regulatory filings and will initially focus on development of Axenohl-based products for the treatment of bacterial, viral and fungal mediated diseases and conditions.

Our bioscience division also includes a line of pesticide technologies. Branded as Innovex(TM), the product line launched in October 2001 with our EPA-approved, patent-pending RoachX(TM). Subsequently, we have developed and launched additional products in the Innovex product line, including the EPA-approved AntX75(TM), two formulas of EPA-exempt non-toxic TrapX rodent lure, Pro's Choice(TM) caulk for pest control operators, and EPA approved CleanKill(TM), the Axen-based hard surface disinfectant for the pest control industry.

United States Department of Agriculture testing confirms that RoachX is over 96% effective in three to four days with one application for indoor and outdoor eradication of cockroaches, and can be used near children and food preparation areas. Boric acid is a well-known and effective deterrent of cockroaches and will kill them on contact, but cockroaches do not naturally eat the repellent. Although many pesticide products contain boric acid as the listed active ingredient, we believe RoachX to be new because of the endothermic reaction caused by the combination of boric acid and polyglycol that produces three unique results: 1) The formula protects the boric acid from water and humidity, 2) When combined with an attractant, the cockroaches perceive the formulation as food and will actually eat the polyglycol-encapsulated boric acid, and 3) The formula acts as a time-released pesticide, allowing the cockroach to return to

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the nest before it dies and then becomes a "bait station" for other roaches in the colony. We believe the product line, containing particular formulas and attractants for specific pests, is effective against cockroaches, ants, palmetto bugs, silverfish, waterbugs, ticks, fleas, lice and garden pests. Like the Axenohl antimicrobial technology, the boric acid based pesticides are very competitive with regard to efficacy when compared to leading brands while maintaining lower toxicity ratings.

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RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED OCTOBER 31, 2003 VERSUS THREE MONTH ENDED OCTOBER 31, 2002

During the quarter we decided to sell our water treatment division. Following the closing of the divestment transaction, we will be focused on our bioscience segment. Our current bioscience technologies include our Axenohl (silver dihydrogen citrate) antimicrobial product and our Innovex (Triglycylboride) pesticide products. We will realize a gain on the water treatment division sale of approximately \$2,000,000 after federal and California income taxes.

During the quarter ended October 31, 2003, bioscience segment revenues of \$39,300 remained virtually unchanged compared to \$33,900 in the prior period. The antimicrobial market is highly competitive, and we anticipate that market acceptance of a brand new technology may be a long term achievement. In addition to competition challenges, we believe that the investment necessary to pursue research testing and regulatory approval for Axenohl products will continue to be significant. As we receive additional regulatory approvals for Axenohl, however, we expect revenues to develop quickly. For example, now that we have received EPA approval on Axen-30, our Axenohl-based hard surface disinfectant, and we expect to see a shift toward increasing Axenohl division product sales in the coming year, and we believe that sales of Axen-30 will have a significant impact on revenues in future. We continue to believe that pesticide technologies will have a material impact on revenues in the coming year, and we continue to believe that the silver ion technologies will ultimately become the largest revenue generator for PURE Bioscience.

Gross profit for the quarter ended October 31, 2003 was \$11,000 versus \$10,400 in 2002. Gross profit percentage of 28% in 2003 remained unchanged from the prior period.

Net loss from continuing operations for the quarter ended October 31, 2003 was \$783,000 versus net loss of \$646,000 for the same period in 2002. During the quarter, General and Administrative expenses increased \$11,500, or 4%, from \$317,000 at in fiscal 2002 versus \$328,400 in fiscal 2003. Administrative expenses include an increase in amortization costs associated with purchased patents and licenses. Selling expense decreased approximately \$103,500, or 69%, from \$150,200 in 2002 to \$46,700 in 2003 because of a decreased use of salaried sales personnel and an increase in the use of commissioned salespeople. Research and Development increased approximately 125%, or \$203,800, over the same period in 2002 from \$173,100 to \$376,900. This increase was the result of continued time and resources devoted to the development and testing of our emerging pesticide and silver ion technology product lines. Of the loss in the current period, \$159,900 is attributable to non-cash items: \$74,900 of services and interest paid with stock and warrants, \$40,500 of amortization and \$27,500 of depreciation.

DISCONTINUED OPERATION

Income from discontinued operations for the quarter ended October 31, 2003 consisted of revenues of \$467,200, cost of sales of \$209,700 and other costs of \$131,000 resulting in a net income of \$126,500. Income from discontinued

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operations for the same period in 2002 consisted of revenues of \$693,400, cost of sales of \$418,300 and other costs of \$108,000 resulting in a net income of \$167,100. At October 31, 2003 the Company had a backlog of \$349,300 of water treatment products because cash flow limited the Company's ability to purchase raw materials. Had the Company been able to fulfill these orders in the current quarter, water treatment revenues would have exceeded those of the same quarter in 2002.

LIQUIDITY AND CAPITAL RESOURCES

From inception through the present, we have financed our operations primarily through our initial public offering in August of 1996 and by subsequent private placement stock sales. In addition, the Company had obtained short term financing through a \$500,000 line of credit. In September 2002 the Company renegotiated its line of credit and extended it until November 2003. The extension includes an increase from \$500,000 to \$600,000 at an interest rate of 1 1/2 % per month secured against the entire assets of the Company excluding the Axenohl patent. In July 2003, the Company issued a \$300,000 convertible debenture at an interest rate of 10% per annum due July 2004.

The Company is currently attempting to strengthen its liquidity position by working with an investment banker because the Company requires an outside source of capital to fund planned projects relating to new product development and related product launches, research and development projects and regulatory approvals. The Company's operations alone may not generate cash flows, within the next twelve months, sufficient to fund planned expansion.

In August of 2003, the Company completed a financing arrangement which included the acquisition of a \$2,035,000 Trust Deed asset (and \$435,000 offsetting loan payable for a net increase in equity of \$1,600,000) in exchange for the issuance of 2,000,000 shares of the Company's common stock to a party unrelated to the grantor. In October 2003, the Company signed a term sheet to sell the Trust Deed asset for cash at face value. The purchasing party is also acquiring the water treatment division for \$2,750,000 in cash plus up to \$1,250,000 in deferred payments over the next year. Completion of the divestment of the water treatment division is subject to approval by PURE Bioscience shareholders. The Company intends to use a portion of the proceeds of this transaction to satisfy outstanding debt. The remaining proceeds should be sufficient to sustain operations and fund product development and commercialization until our bioscience technologies result in positive cash flow.

If the asset sale is not approved, PURE Bioscience will continue to operate the water treatment division unless and until it is able to negotiate another transaction that the Board of Directors believes is acceptable to the stockholders and to PURE Bioscience. The Board of Directors believes that this transaction relieves the need for additional funding to properly continue the marketing, selling and further development of our bioscience technologies while still making the necessary investments in the water treatment division to maintain our historical growth rates. To the extent that we do not obtain needed capital through the sale of the water treatment division, we will have to obtain it through the issuance of additional debt or equity or through other means, any one of which may reduce the value to us, perhaps substantially, of any commercialization of bioscience products. There is no guarantee that we would be able to obtain such funding on terms acceptable to us or at all.

Stockholder approval is only one of the closing conditions. If the remaining closing conditions are not satisfied or waived, the sale might not be consummated, even if the stockholders approve the sale.

By completing the asset sale, we lose our historical revenue stream and become less diversified. By selling our water treatment division assets, we will be

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selling approximately 95% of our current source of revenue generation (based upon results from the July 31, 2003 fiscal year end). We will become a bioscience company focused on the marketing, selling and continued development of our Axenohl antimicrobial technology and our Triglycylboride pesticide technology. We may invest in other complementary technologies in the future, but we have no current specific plans to do so at this time. This transaction would increase our business risk because we will be less diversified than before the sale of the water treatment division assets and because our remaining business is in the relatively high-risk, but potentially high reward, field of applied biotechnology.

After the sale, we will become a biotechnology company in a highly regulated field with high investment costs and high risks. We currently have two pesticide products, RoachX and AntX and one antimicrobial product, Axen-30 hard surface disinfectant, being sold or ready for sale. We intend to fund and manage additional EPA regulated product development internally and in conjunction with current regulatory consultants, and we do not expect to be able to introduce additional EPA regulated antimicrobial products for several months. It may be several years before we are able to introduce any FDA regulated antimicrobial pharmaceutical products. To that end, we have partnered with Therapeutics, Inc., a California based drug development company, which has assumed responsibility for funding and managing the testing and regulatory process for potential FDA regulated Axenohl-based pharmaceutical products. The FDA and comparable agencies in many foreign countries impose substantial limitations on the introduction of new products through costly and time-consuming laboratory and clinical testing and other procedures. The process of obtaining FDA and other required regulatory approvals is lengthy, expensive and uncertain.

Even after we have invested substantial funds in further development of our Axenohl-based products and related technology, and even if the results of our efforts are favorable, there can be no guarantee that we will be granted necessary regulatory approvals.

If we successfully bring additional EPA or FDA regulated products to market, there is no assurance that we will be able to successfully manufacture or market the products or that potential customers will buy them, if for example, a competitive product has greater efficacy or is deemed more cost effective. In addition, the market in which we will sell any such products is dominated by a number of large, well-capitalized corporations, which may impact our ability to successfully market our products or maintain any technological advantage we might develop. We also would be subject to changes in regulations governing the manufacture and marketing of our products, which could increase our costs, reduce any competitive advantage we may have and/or adversely affect our marketing effectiveness.

Although the Company has no plans to continue to fund operations with additional private placements of stock, we may evaluate opportunities to sell additional equity or debt securities, or obtain credit facilities from lenders to strengthen our financial position. The sale of additional equity or convertible debt securities could result in additional dilution to our stockholders.

Our liquidity is unaffected by the financing program offered to participating dealers in the Nutripure water dealer program. We receive funds from our lender and disperse the funds to the dealer, less a commission charged by us, upon completion of the contract. The lender disperses funds to us. We record a liability when the funds are received and relief of liability when funds are dispersed, and we do not retain liability on the credit extended.

At October 31, 2003, our current assets to liabilities ratio increased from 0.27 to 1.06. Current assets increased \$2,011,900 from \$540,900 at July 31, 2003 to \$2,552,800 at October 31, 2003 due mainly to the acquisition of the \$2,035,000 Trust Deed discussed above. Current liabilities increased \$432,300 from

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\$1,974,200 to \$2,406,500. This increase was due mainly to the addition to notes payable of the \$435,000 note also mentioned above

Net fixed assets decreased approximately \$27,500 due mainly to depreciation of equipment. Noncurrent assets decreased approximately \$4,900 due to amortization. Non-current assets of \$2,489,500 consist almost entirely of Patents and Licenses.

Cash flows used from continuing operations were \$2,663,800 in quarter ended October 31, 2003 and \$211,500 in 2002. For fiscal 2003, cash flows used in investing activities included \$45,000 for the purchase of patents and licenses. In fiscal 2002 cash flows used in investing activities included \$8,900 for the purchase of machinery and equipment and \$4,700 for the purchase of patents and licenses.

Cash flows from financing activities were \$545,000 in fiscal 2003 and \$176,950 in fiscal 2002. During the quarter ended October 31, 2003 the Company conducted three private placements to three accredited investors in which it issued 950,000 shares of common stock at prices that range from \$0.50 to \$0.75 per share for a total of \$545,000. In the prior period, cash flows from financing activities included the addition of \$100,000 in loans payable from a line of credit renegotiated in September 2002 which was reclassified to long-term debt. Cash flows from financing activities in the prior period also included an increase of common stock of \$76,950 from the exercise of stock options.

COMMITMENTS

As a condition of the purchase agreement of the Axenohl patent, the Company agreed to make certain royalty payments to NVID of 5% of the gross product sales with a minimum royalty payment total of \$1,000,000 for the period from November 15, 2001 to July 31, 2004 and subsequently \$1,000,000 per year for the remaining life of the patent. The contract states that at July 31, 2004 the Company shall have the right, in its sole and absolute discretion, to do one of the following: a) pay the initial minimum royalty payment of \$1,000,000 in cash or common stock of the Company to NVID, less royalty amounts already paid, on or before July 31, 2004, b) transfer the patent back to NVID, at which time the Company would be released of any future minimum payments and granted a license to manufacture and distribute products covered by the patent while retaining all Axen and Axenohl related patents filed by the Company, including retention of all of its previously granted license rights to sell, distribute and manufacture all Axenohl based products, or c) cancel any royalty obligation under the contract by selling, transferring or assigning its ownership of the primary patent to a third party and paying NVID a percentage of the gross proceeds of 5% while retaining all Axen and Axenohl related patents filed by the Company, including retention of all of its previously granted license rights to sell, distribute and manufacture all Axenohl based products. The Company has not recorded or accrued an amount for the minimum royalty payments in the financial statements because the Company has determined that it is unlikely to choose the option to pay the minimum royalty.

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ITEM 3

CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure based closely on the definition of "disclosure

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controls and procedures" in Rule 13a-14(c). In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Within 90 days prior to the date of this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on the foregoing, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective.

There have been no significant changes in the Company's internal controls or in other factors that could significantly affect the internal controls subsequent to the date the Company completed its evaluation.

PART II OTHER INFORMATION, ITEM 1

LEGAL PROCEEDINGS

There have been no developments in the case involving PURE Bioscience and Zedburn Corporation et. al. in Circuit Court of Pinellas County, Florida as previously disclosed and incorporated by reference herein from Annual Report on Form 10KSB for fiscal year ended July 31, 2003.

There have been no developments in the case involving PURE Bioscience and Billy Stapleton and Susie Stapleton as previously disclosed and incorporated by reference herein from Annual Report on Form 10KSB for fiscal year ended July 31, 2003.

ITEM 2

CHANGES IN SECURITIES

On August 25, 2003, 60,000 shares of common stock were issued in exchange for attorneys fees incurred in connection with the acquisition of the Axenohl patent. Also in August 2003, the Company completed a financing arrangement with Next9 LLC which included the acquisition of a \$2,000,000 Trust Deed receivable and \$35,000 related accrued interest and issuing a \$435,000 note payable resulting in a net increase of \$1,600,000 in equity during the period. This note receivable was in exchange for the issuance of 2,000,000 shares of the Company's common stock to a party unrelated to the Company, and that is fully secured by specific assets other than the equity instruments granted. During the quarter we conducted three private placements to three accredited investors in which it issued 950,000 shares of common stock at prices that range from \$0.50 to \$0.75 per share for a total of \$545,000 with a weighted average price of \$0.57 per share.

With respect to the sales made, we relied on Section 4(2) of the Securities Act of 1933, as amended. No advertising or general solicitation was employed in offering the securities. The securities were offered solely to accredited or sophisticated investors who were provided all of the current public information available on PURE Bioscience.

ITEM 3.

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DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4.

SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

ITEM 5.

OTHER INFORMATION

Not applicable.

ITEM 6.

EXHIBITS AND REPORTS ON FORM 8-K

Exhibits

A. The following Exhibits are filed as part of this report pursuant to Item 601 of Regulation S-B:

- 3.1 (1) -- Articles of Incorporation, Articles of Amendment and Bylaws
 - 3.1.1(13) -- Articles of Amendment dated March 11, 2002
 - 4.1 (1) -- Form of Class A Warrant
 - 4.2 (1) -- Form of Class Z Warrant
 - 4.3 (1) -- Form of Common Stock Certificate
 - 4.4 (1) -- Warrant Agreement
 - 4.5 (2) -- March 2000 Warrant
 - 4.6 (3) -- January 2001 Warrant
 - 4.7 (4) -- Convertible Debenture
 - 4.8 (5) -- Convertible Debenture Purchase Agreement
 - 4.9 (6) -- Convertible Debenture Warrant
 - 10.1 (1) -- Employment Contract/Michael L. Krall
 - 10.2 (7) -- Manufacturing, Licensing and Distribution Agreement dated March 26, 2001
 - 10.3 (8) -- Axenohl License Agreement
 - 10.4 (9) -- Weaver - Roach X Assignment
 - 10.5 (9) -- Dodo Agreement [CONFIDENTIAL TREATMENT REQUESTED FOR CERTAIN OMITTED INFORMATION FILED SEPARATELY]
 - 10.6 (8) -- Promissory Note of Michael Krall
 - 10.7 (8) -- Promissory Note of Gary Brownell
 - 10.8 (9) -- Nutripure Dealer Agreement
 - 10.9 (9) -- Sales Finance Agreement
 - 10.10 (10) -- ETIH20, Inc., Acquisition Agreement
 - 10.11 (11) -- NVID Litigation Settlement Agreement
 - 10.12 (12) -- Addendum #1 to NVID Settlement Agreement
 - 13 (13) -- Subsidiaries of the Registrant
- (1) Incorporated by reference from Form SB-2 registration statement SEC File # 333-00434 effective August 8, 1996
- (2) Incorporated by reference from S-3 registration statement, SEC File #333-36248 effective on May 17, 2000
- (3) Incorporated by reference from S-3 registration statement, SEC File #333-55758 effective on February 26, 2001

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- (4) Incorporated by reference from S-3 registration statement, SEC File #333-61664 filed on May 25, 2001
- (5) Incorporated by reference from pre-effective amendment no. 1 to S-3 registration statement, SEC File #333-61664 filed on July 10, 2001
- (6) Incorporated by reference from pre-effective amendment no. 2 to S-3 registration statement, SEC File #333-61664 filed on August 13, 2001
- (7) Incorporated by reference from Current Report on Form 8-K filed on May 24, 2001 as amended on October 19, 2001
- (8) Incorporated by reference from the Amended Annual Report on Form 10KSB for the fiscal year ended July 31, 2000 filed on October 19, 2001
- (9) Incorporated by reference from Amended Form 10QSB for the nine month period ended April 30, 2001 filed on October 19, 2001
- (10) Incorporated by reference from the Amended Annual Report on Form 10KSB for the fiscal year ended July 31, 2001 filed on November 13, 2001
- (11) Incorporated by reference from Current Report on Form 8-K filed on December 6, 2001
- (12) Incorporated by reference from Amended Current Report on Form 8-K filed on December 7, 2001
- (13) Incorporated by reference from the Annual Report on Form 10KSB for the fiscal year ended July 31, 2002 filed on October 29, 2003

B. Reports on Form 8-K:

We filed a Form 8-K Current Report, Item 9, on August 20, 2003 and on August 23, 2003 which was amended on August 26, 2003..

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SIGNATURES

Pursuant to the requirement 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.

PURE BIOSCIENCE

By: /s/ Michael L. Krall

Michael L. Krall, President/CEO
December 12, 2003

By: /s/ Gary Brownell

Gary Brownell, Chief Financial Officer
December 12, 2003

