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

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934
For The Fiscal Year Ended December 31, 2010

Commission File Number: 0-31641

SCI ENGINEERED MATERIALS, INC.

(Exact name of registrant as specified in its charter)

Ohio	**31-1210318**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2839 Charter Street
Columbus, Ohio 43228
(Address of principal executive offices)

Registrant's telephone number, including area code: **(614) 486-0261**

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

Securities registered pursuant to Section 12(g) of the Act: Common Stock, without par value (Title of Class)

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

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the 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 at least the past 90 days.
Yes ☑ No ☐

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.
Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☑

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

The aggregate market value of the Registrant's common equity held by non-affiliates of the Registrant was approximately $9,612,062 on June 30, 2010**.** For purposes of this disclosure, shares of common stock held by persons who hold more than 10% of the outstanding shares of common stock and shares held by executive officers and directors of the registrant have been excluded because such persons may be deemed to be affiliates. This determination of executive officer or affiliate status is not necessarily a conclusive determination for other purposes.

There were 3,775,898 shares of the Registrant's Common Stock outstanding on February 21, 2011.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of our Proxy Statement for the 2011 Annual Meeting of Stockholders are incorporated by reference in Part III.

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Note Regarding Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 26A of the Securities Act of 1933, as amended. The words "anticipate," "believe," "expect," "estimate," and "project" and similar words and expressions identify forward-looking statements, which speak only as of the date hereof. Investors are cautioned that such statements involve risks and uncertainties that could cause actual results to differ materially from historical or anticipated results due to many factors, including, but not limited to, the factors discussed in "Risk Factors." The Company undertakes no obligation to publicly update or revise any forward-looking statements.

PART I

ITEM 1. BUSINESS

Introduction

SCI Engineered Materials, Inc. ("SCI", "we" or the "Company"), formerly Superconductive Components, Inc., an Ohio corporation, was incorporated in 1987. We operate in the physical vapor deposition industry in which we develop, commercialize technologies, and manufacture ceramics and metals for advanced applications in: Photonics, Solar, Thin Film Battery, Semiconductor, and, to a lesser extent High Temperature Superconductor ("HTS") materials. Photonics currently represents the largest market for our targets. Solar is an industry that is exhibiting rapid growth and we expect this market to grow quickly. Thin Film Battery is a developing market where manufacturers of batteries use our products to produce very small power supplies with small quantities of stored energy. Semiconductor is a developing market for us. In recent years we added to our sales staff for the purpose of focusing on opportunities for our products in the Solar industry. We also added staff to our Technology group for the development of innovative products.

History of the Company

The late Dr. Edward Funk, Sc.D., and his late wife Ingeborg founded SCI in 1987. Dr. Funk, formerly a Professor of Metallurgy at The Ohio State University and a successful entrepreneur, envisioned significant market potential for the newly discovered High Temperature Superconductivity (HTS) material YBCO (T_c of 90^o K). Our first product was a 99.999% pure, co-precipitated YBCO 1-2-3 powder. Over the years we expanded our product line by adding other High T_c Powders, sintered shapes, single crystal substrates, and non-superconducting sputtering targets.

We opened a subdivision, Target Materials Inc. (TMI), in 1991 to supply the increasing worldwide demand for sputtering and laser ablation targets. We became a full service manufacturer of high performance thin film materials, providing a wide selection of metals, ceramics, and alloys for sputtering targets, evaporation sources, and other Physical Vapor Deposition (PVD) applications. We served the R&D market as well as the Industrial and Decorative Coating markets. During this time, we began to manufacture targets for the Photovoltaic, Flat Panel Display, and Semiconductor industries.

SCI and TMI were merged in 2002. We continued to manufacture complex ceramic, metal, and alloy products for the photovoltaic, thin film battery, media storage, flat panel display, semiconductor, and photonic industries.

In April of 2010, we received ISO 9001:2008 registration, an internationally recognized quality standard. Prior to April 2010 we were ISO 9001:2000 registered.

Over the past two decades, we have developed considerable expertise in the development and ramp-up of manufacturing novel materials, such as Transparent Conductive Oxides for Thin Film Solar applications and targets for thin film batteries as well as Bismuth Strontium Calcium Copper Oxide (a superconductor powder). Today, we serve a diverse base of domestic and multi-national corporations, universities, and leading research institutions. We actively seek to partner with organizations to provide solutions for difficult material challenges.

Throughout our history, we have conducted funded research primarily under grants from entities such as the Department of Energy, the National Science Foundation, NASA, and the Ohio Department of Development. These activities are generally limited to funded research that is consistent with our focus on commercial applications in our principal markets.

Business

We are a supplier of materials to the Physical Vapor Deposition ("PVD") industry. Our customers need our materials to produce nano layers of metals and oxides for advanced material systems. PVD coatings range from every day items to complex computer processors. For example, every day applications include transparent anti-scratch coatings on eyeglasses, coatings on kitchen faucets, as well as low emissivity glass for household windows. More technically advanced applications of our product include semiconductors, thin film solar, flat panel displays and an emerging technology - Thin Film Battery.

We are focused on four distinct markets within the PVD industry. These markets are Photonics, Thin Film Solar, Thin Film Battery and Semiconductor. The Company continues to pursue niche opportunities, specifically for the Solar and semiconductor markets. We receive requests from potential customers in other markets within the PVD industry; however, at this time we have chosen not to pursue them. This disciplined approach enables us to focus on those opportunities that are the best fit for our capabilities and also offer the greatest long-term return. Considerations include our core strengths, resource requirements, and time-to-market.

The production and sale of High Temperature Superconductor materials was the initial focus of our operations and these materials continue to be part of our development efforts. We continue to work with private companies and government agencies to develop new and improved products for future applications; however, our principal business focus is on products positioned for near term commercialization.

Photonics currently represents the largest market for our materials. Our customers are continually identifying new materials that improve the utility of optical coatings. This includes improvements in their ability to focus, filter or reflect light, all of which increase the potential demand for the types and amounts of materials we sell in this market. Photonic applications continue to expand as new methods are found to manipulate light waves to enhance the various properties of light.

We have developed new products for the growing Thin Film Solar ("TFS") market. We are well positioned in the TFS area having supplied materials to that market for over 10 years from the early stages of TFS development. Since the beginning of 2007, we have added over $2.6 million of new manufacturing equipment, as well as Engineering and Sales staff to develop new materials to support the anticipated growth of Solar. We were awarded a grant of approximately $700,000 in 2008 and a second grant in 2009 for approximately $775,000 from the Ohio Department of Development to assist in the commercialization of TFS. Our new materials are Transparent Conductive Oxides ("TCO"). Every square foot of a TFS panel is coated with up to 3 layers of TCO, 1 micron thick. We continue to increase our visibility in the global arena by attending various trade shows targeted at the Solar market. In 2009 we added an exclusive representative for Korea and one for Taiwan and China. Commercialization and market expansion is expected to continue in 2011. We plan to add approximately $3 million in equipment and infrastructure improvements during the next two years to support this planned growth.

Thin Film Battery is a developing market where manufacturers of batteries use our targets, especially lithium orthophosphate (Li3PO4) and lithium cobalt oxide (LiCoO) as key elements to produce power supplies with small quantities of stored energy. A typical Thin Film Battery would be produced via PVD with five or more thin layers. These batteries are often one centimeter square but only 15 microns thick. Following several years of industry developments, some Thin Film Battery customers announced their batteries are commercially available. Our customers anticipate the unique properties of these batteries could be used in applications in medical devices, integrated circuits, RFID, smart cards, hand held electronics and many other applications.

We are still in the early stages of developing a market presence in the Semiconductor industry. We continue to develop innovative products for this industry. Thus far we have experienced some success and this market continues to hold significant potential for us. In 2008 we applied for a patent for products targeted at this market. The application was published in 2010 and is expected to be finalized by 2013.

We had total revenue of $8.9 million, $8.0 million, and $9.6 million during the years ended December 31, 2010, 2009, and 2008, respectively. Gross profit was $2.3 million, $1.9 million, and $2.2 million during the years ended December 31, 2010, 2009, and 2008, respectively. The increase in revenue in 2010 can be attributed to an increase in product volume due to an increase in customer demand. The reduction in revenue during 2009 was related to a high priced commodity that experienced a cyclical peak in 2007. This material returned to its long-term average during 2009, which reduced revenues in 2009 but had less of an effect on gross profit during that year.

Our largest customer represented approximately 27% of total revenues in 2010 and 25% in 2009. We had contract research revenue of $877,348 and $1,005,708 representing 9.8% and 12.6% of total revenue for the years ended December 31, 2010 and 2009, respectively.

Marketing and Sales

Europe and Asia have high demand for Solar and Semiconductor sputtering targets. Late in 2010 we added two non-exclusive distributors in Europe. In 2009 we significantly expanded our marketing reach into Asia continuing our efforts which began in 2008. We added a manufacturing representative for the Korean market for solar and another for the Taiwanese and Chinese markets for specialty glass coaters. We use various distribution channels to reach end user markets, including direct sales by our sales persons, independent manufacturers' representatives in the United States, and independent distributors and manufacturers' representatives for international markets. Also, the Internet provides tremendous reach for new customers to be able to identify us as a source of their product needs. We have an operating website www.sciengineeredmaterials.com, which includes expanded online product inquiry capabilities and additional product information.

Ceramics

We are capable of producing ceramic powders via several different processing techniques including solid state and precipitation. Ceramic targets can also be produced in a variety of ways depending on the end user applications. Production techniques include sintering, cold isostatic pressing and hot pressing.

Most of our products are manufactured from component chemicals and metal oxides supplied by various vendors. If we suddenly lost the services of a supplier, there could be a disruption in our manufacturing process until the supplier was replaced. We have identified several firms as potential back-up suppliers who would be capable of supplying these materials to us as necessary. To date, we have not experienced an interruption of raw material supply.

Metals

In addition to the ceramic targets previously mentioned, we produce metal sputtering targets and backing plates. The targets are bonded to the backing plates for application in the PVD industry. These targets can be produced by casting, hot pressing and machining of metals and metal alloys depending on the application.

Applications for metal targets are highly varied from applying decorative coatings for end uses such as sink faucets to the production of various electronic, photonic and semiconductor products.

We purchase various metals of reasonable high purity (often above 99.9%) for our applications. We are not dependent on a single source for these metals and do not believe losing a vendor would materially affect our business.

We have continually added production processes and testing equipment for the many product compositions that can be used as PVD materials.

Competition

We have a number of domestic and international competitors in both the ceramic and metal fields, many of whom have resources far in excess of our resources. Tosoh, Williams Advanced Materials, Kurt Lesker and Heraeus are competing suppliers in regard to targets. Dowa Chemicals of Japan supplies HTS materials.

Suppliers

Principal suppliers in 2010 were West Coast Quartz, MCP Metalspecialties, and Johnson Matthey. In every case, we believe that suitable alternate vendors can be used to ensure availability of required materials. As volume grows, we may enter into alliances or purchasing contracts with these or other vendors.

Research and Development

We are developing sputtering targets for semiconductor applications, which could be used to produce high K dielectric films via PVD processing. We are developing Transparent Conductive Oxide (TCO) and transparent dielectric materials for Thin Film Solar and wide area coating applications. We focus our research and development efforts in areas that build on our expertise in multi-component ceramic oxides. Contract research revenues were $877,348 during 2010 and $1,005,708 during 2009.

During the fourth quarter of 2009 we were notified we had been awarded a grant in the amount of $775,400 by the Ohio Department of Development's Third Frontier Photovoltaic Program (TFPVP) to commercialize advanced technology for high power density rotatable ceramic sputtering targets. These targets are used in the manufacture of thin film photovoltaics. This technology will enable manufacturers to operate rotatable sputtering targets at higher power densities than current technology. The approval of the grant was received during January 2010 and the work on the contract commenced in the first quarter of 2010. The work on the contract is expected to continue through the first quarter of 2012.

During the third quarter of 2009 we received notification from the Department of Energy (DOE) of an Assistance Agreement in the amount of approximately \$650,000. This grant provides support for Phase II of a Small Business Innovation Research (SBIR) award entitled “Homogenous BSCCO-2212 Round Wires for Very High Field Magnet Applications.” The work on the contract is expected to continue through August 2011.

We received notification during the fourth quarter of 2008 from the Ohio Department of Development’s Third Frontier Advanced Energy Program (TFAEP) of an award in the amount of \$708,715. This grant provides support to commercialize technologies for the manufacture of rotatable ceramic sputtering targets for the production of transparent conductive oxide-coated glass used in manufacturing thin film photovoltaic solar cell panels. The work on the contract began in January of 2009 and is expected to be completed during the first quarter of 2011.

During the third quarter of 2008 we received notification from the Department of Energy of a Notice of Financial Assistance Award in the amount of approximately \$750,000. This grant provides support for Phase II of a Small Business Innovation Research (SBIR) award entitled “Flux Pinning Additions to Increase Jc Performance in BSCCO-2212 Round Wire for Very High Field Magnets.” The work on the contract began during the third quarter of 2008 and is expected to be completed during the first quarter of 2011.

We intend to continue to seek funded research opportunities within our core competencies that maintain and expand technical understanding within our company.

We have certain proprietary knowledge and trade secrets related to the manufacture of ceramic oxide PVD materials and patents covering some HTS products.

New Product Initiatives

We continue to develop TCO target materials for the fast growing Thin Film Solar market in partnership with both original equipment manufacturers and Thin Film Solar Cell panel fabricators. Due to our flexibility in manufacturing both planar and rotatable target material designs, we are able to provide TCO compositions tailored to customer requests. In addition, we have obtained a grant from the Ohio Department of Development’s Third Frontier Advanced Energy Program (TFAEP) to aid us in the commercialization of our rotatable target production capabilities. The TFAEP grant will enable us to expedite the expansion of our rotatable target manufacturing capacity to meet anticipated customer demand.

We are exploring opportunities in the area of high dielectric constant (Hi-K) gate dielectrics for solid state memory applications. We have developed contacts within the R&D departments of several companies developing next generation memory products and have been supplying materials for their research efforts. We foresee the development of a market for these materials as devices continue to shrink in size.

We continue to pursue research and development opportunities with respect to new and innovative materials and processes to be used in connection with the production of Thin Film Batteries. Presently, there are approximately five manufacturers of Thin Film Batteries in the United States, each in various stages of development from prototype to commercial activity. In addition there are several firms and research institutes conducting tests on Thin Film Batteries. We believe this market may potentially become large with growth expected during the next two years. There are numerous applications for Thin Film Batteries, including, but not limited to, active RFID tags, battery on chip, portable electronics, medical implant devices, and remote sensors. Given the many potential uses for Thin Film Batteries, we anticipate that the market for materials it produces will grow in direct correlation to the Thin Film Battery market itself.

We currently face competition from other producers of materials used in connection with the manufacture of Thin Film Batteries. We believe that we have certain competitive advantages in terms of quality. We intend to actively market our materials to Thin Film Battery producers in the upcoming year in order to maintain our strong presence in this market.

Intellectual Property

We have received a patent for Fine-Particle Bi-Sr-Ca-Cu-O Having High Phase Purity made by a Chemical Precipitation and Low-Pressure Calcination method from the United States Patent and Trademark Office. We also have received a patent for a process to join two individual strongly linked super-conductors utilizing a melt processing technique.

At present, we have applied for a patent for the manufacture of a precious metal composite target that will significantly reduce the amount of precious metal required to produce such targets that are used in the semiconductor and photonics industries. We have several customers interested in this invention and are pursuing both domestic (US) and foreign coverage.

In the future, we may submit additional patent applications covering various applications, which have been developed by us. Because the publication of U.S. patent applications can be delayed for up to one year, they tend to lag behind actual discoveries and we may not be the first creator of inventions covered by pending patent applications or the first to file patent applications for such inventions. Additionally, other parties may independently develop similar technologies, duplicate our technologies or, if patents are issued to us or rights licensed by us, design around the patented aspects of any technologies we developed or licensed.

We rely on a combination of patent and trademark law, license agreements, internal procedures and nondisclosure agreements to protect our intellectual property. Unfortunately, these may be invalidated, circumvented or challenged. In addition, the laws of some foreign countries in which our products may be produced or sold may not protect our intellectual property rights to the same extent as the laws of the United States.

Employees

We had 26 full-time employees and one part-time employee as of December 31, 2010. One of these employees held a PhD in Material Science. We have never experienced a work stoppage and consider our relations with employees to be good. The employees do not have a bargaining unit.

Environmental Matters

We handle all materials according to Federal, State and Local environmental regulations and include Material Safety Data Sheets (MSDS) with all shipments to customers. We maintain a collection of MSDS sheets for all raw materials used in the manufacture of products and maintenance of equipment and insure that all personnel follow the handling instructions contained in the MSDS for each material. We contract with a reputable fully permitted hazardous waste disposal company to dispose of the small amount of hazardous waste materials generated.

Collections and Write-offs

We collected receivables in an average of 29 days in 2010. We have occasionally been forced to write-off negligible amount of accounts receivable as uncollectible. We consider credit management critical to our success.

Seasonal Trends

We have not experienced and do not expect to experience seasonal trends in future business operations.

ITEM 1A. RISK FACTORS

We desire to take advantage of the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. The following factors have affected or could affect actual results and could cause such results to differ materially from those expressed in any forward-looking statements made. Investors should consider carefully the following risks and speculative factors inherent in and affecting the business of SCI and an investment in our common stock.

We have limited marketing and sales capabilities.

In 2009 we expanded our marketing reach into Asia continuing our efforts which began in 2008. We also added a manufacturing representative for the Korean market and another for the Taiwanese and Chinese markets. In late 2008, we formed an exclusive relationship with a manufacturer’s representative in Europe, which we terminated in January 2010. As previously mentioned, we hired a full time sales engineer in 2007 to expand our marketing activities, especially in the solar area of the photonics market. We must continue to develop appropriate marketing, sales, technical, customer service and distribution capabilities, or enter into agreements with third parties to provide these services to successfully market our products. A failure to develop these capabilities or obtain third-party agreements could adversely affect us.

Our success depends on our ability to retain key management personnel.

Our success depends in large part on our ability to attract and retain highly qualified management, administrative, manufacturing, sales, and research and development personnel. Due to the specialized nature of our business, it may be difficult to locate and hire qualified personnel. The loss of services of one of our executive officers or other key personnel, or our failure to attract and retain other executive officers or key personnel could have a material adverse effect on our business, operating results and financial condition. Although we have been successful in planning for and retaining highly capable and qualified successor management in the past, there can be no assurance that we will be able to do so in the future.

Our competitors have far greater financial and other resources than we have.

The market for Physical Vapor Deposition materials is a substantial market with significant competition in both ceramic and metal materials. While we believe that our products enjoy certain competitive advantages in design, function, quality, and availability, considerable competition exists from well-established firms such as Williams Advanced Materials, Kurt Lesker, Heraeus and Tosoh, all of which have more financial resources than us. We cannot provide assurance that developments by others will not render our products or technologies obsolete or less competitive.

Our revenues depend on patents and proprietary rights that may not be enforceable.

We rely on a combination of patent and trademark law, license agreements, internal procedures and nondisclosure agreements to protect our intellectual property. These may be invalidated, circumvented or challenged. In addition, the laws of some foreign countries in which our products may be produced or sold may not protect our intellectual property rights to the same extent as the laws of the United States. Our failure to protect our proprietary information could adversely affect us.

Rights we have to patents and pending patent applications may be challenged.

We have received, from the United States Patent and Trademark Office, a patent for Fine-Particle Bi-Sr-Ca-Cu-O Having High Phase Purity made by a Chemical Precipitation and Low-Pressure Calcination method, and have also received a patent for a process to join two individual strongly linked super-conductors utilizing a melt processing technique. We have applied for a patent for the manufacture of a precious metal composite target that will significantly reduce the amount of precious metal required to produce such targets that are used in the semiconductor and photonics industries. We have several customers interested in this invention and are pursuing both domestic (US) and foreign coverage. In the future, we may submit additional patent applications covering various applications. The patent application we filed and patent applications that we may file in the future may not result in patents being issued, and any patents issued may not afford meaningful protection against competitors with similar technology, and may be challenged by third parties.

Because U.S. patent applications are maintained in secret until patents are issued, and because publications of discoveries in the scientific or patent literature tend to lag behind actual discoveries by several months, we may not be the first creator of inventions covered by issued patents or pending patent applications or the first to file patent applications for such inventions. Moreover, other parties may independently develop similar technologies, duplicate our technologies or, if patents are issued to us or rights licensed by us, design around the patented aspects of any technologies we developed or licensed. We may have to participate in interference proceedings declared by the U.S. Patent and Trademark Office to determine the priority of inventions, which could result in substantial costs. Litigation may also be necessary to enforce any patents held by or issued to us or to determine the scope and validity of others' proprietary rights, which could result in substantial costs.

The rapid technological changes of our industry may adversely affect us if we do not keep pace with advancing technology.

The Physical Vapor Deposition market is characterized by rapidly advancing technology. Our success depends on our ability to keep pace with advancing technology and processes and industry standards. We have focused our development efforts on sputtering targets. We intend to continue to develop and integrate advances in the thin film coatings industry. However, our development efforts may be rendered obsolete by research efforts and technological advances made by others, and materials other than those we currently use may prove more advantageous.

Additional development of our products may be necessary due to uncertainty regarding development of markets.

Some of our products are in the early stages of commercialization and we believe that it will be several years before these products will have significant commercial end-use applications, and that significant additional development work may be necessary to improve the commercial feasibility and acceptance of these products. There can be no assurance that we will be able to commercialize any of the products currently under development.

To date, there has been no widespread commercial use of High Temperature Superconductive (HTS) products. Additionally, the market for the Thin Film Battery materials is still in its early stages. At present, we have several customers for the materials we produce for Thin Film Batteries. Since we have begun producing materials for the Thin Film Battery market, we have experienced no problems securing the supplies needed to produce the materials. We do not anticipate supply problems in the near future. However, changes in production methods and advancing technologies could render our current products obsolete and new production protocols may require supplies that are less available in the marketplace, which may cause a slowing or complete halt to production as well as expanding costs which we may or may not be able to pass on to our customers. Some of our materials are in early stages of development for Thin Film Solar applications. The Thin Film Solar market is expected to grow significantly during the next few years.

The market for our common stock is limited, and as such our shareholders may have difficulty reselling their shares when desired or at attractive market prices.

Our stock price and our listing may make it more difficult for our shareholders to resell shares when desired or at attractive prices. In 2001, our stock began trading on The Over the Counter Bulletin Board ("OTC Bulletin Board"). Nevertheless, our common stock has continued to trade in low volumes and at low prices. Some investors view low-priced stocks as unduly speculative and therefore not appropriate candidates for investment. Many institutional investors have internal policies prohibiting the purchase or maintenance of positions in low-priced stocks. This has the effect of limiting the pool of potential purchases of our common stock at present price levels. Shareholders may find greater percentage spreads between bid and asked prices, and more difficulty in completing transactions and higher transaction costs when buying or selling our common stock than they would if our stock were listed on a major stock exchange, such as The New York Stock Exchange or The Nasdaq National Market.

Our common stock has been subject to the Securities and Exchange Commission's "penny stock" regulations, which may limit the liquidity of common stock held by our shareholders.

At the present time, our common stock trades on the OTC Bulletin Board. Based on its trading price, our common stock is considered a "penny stock" for purposes of federal securities laws, and therefore has been subject to regulations, which affected the ability of broker-dealers to sell our securities. Broker-dealers who recommend a "penny stock" to persons (other than established customers and accredited investors) must make a special written suitability determination and receive the purchaser's written agreement to a transaction prior to sale.

If penny stock regulations apply to our common stock, it may be difficult to trade the stock because compliance with the regulations can delay and/or preclude certain trading transactions. Broker-dealers may be discouraged from effecting transactions in common stock because of the sales practice and disclosure requirements for penny stock. This could adversely affect the liquidity and/or price of our common stock, and impede the sale of the common stock in the secondary market.

Our Articles of Incorporation authorize us to issue additional shares of stock.

We are authorized to issue up to 15,000,000 shares of common stock, which may be issued by our board of directors for such consideration, as they may consider sufficient without seeking shareholder approval. The issuance of additional shares of common stock in the future may reduce the proportionate ownership and voting power of current shareholders.

Our Articles of Incorporation authorize us to issue up to 260,000 shares of preferred stock. The issuance of preferred stock in the future could create additional securities which would have dividend and liquidation preferences prior in right to the outstanding shares of common stock. These provisions could also impede a non-negotiated change in control.

We have not paid dividends on our common stock in the past and do not expect to do so in the future.

We have never paid dividends on our common shares in the past and do not expect to do so in the foreseeable future. We intend to retain future earnings for use in the business.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

Not applicable.

ITEM 2. PROPERTIES.

Our office and manufacturing facilities are located at 2839 Charter Street, Columbus, Ohio, where we occupy approximately 32,000 square feet. We moved our operations into this facility in 2004. The lease on the property expires on August 16, 2014. We believe these facilities are in good condition and will be adequate for our needs for the immediate future. We anticipate the need for additional manufacturing and warehouse space in 2012.

We are current on all operating lease liabilities.

ITEM 3. LEGAL PROCEEDINGS.

Not applicable.

ITEM 4. (REMOVED AND RESERVED)

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Market for Common Stock

Our common stock currently trades on the OTC Bulletin Board under the symbol "SCIA." The following table sets forth for the periods indicated the high and low bid quotations for our common stock.

	High	Low
Fiscal 2010		
Quarter Ended March 31, 2010	$ 3.50	$ 2.75
Quarter Ended June 30, 2010	3.50	2.65
Quarter Ended September 30, 2010	4.00	2.65
Quarter Ended December 31, 2010	3.40	1.07
Fiscal 2009		
Quarter Ended March 31, 2009	$ 6.00	$ 2.75
Quarter Ended June 30, 2009	3.50	2.60
Quarter Ended September 30, 2009	3.80	1.75
Quarter Ended December 31, 2009	3.75	2.00

The quotations provided herein may reflect inter-dealer prices without retail mark-up, markdown, or commissions, and may not represent actual transactions.

As discussed above, at the present time, our common stock trades on the OTC Bulletin Board. Based on its trading price, our common stock is considered a "penny stock" for purposes of federal securities laws, and therefore has been subject to certain regulations, which are summarized below.

Our common stock is classified as a penny stock and as such, broker dealers trading our common stock will be subject to the disclosure rules for transactions involving penny stocks, which require the broker dealer to determine if purchasing our common stock is suitable for a particular investor. The broker dealer must also obtain the written consent of purchasers to purchase our common stock. The broker dealer must also disclose the best bid and offer prices available for our stock and the price at which the broker dealer last purchased or sold our common stock. These additional burdens imposed on broker dealers may discourage them from effecting transactions in our common stock, which could make it difficult for an investor to sell their shares.

Holders of Record

As of December 31, 2010, there were approximately 460 holders of record of our common stock and 3,775,898 shares outstanding. There were approximately 50 holders of Series B Preferred shares and as of December 31, 2010 there were 24,152 shares outstanding.

Dividends

We have never paid cash dividends on our common stock and do not expect to pay any dividends in the foreseeable future. We intend to retain future earnings for use in the business.

Equity Compensation Plan Information

The following table sets forth additional information as of December 31, 2010, concerning shares of our common stock that may be issued upon the exercise of options, warrants and rights under our existing equity compensation plans and arrangements, divided between plans approved by our shareholders and plans or arrangements not submitted to the shareholders for approval. The information includes the number of shares covered by, and the weighted average exercise price of, outstanding options and other rights and the number of shares remaining available for future grants excluding the shares to be issued upon exercise of outstanding options, warrants, and other rights.

	Number of Securities to be issued upon exercise of outstanding options, warrants and rights *(a)*	Weighted-average exercise price of outstanding options, warrants and rights *(b)*	Number of securities remaining available for issuance under equity compensation plans (excluding securities reflected in column (a)) *(c)*
Equity compensation plans approved by security holders [1]	1,066,250	$ 4.15	14,500

(1) Equity compensation plans approved by shareholders include our 1995 Stock Option Plan and 2006 Stock Option Plan.

ITEM 6. SELECTED FINANCIAL DATA.

Not applicable.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATION.

Overview

SCI Engineered Materials, Inc. ("SCI", "we" or the "Company"), formerly Superconductive Components, Inc., an Ohio corporation, was incorporated in 1987. We develop, commercialize technologies and manufacture ceramics and metals for advanced applications in the physical vapor deposition industry including: Photonics, Solar, Thin Film Battery, Semiconductor, and, to a lesser extent HTS materials. Photonics currently represents the largest market for our targets. Solar is an industry that is exhibiting rapid growth and we expect this market to grow quickly. Thin Film Battery is a developing market where manufacturers of batteries use our products to produce very small power supplies with small quantities of stored energy. Semiconductor is a developing market for us. In recent years we added to our sales staff for the purpose of focusing on opportunities for our products in the Solar industry. We also added staff to our Technology group for the development of innovative products.

Executive Summary

During 2010, we generated approximately $561,000 in cash from operations, invested over $225,000 of cash in new equipment, leased an additional $193,000 of equipment and paid $452,000 of principle towards outstanding debt.

In the past three years (2008 – 2010) we have invested over $1.6 million in new equipment to increase our manufacturing capacity and advanced test equipment to position the company to become a meaningful supplier of Zinc Oxide based Transparent Conductive Oxides (TCO) for the Thin Film Solar (TFS) Industry. The solar industry is projected to have strong growth for the next few decades; in addition TFS market share is expected to increase during that period.

During February 2011 we positioned the company for continued growth as two loans with Agencies of the State of Ohio for approximately $2.1 million were finalized. These loans carry attractive interest rates of 3.25%. In addition, we expect to invest an additional $900,000 in the expansion project and to add approximately 50 jobs during the next three years.

For the year ended December 31, 2010, we had total revenue of $8,916,122. This was an increase of $905,887, or 11.3% when compared to 2009. The increase in revenue can be attributed to an increase in product volume due to an increase in customer demand. Product revenue increased $1,034,247 or 14.8%, for the year ended December 31, 2010 from the same period in 2009. The revenue during 2010 and 2009 included a high priced commodity that experienced a cyclical peak in 2007 and returned to its long-term average during 2009. Should this material fluctuate in cost in the future it could have an effect on revenue but less of an effect on gross profit due to the low margin. Contract research revenue decreased to $877,348 during 2010 from $1,005,708 during 2009, a decrease of $128,360, or 12.8%, as one of the grants drew to a close in the fourth quarter of 2010. We received notification in January 2011 that one of our large customers will be closing its manufacturing plant during the first quarter of 2011. We have collected all outstanding accounts receivable from this customer at December 31, 2010. This customer placed an additional order with us for approximately $700,000 in November 2010 with releases scheduled during the first half of 2011. We expect to ship approximately $450,000 against this order in the first quarter of 2011. Revenue from this customer was approximately $1.9 million in 2010. Our 2011 plans include increased sales of solar products, especially our innovative transparent conductive oxide systems for the solar industry. The anticipated sales growth is based on revenue from new customers, current product trials being converted into production orders, and increased bookings from core customers in other markets. We expect sales to these customers to offset the loss of revenue from this customer.

Gross profit was $2,273,984 for year ended December 31, 2010 compared to $1,869,879 for 2009, an increase of 21.6%. This increase in gross profit can be attributed to the increase in product volume. Gross profit in 2010 was reduced by scale-up expenses of approximately $71,000 which were incurred late in the year. Gross margin was 25.5% of total revenue for 2010 compared to 23.3% in 2009. The increase was due to increased volume and product mix.

Income from operations increased $409,933 to $79,895 for the year ended December 31, 2010 compared with 2009. Loss applicable to common shares was ($7,229) for the year ended December 31, 2010 compared to a loss of ($521,649) for the year ended December 31, 2009. The increase was due to the greater gross profit related to the increase in product volume as well as a reduction in non-cash stock compensation expense. For the year ended December 31, 2010, we had $203,403 in non-cash stock compensation expenses compared to $457,417 for the year ended December 31, 2009, a decrease of $254,014, or 55.5%. These charges had a material effect on our Statement of Operations in 2010 and 2009. These ongoing non-cash charges will continue to decline in 2011. Scale-up expenses of approximately $71,000 were incurred late in 2010 which had an effect on the loss applicable to common shares for the year ended December 31, 2010.

Given current market opportunities, we continue to invest in expanding production, research and development, marketing, and sales. This has resulted in trial and qualification orders that were shipped to customers in the solar industry throughout 2010 and 2009. This should allow us to gain market share and to be poised to receive large orders in targeted applications.

Results of Operations

Critical Accounting Policies

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States requires management to make judgments, assumptions and estimates that affect the amounts reported in the Financial Statements and accompanying notes. Note 2 to the Financial Statements in the Annual Report on Form 10-K for the year ended December 31, 2010 describes the significant accounting policies and methods used in the preparation of the Financial Statements. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventory allowances, property and equipment depreciable lives, patents and licenses useful lives and assessing changes in which impairment of certain long-lived assets may occur. Actual results could differ from these estimates. The following critical accounting policies are impacted significantly by judgments, assumptions and estimates used in the preparation of the Financial Statements. The allowance for doubtful accounts is based on our assessment of the collectability of specific customer accounts and the aging of the accounts receivable. If there is a deterioration of a major customer’s credit worthiness or actual defaults are higher than our historical experience, our estimates of the recoverability of amounts due us could be adversely affected. Inventory purchases and commitments are based upon future demand forecasts. If there is a sudden and significant decrease in demand for our products or there is a higher risk of inventory obsolescence because of rapidly changing technology and customer requirements, we may be required to increase our inventory allowances and our gross margin could be adversely affected. Depreciable and useful lives estimated for property and equipment, licenses and patents are based on initial expectations of the period of time these assets and intangibles will provide benefit. Changes in circumstances related to a change in our business, change in technology or other factors could result in these assets becoming impaired, which could adversely affect the value of these assets.

Year 2010 As Compared to Year 2009

Revenue

Total revenue was $8,916,122 in 2010, an increase of $905,887, or 11.3%, from 2009. The increase in revenue can be attributed to an increase in product volume due to customer demand. Product revenue increased $1,034,247 or 14.8%, for the year ended December 31, 2010 from the same period in 2009. Contract research revenue decreased to $877,348 for 2010 from $1,005,708 for 2009, a decrease of $128,360, or 12.8%, as one of the grants drew to a close in the fourth quarter of 2010.

Revenue from product sales is recognized upon shipment to customers. Provisions for discounts and rework costs for returns are established when products are shipped based on historical experience. Customer deposits represent cash received in advance of revenue earned.

Revenue from contract research provided for third parties is recognized on the percentage of completion method. Contract research revenue is recognized during the period qualifying expenses are incurred for the research that is performed as set forth under the terms of the grant award agreements.

Gross Profit/Margin

Gross profit was $2,273,984 for year ended December 31, 2010 compared to $1,869,879 for 2009, an increase of 21.6%. This increase in gross profit can be attributed to the increase in product revenue as well as product mix. Gross margin was 25.5% of total revenue for the year ended December 31, 2010. This was higher due to increased product volume and product mix compared to 23.3% for the year ended December 31, 2009. Gross profit in 2010 was reduced by approximately $71,000 of scale-up expenses which were incurred late in the year.

General and Administrative Expense

General and administrative expense for the year ended December 31, 2010 decreased to $1,128,644 from $1,237,672 for the year ended December 31, 2009, or 8.8%. The decrease was the result of less non-cash stock based compensation of approximately $128,000 and less expense related to Sarbanes-Oxley compliance of approximately $58,000. Wages increased approximately $40,000 in 2010 primarily as a result of the reinstatement of wage cuts implemented during 2009.

Professional Fees

Included in General and Administrative expense was $197,651 and $249,341 for professional fees for the years ended December 31, 2010 and 2009, respectively. The increase in SEC compliance costs of legal, accounting and stockholder relations fees were offset by a decrease in expense related to Sarbanes-Oxley compliance.

Research and Development Expense

Research and development expense for the year ended December 31, 2010 was $442,214 compared to $314,386 for the same period in 2009, an increase of 40.7%. We continue to develop innovative transparent conductive oxide systems to further align our activities with customer needs, as well as trial orders which resulted in increased research and development expense. These new research and development endeavors have moved us beyond the scope of our current federal and state grants and awards.

Marketing and Sales Expense

Marketing and Sales expense for the year ended December 31, 2010 decreased 3.8% to $623,231 from $647,859 for the same period in 2009. The decrease was primarily due to less non-cash stock based compensation expense of approximately $21,000 as well as less compensation and benefits expense of approximately $21,000. These lower expenses were partially offset by increased commissions to our outside manufacturing sales representatives of approximately $29,000.

Stock Compensation Expense

Included in operating expenses were non cash stock based compensation costs of $198,093 and $375,719 for the years ended December 31, 2010 and 2009, respectively.   Compensation cost for all stock-based awards is based on the grant date fair value and recognized over the required service (vesting) period. Unrecognized non cash stock based compensation expense was $724,842 as of December 31, 2010 and will be recognized through 2017.

Interest Expense

Interest expense was $85,643 and $108,712 for the years ended December 31, 2010 and 2009, respectively. These decreases were due to the maturity of some capital leases plus more principal and less interest being applied to ongoing capital lease payments.

Income Tax Benefit

Income tax benefit for the years ended December 31, 2010 and December 31, 2009 was ($9,133) and ($59,000) respectively.   A deferred tax benefit of $156,000 and a current expense of $97,000 were recorded in 2009. We record a valuation allowance to reduce our deferred tax asset to an amount that is more likely than not to be realized. While we have considered future taxable income and used ongoing prudent and feasible tax planning strategies in assessing the need for valuation allowances, if we were to determine that we would be able to realize deferred tax assets in the future in excess of the recorded amount, an adjustment to the deferred tax asset would increase income in the period that such determination was made. Likewise, should we determine that we would not be able to realize all or part of the deferred tax asset in the future, an adjustment to the deferred tax asset would decrease income in the period such determination was made. We regularly evaluate the need for a valuation allowance against our deferred tax asset.

Loss Applicable to Common Shares

Loss applicable to common shares was ($7,229) for the year ended December 31, 2010 compared to a loss of ($521,649) for the year ended December 31, 2009. The improvement was due to greater product revenue and gross profit related to the increase in product volume as well as a reduction in non-cash stock compensation expense.

Common Shares

The following schedule represents our outstanding common shares during the period of 2011 through 2019 assuming all outstanding stock options are exercised during the year of expiration. If each shareholder exercises his or her options, it would increase our common shares by 1,066,250 to 4,842,148 by December 31, 2019. Assuming all such options are exercised in the year of expiration, the effect on shares outstanding is illustrated as follows:

Year	Options due to expire	Potential shares outstanding	Weighted Average Exercise Price
2011	62,500	3,838,398	$ 1.68
2012	158,000	3,996,398	$ 1.55
2013	30,250	4,026,648	$ 1.00
2014	180,000	4,206,648	$ 4.36
2015	140,000	4,346,648	$ 2.97
2016	36,000	4,382,648	$ 3.25
2017	-	4,382,648	-
2018	9,500	4,392,148	$ 3.10
2019	450,000	4,842,148	$ 6.00

Liquidity and Capital Resources

Cash

As of December 31, 2010, cash on-hand was $1,511,752. We believe, based on forecasted sales and expenses, that funding will be adequate to sustain operations at least through December 31, 2011.

Working Capital

At December 31, 2010, working capital was $2,037,193 compared to $1,555,897 at December 31, 2009, an increase of $481,296, or 30.9%. Inventories increased approximately $313,000 while prepaid expenses decreased approximately $926,000. The increase in inventories was due to materials received late in December to be used for blanket orders during 2011. The decrease in prepaid expenses was due to prepaid purchase orders from 2009 for items received in 2010. Accounts payable increased approximately $310,000 at December 31, 2010 due to the receipt of inventory late in December as previously mentioned. Customer deposits decreased approximately $953,000 during 2010 due to deposits received in 2009 that were applied to customer shipments in 2010.

Cash from Operations

Net cash provided by operating activities was approximately $561,000 and $262,000 for the years ended December 31, 2010 and 2009, respectively. In addition to the changes in various current assets and liabilities mentioned above, non cash expenses for depreciation, accretion and amortization increased to approximately $491,000 during 2010 from $447,000 during 2009, an increase of 9.9%. This increase is related to the purchase of additional machinery and equipment. Included in expenses were non cash stock based compensation costs of $203,403 and $381,030 for the years ended December 31, 2010 and 2009, respectively.

Cash from Investing Activities

Cash of approximately $215,000 and $168,000 was used for investing activities for the years ended December 31, 2010 and 2009, respectively. The amounts invested were used to purchase machinery and equipment for increased production capacity and new product lines. Proceeds on sale of equipment totaled $10,500 and $0 during 2010 and 2009, respectively.

Cash from Financing Activities

Cash of approximately $58,000 was provided by financing activities for the year ended December 31, 2010. Principal payments to third parties for capital lease obligations and a note payable approximated $452,000. Net proceeds received from the exercise of common stock warrants were $490,799. Proceeds received from the exercise of common stock options were $19,175. We incurred new capital lease obligations of approximately $193,000 for new production equipment during 2010.

During the year ended December 31, 2009 cash of approximately $385,000 was used for financing activities. Principal payments to third parties for capital lease obligations approximated $382,000. Proceeds received from the exercise of common stock options were $21,206. Payments related to Series B Preferred stock dividends were $24,430. We incurred new capital lease obligations of approximately $556,000 for new production equipment during 2009.

Debt Facilities

We have the ability to draw on a Revolving Note from The Huntington National Bank. The principal amount of the Revolving Note is $500,000. As of December 31, 2010 there was no outstanding balance on the Revolving Note.

We now have the ability to draw on a Promissory Note from The Huntington National Bank. The principal amount of the Note is $840,000. The date of this note was January 6, 2011 and thus, as of December 31, 2010 there was no outstanding balance on the Note.

Closing documents were signed in February 2011 for a 166 Direct Loan in the amount of $744,250 with the Ohio Department of Development (ODOD). ODOD also recommended that the Ohio Tax Credit Authority approve a tax credit equal to 45 percent of employee income tax withholdings resulting from the project for five years. This credit has an estimated value of $86,000 during the entire term. ODOD also is prepared to offer funding from the Rapid Outreach Grant for up to $25,000 for costs associated with the acquisition and installation of machinery and equipment.

Closing documents were also signed in February 2011 for a 166 Direct Loan through the Advanced Energy Program with The Ohio Air Quality Development Authority (OAQDA) for approximately $1.4 million. The OAQDA and ODOD loans can fund approximately 70% of the current capital requirements of approximately $3 million to support our planned growth.

Debt Outstanding

Total debt outstanding decreased during 2010 from approximately $1,482,000 to $1,223,000, or 17.5%. We paid cash of approximately $452,000 towards capital lease obligations and incurred new capital leases for additional production equipment of approximately $193,000 during 2010.

Government Grants and Contracts

During the fourth quarter of 2009 we were notified we had been awarded a grant in the amount of $775,400 by the Ohio Department of Development's Third Frontier Photovoltaic Program (TFPVP) to commercialize advanced technology for high power density rotatable ceramic sputtering targets. These targets are used in the manufacture of thin film photovoltaics. This technology will enable manufacturers to operate rotatable sputtering targets at higher power densities than current technology. The approval of the grant was received during January 2010 and the work on the contract commenced in the first quarter of 2010. Revenue totaled $145,736 during 2010. The work on the contract is expected to continue through the first quarter of 2012.

During the third quarter of 2009 we received notification from the Department of Energy (DOE) of an Assistance Agreement in the amount of approximately $650,000. This grant provides support for Phase II of a Small Business Innovation Research (SBIR) award entitled "Homogenous BSCCO-2212 Round Wires for Very High Field Magnet Applications." Total revenue of the project through December 31, 2010 was $350,947. Revenue was $234,729 during 2010 and $116,218 during 2009. The work on the contract is expected to continue through August 2011.

We received notification during the fourth quarter of 2008 from the Ohio Department of Development's Third Frontier Advanced Energy Program (TFAEP) of an award in the amount of $708,715. This grant provides support to commercialize technologies for the manufacture of rotatable ceramic sputtering targets for the production of transparent conductive oxide-coated glass used in manufacturing thin film photovoltaic solar cell panels. Total revenue of the project through December 31, 2010 was $708,715. Revenue was $278,613 during 2010 and $430,102 during 2009. The work on the contract began in January of 2009 and was completed late in 2010.

During the third quarter of 2008 we received notification from the Department of Energy of a Notice of Financial Assistance Award in the amount of approximately $750,000. This grant provides support for Phase II of a Small Business Innovation Research (SBIR) award entitled "Flux Pinning Additions to Increase Jc Performance in BSCCO-2212 Round Wire for Very High Field Magnets." Total revenue of the project through December 31, 2010 was $689,919. Revenue was $216,402 during 2010 and $423,340 during 2009. The work on the contract began during the third quarter of 2008 and is expected to continue through the first quarter of 2011.

The granting agency may suspend or terminate the award in whole or in part if we fail to materially comply with the terms and conditions. We expect to complete each award while complying with the terms and conditions.

Inflation

We believe that there has not been a significant impact from inflation on our operations during the past three fiscal years.

Purchase Commitments

We plan to continue to place some of our larger purchase commitments for raw materials on an annualized basis because they can be purchased in larger quantities at reduced prices. In general, we attempt to limit inventory price increases by making an annual commitment, and drawing the material either as required, or on a monthly or quarterly basis. Individual annual commitments may reach $500,000 in 2011 and greater in 2012 depending on sales volume increases. The terms of payment for such commitments are worked out with the vendor on a case-by-case basis, but in all cases are cancelable at our discretion without penalty.

Safe Harbor Statement under the Private Securities Litigation Reform Act of 1995

This document contains forward-looking statements that reflect the views of management with respect to future events and financial performance. These forward-looking statements are subject to certain uncertainties and other factors that could cause actual results to differ materially from such statements. See “Risk Factors” above. These uncertainties and other factors include, but are not limited to, the words “anticipates,” “believes,” “estimates,” “expects,” “plans,” “projects,” “targets” and similar expressions which identify forward-looking statements. You should not place undue reliance on these forward-looking statements, which speak only as of the date the statements were made. We undertake no obligation to publicly update or revise any forward-looking statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Our balance sheets as of December 31, 2010 and 2009, and the related statements of operations, shareholders’ equity and cash flows for the years ended December 31, 2010 and 2009, together with the independent certified public accountants’ report thereon appear beginning on Page F-1.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

The Audit Committee of the Board of Directors (the "Audit Committee") of SCI Engineered Materials, Inc. conducted a competitive process to select a firm to serve as the Company's independent registered public accounting firm for the year ending December 31, 2010. The Audit Committee invited several firms to participate in this process.

As a result of this process and following careful deliberation, effective May 10, 2010, the Audit Committee approved the engagement of Crowe Horwath LLP ("Crowe") as the Company's independent registered public accounting firm for the year ended December 31, 2010. The Audit Committee also informed Maloney + Novotny LLC that it was dismissed as the Company’s independent registered public accounting firm effective May 10, 2010.

Maloney + Novotny's audit reports on the Company's consolidated financial statements as of and for the years ended December 31, 2009 and 2008, did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope or accounting principles.

During the years ended December 31, 2009 and 2008, and in the subsequent interim period through May 10, 2010, there were (i) no disagreements between the Company and Maloney + Novotny on any matter of accounting principles or practices, financial statement disclosure or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Maloney + Novotny, would have caused Maloney + Novotny to make reference to the subject matter of the disagreement in their reports on the financial statements for such years, and (ii) no "reportable events" as that term is defined in Item 304(a)(1)(v) of Regulation S-K.

The Company provided Maloney + Novotny with a copy of the disclosures it made on Form 8-K (the "Report") prior to the time the Report was filed with the Securities and Exchange Commission (the "SEC").

The Company requested that Maloney + Novotny furnish a letter addressed to the SEC stating whether or not it agrees with the statements made herein. Maloney + Novotny's letter dated May 12, 2010 confirmed its agreement.

In deciding to engage Crowe, the Audit Committee reviewed auditor independence and existing commercial relationships with Crowe, and concluded that Crowe had no commercial relationship with the Company that would impair its independence. During the years ended December 31, 2009, and 2008, and in the subsequent interim period through May 10, 2010 neither the Company nor anyone acting on its behalf had consulted with Crowe on any of the matters or events set forth in Item 304 (a)(2) of Regulation S-K.

ITEM 9A. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of the Company's Principal Executive Officer and Principal Accounting Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving the desired control objectives and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Due to a segregation of duties material weakness described below, and based on this evaluation, the Company's Principal Executive Officer and Principal Accounting Officer have concluded that as of December 31, 2010, the Company's disclosure controls and procedures were not effective, at the reasonable assurance level, in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act and in ensuring that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including the Principal Executive Officer and Principal Accounting Officer, as appropriate to allow timely discussions regarding required disclosure. Until we are able to hire additional employees, we will continue to report to the Audit Committee and the Board of Directors at least monthly (and more often as necessary). We believe this will continue to mitigate this weakness. This reporting includes balance sheets, statements of operations, statements of cash flows, and other detail supporting these statements. Accordingly, we believe that the financial statements included in this report fairly present, in all material respects, our financial condition, results of operation, changes in shareholder's equity and cash flows for all periods presented.

Inherent Limitations Over Internal Controls

Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. Our internal control over financial reporting includes those policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of our assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of assets that could have a material effect on the financial statements.

Management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our internal controls will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of internal controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected. Also, any evaluation of the effectiveness of controls in future periods are subject to the risk that those internal controls may become inadequate because of changes in business conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management's Annual Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934, as amended). Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the criteria set forth in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on this evaluation, management has concluded that our internal control over financial reporting was not effective as of December 31, 2010. The matter involving internal controls over financial reporting that management considered to be a material weakness under the standards of the Public Company Accounting Oversight Board (PCAOB) was insufficient segregation of duties consistent with control objectives. Management is aware of the risks associated with the lack of segregation of duties due to the small number of employees currently working with general administrative and financial matters. Due to our size and nature, segregation of all conflicting duties may not always be possible and may not be economically feasible. However, to the extent possible, the initiation of transactions, the custody of assets and the recording of transactions should be performed by separate individuals.

In order to remediate this weakness, we will need to hire additional employees. Although we will periodically reevaluate this situation, at this point we consider that the risks associated with such lack of segregation of duties and the potential benefits of adding employees to segregate such duties are not cost justified. Until we are able to hire additional employees, we will continue to report to the Audit Committee and the Board of Directors at least monthly (and more often as necessary). We believe this will continue to mitigate this weakness. This reporting includes balance sheets, statements of operations, statements of cash flows, and other detail supporting these statements.

This annual report does not include an attestation report of our registered public accounting firm regarding internal control over financial reporting. Our report was not subject to attestation by our registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permits us to provide only management's report in this annual report.

Additionally, there were no changes in our internal controls that could materially affect the disclosure controls and procedures subsequent to the date of their evaluation. As a result, no corrective actions were required or undertaken.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE.

The information required by this item is included under the captions, "**Election of Directors**," "**Executive Officers**" and "**Section 16(a) Beneficial Ownership Reporting Compliance**" in our proxy statement relating to our 2011 Annual Meeting of Shareholders scheduled to be held on June 10, 2011, and is incorporated herein by reference.

We have a Business Conduct Policy applicable to all employees of SCI. Additionally, the Chief Executive Officer ("CEO") and all senior financial officers, including the principal financial officer, the principal accounting officer or controller, or any person performing a similar function (collectively, the "Senior Financial Officers") are bound by the provisions of our code of ethics relating to ethical conduct, conflicts of interest, and compliance with the law. The code of ethics is posted on our website at http://www.sciengineeredmaterials.com/investors /main/corpgov.htm.

We intend to satisfy the disclosure requirement under Item 10 of Form 8-K regarding any amendment to, waiver of, any provision of this code of ethics by posting such information on our website at the address and location specified above.

ITEM 11. EXECUTIVE COMPENSATION.

The information required by this item is included under the caption "**Executive Compensation**" in our proxy statement relating to our 2011 Annual Meeting of Shareholders scheduled to be held on June 10, 2011, and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS.

The information required by this item is included under the captions "**Ownership of Common Stock by Directors and Executive Officers"** and "**Ownership of Common Stock by Principal Shareholders**" in our proxy statement relating to our 2011 Annual Meeting of Shareholders scheduled to be held on June 10, 2011, and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE.

The information required by this item is included under the caption "**Certain Relationships and Related Transactions, and Director Independence**" in our proxy statement relating to our 2011 Annual Meeting of Shareholders scheduled to be held on June 10, 2011, and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

The information required by this item is included under the caption "**Fees of the Registered independent public accounting firm for the year ended December 31, 2010"** in our proxy statement relating to our 2011 Annual Meeting of Shareholders scheduled to be held on June 10, 2011, and is incorporated herein by reference.

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

Exhibit Number	Exhibit Description
3(a)	Certificate of Second Amended and Restated Articles of Incorporation of Superconductive Components, Inc. (Incorporated by reference to Exhibit 3(a) to the Company’s initial Form 10-SB, filed on September 28, 2000)
3(b)	Restated Code of Regulations of Superconductive Components, Inc. (Incorporated by reference to Exhibit 3(b) to the Company’s initial Form 10-SB, filed on September 28, 2000)
3(c)	Amendment to Articles of Incorporation recording the change of the corporate name to SCI Engineered Materials, Inc. (Incorporated by reference to Exhibit 3.1 to the Company’s Quarterly Report on Form 10-QSB filed November 7, 2007).
4(a)	Superconductive Components, Inc. 2006 Stock Incentive Plan (Incorporated by reference to Appendix A to the Company’s Definitive Proxy Statement for the 2006 Annual Meeting of Shareholders held on June 9, 2006, filed May 1, 2006).
4(b)	Description of the Material Terms of the Stock Option Grant and Cash Bonus Plan for Executive Officers (Incorporated by reference to the Company’s Current Report on Form 8-K, dated June 19, 2006, filed June 23, 2006)
4(c)	Form of Incentive Stock Option Agreement under the Superconductive Components, Inc. 2006 Stock Incentive Plan (Incorporated by reference to Exhibit 10.1 to the Company’s Current Report on Form 8-K dated June 19, 2006, filed June 23, 2006).
4(d)	Form of Non-Statutory Stock Option Agreement under the Superconductive Components, Inc. 2006 Stock Incentive Plan (Incorporated by reference to Exhibit 10.2 to the Company’s Current Report on Form 8-K dated June 19, 2006, filed June 23, 2006).
4(e)	Description of the Material Terms of the Stock Option Grant for Executive Officers and Board of Directors (Incorporated by reference to the Company’s Current Report on Form 8-K dated January 2, 2009, filed January 6, 2009).
4(f)	Fourth Amended and Restated 1995 Stock Option Plan (Incorporated by reference to Exhibit 4(a) to the Company’s Registration Statement on Form S-8 (Registration No. 333-97583), filed on August 2, 2002)
4(g)	Form of Non-Statutory Stock Option Agreement Under the Superconductive Components, Inc. Fourth Amended and Restated 1995 Stock Option Plan (Incorporated by reference to Exhibit 10.1 to the Company’s Current Report on Form 8-K, filed on December 22, 2005)
4(h)	Warrant to purchase common stock of Superconductive Components, Inc. issued to the Estate of Edward R. Funk, dated October 19, 2005 (Incorporated by reference to Exhibit 10(r) to the Company’s Registration Statement Form on SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)

4(i)	Warrant to purchase common stock of Superconductive Components, Inc. issued to the Estate of Ingeborg V. Funk, dated October 19, 2005 (Incorporated by reference to Exhibit 10(s) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
4(j)	Warrant to purchase common stock of Superconductive Components, Inc. issued to Robert H. Peitz, effective October 19, 2005 (Incorporated by reference to Exhibit 10(t) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
10(a)	Employment Agreement entered into as of February 26, 2002, between Daniel Rooney and the Company (Incorporated by reference to Exhibit 10(a) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
10(b)	Lease Agreement between Superconductive Components, Inc. and Duke Realty Ohio dated as of September 29, 2003, with Letter of Understanding dated February 17, 2004 (Incorporated by reference to Exhibit 10(a) to the Company's Quarterly Report on Form 10-QSB, filed on March 31, 2004)
10(c)	License Agreement with Sandia Corporation dated February 26, 1996 (Incorporated by reference to Exhibit 10(f) to the Company's Form 10-SB Amendment No. 1, filed on January 3, 2001)
10(d)	Nonexclusive License with The University of Chicago (as Operator of Argonne National Laboratory) dated October 12, 1995 (Incorporated by reference to Exhibit 10(g) to the Company's Form 10-SB Amendment No. 1, filed on January 3, 2001)
10(e)	Nonexclusive License with The University of Chicago (as Operator of Argonne National Laboratory) dated October 12, 1995 (Incorporated by reference to Exhibit 10(h) to the Company's Form 10-SB Amendment No. 1, filed on January 3, 2001)
10(f)	Ohio Department of Development Third Frontier Action Fund Award dated February 20, 2004 (Incorporated by reference to Exhibit 10 (o) to the Company's Annual Report on Form 10-KSB, filed on March 30, 2004)
10(g)	Subscription Agreement between the Company and the Estate of Edward R. Funk, dated October 14, 2005 (Incorporated by reference to Exhibit 10(o) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
10(h)	Subscription Agreement between the Company and the Estate of Ingeborg V. Funk, dated October 14, 2005 (Incorporated by reference to Exhibit 10(p) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
10(i)	Subscription Agreement between the Company and Robert H. Peitz, dated October 14, 2005 (Incorporated by reference to Exhibit 10(q) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)

10(j)	Conversion Agreement between the Company and the Estate of Edward R. Funk, dated October 14, 2005 (Incorporated by reference to Exhibit 10(u) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
10(k)	Conversion Agreement between the Company and the Estate of Ingeborg V. Funk, dated October 14, 2005 (Incorporated by reference to Exhibit 10(v) to the Company's Registration Statement on Form SB-2 (Registration No. 333-131605), filed on February 6, 2006, and amended by Pre-effective Amendment No. 1 filed March 23, 2006)
10(l)	Description of purchase order received from an existing customer (Incorporated by reference to the Company's Current Report on Form 8-K, filed January 24, 2007).
10(m)	Ohio Department of Development Third Frontier Advanced Energy Program Award (Incorporated by reference to the Company's Current Report on Form 8-K, filed December 16, 2008).
10(n)	Description of material terms of Stock Option Agreements with the Company's Executive Officers and Board of Directors (Incorporated by reference to the Company's Current Report on Form 8-K, filed January 6, 2009).
10(o)	Business Loan Agreement between the Company and The Huntington National Bank, dated as of January 13, 2009 (Incorporated by reference to the Company's Current Report on Form 8-K, filed January 23, 2009).
10(p)	Description of material modification to rights of security holders of common stock purchase warrants set to expire in 2009 (Incorporated by reference to the Company's Current Report on Form 8-K, filed May 7, 2009).
10(q)	Description of Purchase Order received from a new customer (Incorporated by reference to the Company's Current Report on Form 8-K, filed June 22, 2009).
10(r)	Description of information received from a customer regarding customer's intent to purchase material (Incorporated by reference to the Company's Current Report on Form 8-K, filed September 17, 2009).
10(s)	Notification from the Ohio Department of Development Third Frontier Photovoltaic Program of grant to be awarded dated December 17, 2009 (Incorporated by reference to the Company's Current Report on Form 8-K, filed December 22, 2009).
10(t)	Description of exercise of 150,000 common stock warrants (Incorporated by reference to the Company's Current Report on Form 8-K, dated January 8, 2010).
10(u)	Description of exercise of 40,833 common stock warrants (Incorporated by reference to the Company's Current Report on Form 8-K, dated June 4, 2010).

16(a)		Description of the approval of the engagement of Crowe Horwath LLP ("Crowe") as the Company's independent registered public accounting firm for the year ended December 31, 2010. (Incorporated by reference to the Company’s Current Report on Form 8-K, dated May 13, 2010).
22(a)		Description of submission of matters to a vote of security holders for the election of five members to the board of directors (Incorporated by reference to the Company’s Current Report on Form 8-K, dated June 10, 2010).
23	*	Consent of Independent Registered Accounting Firms
24	*	Powers of Attorney.
31.1	*	Rule 13a-14(a) Certification of Principal Executive Officer.
31.2	*	Rule 13a-14(a) Certification of Principal Financial Officer.
32.1	*	Section 1350 Certification of Principal Executive Officer.
32.2	*	Section 1350 Certification of Principal Financial Officer.
99.1		Press Release dated February 28, 2011, entitled “SCI Engineered Materials, Inc., Reports Fourth Quarter and Full-Year 2010 Results.”

* Filed herewith

SIGNATURES

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

SCI ENGINEERED MATERIALS, INC.

Date: February 28, 2011

By: /s/ Daniel Rooney
Daniel Rooney, Chairman of the Board of Directors, President and Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities indicated on the 28th day of February 2011.

Signature	*Title*
/s/ Daniel Rooney	Chairman of the Board of Directors, President, and Chief Executive Officer (principal executive officer)
/s/ Gerald S. Blaskie Gerald S. Blaskie	Vice President and Chief Financial Officer (principal financial officer and principal accounting officer)
Robert J. Baker* Robert J. Baker	Director
Edward W. Ungar* Edward W. Ungar	Director
Robert H. Peitz* Robert H. Peitz	Director
Walter J. Doyle* Walter J. Doyle	Director

*By: /s/ Daniel Rooney
Daniel Rooney, Attorney-in-Fact

INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders
SCI Engineered Materials, Inc.
Columbus, Ohio

We have audited the accompanying balance sheet of SCI Engineered Materials, Inc. (the "Company") as of December 31, 2010, and the related statements of operations, shareholders' equity, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2010, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Crowe Horwath LLP

Columbus, Ohio
February 28, 2011

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
SCI Engineered Materials, Inc.

Columbus, Ohio

We have audited the accompanying balance sheet of SCI Engineered Materials, Inc. as of December 31, 2009, and the related statements of operations, shareholders' equity and cash flows for the year ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of SCI Engineered Materials, Inc. as of December 31, 2009, and the results of its operations and its cash flows for the year ended December 31, 2009 in conformity with accounting principles generally accepted in the United States of America.

/s/ MALONEY + NOVOTNY LLC

Canton, Ohio
February 17, 2010

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

SCI ENGINEERED MATERIALS, INC.

BALANCE SHEETS

DECEMBER 31, 2010 AND 2009

ASSETS

	2010	2009
Current Assets		
Cash	$ 1,511,752	$ 1,107,216
Accounts receivable		
Trade, less allowance for doubtful accounts of $16,000	574,965	539,398
Contract	86,501	19,714
Other	20,551	11,000
Inventories	1,344,426	1,031,777
Deferred income taxes	156,000	156,000
Prepaid expenses	51,369	977,536
Total current assets	3,745,564	3,842,641
Property and Equipment, at cost		
Machinery and equipment	5,267,891	4,933,855
Furniture and fixtures	134,666	127,451
Leasehold improvements	315,054	315,054
Construction in progress	-	22,966
	5,717,611	5,399,326
Less accumulated depreciation	(3,250,237)	(2,868,198)
	2,467,374	2,531,128
Other Assets		
Deposits	29,621	21,909
Intangibles	49,276	41,358
Total other assets	78,897	63,267
TOTAL ASSETS	$ 6,291,835	$ 6,437,036

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

SCI ENGINEERED MATERIALS, INC.

BALANCE SHEETS

DECEMBER 31, 2010 AND 2009

LIABILITIES AND SHAREHOLDERS' EQUITY

	2010	2009
Current Liabilities		
Capital lease obligations, current portion	$ 399,780	$ 363,270
Note payable, current portion	64,292	62,394
Accounts payable	573,741	263,468
Customer deposits	366,153	1,319,455
Accrued compensation	71,704	67,863
Accrued expenses and other	232,701	210,294
Total current liabilities	1,708,371	2,286,744
Capital lease obligations, net of current portion	505,758	738,750
Note payable, net of current portion	252,927	317,219
Total liabilities	2,467,056	3,342,713
Commitments and contingencies (Note 6)		
Shareholders' Equity		
Convertible preferred stock, Series B, 10% cumulative, nonvoting, no par value, $10 stated value, optional redemption at 103%; optional shareholder conversion 2 shares for 1; 24,152 and 24,297 shares issued and outstanding, respectively	393,678	371,612
Common stock, no par value, authorized 15,000,000 shares; 3,775,898 and 3,571,775 shares issued and outstanding, respectively	9,725,390	9,209,424
Additional paid-in capital	1,587,727	1,412,382
Accumulated deficit	(7,882,016)	(7,899,095)
	3,824,779	3,094,323
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 6,291,835	$ 6,437,036

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

SCI ENGINEERED MATERIALS, INC.

STATEMENTS OF OPERATIONS

YEARS ENDED DECEMBER 31, 2010 AND 2009

	2010	2009
PRODUCT REVENUE	$ 8,038,774	$ 7,004,527
CONTRACT RESEARCH REVENUE	877,348	1,005,708
TOTAL REVENUE	8,916,122	8,010,235
COST OF PRODUCT REVENUE	6,002,686	5,311,459
COST OF CONTRACT RESEARCH REVENUE	639,452	828,897
TOTAL COST OF REVENUE	6,642,138	6,140,356
GROSS PROFIT	2,273,984	1,869,879
GENERAL AND ADMINISTRATIVE EXPENSE	1,128,644	1,237,672
RESEARCH AND DEVELOPMENT EXPENSE	442,214	314,386
MARKETING AND SALES EXPENSE	623,231	647,859
INCOME (LOSS) FROM OPERATIONS	79,895	(330,038)
OTHER INCOME (EXPENSE)		
Interest income	5,273	6,394
Interest expense	(85,643)	(108,712)
Gain (loss) on disposal of equipment	10,251	(45,646)
Financing expense	-	(76,387)
Miscellaneous, net	(1,830)	(1,830)
	(71,949)	(226,181)
INCOME (LOSS) BEFORE INCOME TAXES	7,946	(556,219)
INCOME TAX BENEFIT	(9,133)	(59,000)
NET INCOME (LOSS)	17,079	(497,219)
DIVIDENDS ON PREFERRED STOCK	(24,308)	(24,430)
LOSS APPLICABLE TO COMMON SHARES	$ (7,229)	$ (521,649)
EARNINGS PER SHARE - BASIC AND DILUTED (Note 7)		
INCOME (LOSS) PER COMMON SHARE		
Basic	$ 0.00	$ (0.15)
Diluted	$ 0.00	$ (0.15)
WEIGHTED AVERAGE SHARES OUTSTANDING		
Basic	3,750,376	3,562,960
Diluted	3,750,376	3,562,960

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

SCI ENGINEERED MATERIALS, INC.

STATEMENTS OF SHAREHOLDERS' EQUITY

YEARS ENDED DECEMBER 31, 2010 AND 2009

	Convertible Preferred Stock, Series B	Common Stock	Additional Paid-In Capital	Accumulated Deficit	Total
Balance 01/01/09	$ 373,647	$ 9,180,183	$ 985,396	$ (7,401,876)	$ 3,137,350
Accretion of cumulative dividends	24,430	-	(24,430)	-	-
Common stock conversion from preferred stock (Note 7)	(2,035)	2,035	-	-	-
Stock based compensation expense (Note 2G)	-	-	451,416	-	451,416
Proceeds from exercise of stock options (Note 7)	-	21,206	-	-	21,206
Common stock issued	-	6,000	-	-	6,000
Payment of cumulative dividends	(24,430)	-	-	-	(24,430)
Net loss	-	-	-	(497,219)	(497,219)
Balance 12/31/09	$ 371,612	$ 9,209,424	$ 1,412,382	$ (7,899,095)	$ 3,094,323
Accretion of cumulative dividends	24,308	-	(24,308)	-	-
Common stock conversion from preferred stock (Note 7)	(2,242)	2,242	-	-	-
Stock based compensation expense (Note 2G)	-	-	199,653	-	199,653
Proceeds from exercise of stock warrants (Note 7)	-	490,799	-	-	490,799
Proceeds from exercise of stock options (Note 7)	-	19,175	-	-	19,175
Common stock issued	-	3,750	-	-	3,750
Net income	-	-	-	17,079	17,079
Balance 12/31/10	$ 393,678	$ 9,725,390	$ 1,587,727	$ (7,882,016)	$ 3,824,779

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

SCI ENGINEERED MATERIALS, INC.

STATEMENTS OF CASH FLOWS

YEARS ENDED DECEMBER 31, 2010 AND 2009

	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	$ 17,079	$ (497,219)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and accretion	488,003	443,800
Amortization	3,088	3,088
Stock based compensation	203,403	381,030
Financing expense related to warrant extension	-	76,387
(Gain) loss on sale of equipment	(10,251)	45,646
Deferred income taxes	-	(156,000)
Inventory reserve	403	554
Changes in allowance for doubtful accounts	-	(8,947)
Changes in operating assets and liabilities:		
Accounts receivable	(111,905)	15,991
Inventories	(313,052)	232,102
Prepaid expenses	926,167	(934,973)
Other assets	(18,718)	(3,099)
Accounts payable	310,273	14,159
Accrued expenses and customer deposits	(933,678)	649,246
Net cash provided by operating activities	560,812	261,765
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds on sale of equipment	10,500	-
Purchases of property and equipment	(225,209)	(168,132)
Net cash used in investing activities	(214,709)	(168,132)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from exercise of common stock options	19,175	21,206
Proceeds from exercise of common stock warrants	490,799	-
Payment for accumulated dividends on preferred stock	-	(24,430)
Principal payments on capital lease obligations and note payable	(451,541)	(382,243)
Net cash provided by (used in) financing activities	58,433	(385,467)
NET INCREASE (DECREASE) IN CASH	$ 404,536	$ (291,834)
CASH - Beginning of year	1,107,216	1,399,050
CASH - End of year	$ 1,511,752	$ 1,107,216
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the year for:		
Interest	$ 85,643	$ 108,712
Income taxes	$ 2,400	$ 2,450
SUPPLEMENTAL DISCLOSURES OF NONCASH INVESTING AND FINANCING ACTIVITIES		
Property and equipment purchased by capital lease	$ 192,665	$ 555,700
Increase in asset retirement obligation	$ 6,624	$ 6,624
Financing expense related to warrant extension	$ -	$ 76,387

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

Note 1. Business Organization and Purpose

SCI Engineered Materials, Inc. ("SCI" or the "Company"), formerly Superconductive Components, Inc., an Ohio corporation, was incorporated in 1987. The Company operates in the physical vapor deposition industry in which it develops, commercializes technologies, and manufactures ceramics and metals for advanced applications in: Photonics, Solar, Thin Film Battery, Semiconductor, and, to a lesser extent High Temperature Superconductor ("HTS"). Photonics currently represents the Company's largest market. Solar is an industry that is exhibiting rapid growth. Thin Film Battery is a developing market where manufacturers of batteries use the Company's products to produce very small power supplies with small quantities of stored energy. Semiconductor is a developing market for the Company.

Note 2. Summary of Significant Accounting Policies

A. Inventories - Inventories are stated at the lower of cost or market on an acquired or internally produced lot basis, and consist of raw materials, work-in-process and finished goods. Cost includes material, labor, freight and applied overhead. Inventory reserves are established for obsolete inventory and excess inventory quantities based on management's estimate of net realizable value. The Company has an inventory reserve of $50,000 at December 31, 2010 and $49,597 at December 31, 2009.

The Company enters into cancelable purchase commitment arrangements with certain suppliers. Estimated purchase commitments to these suppliers approximated $676,000 and $769,000 at December 31, 2010 and 2009, respectively. The Company can cancel these commitments at the Company's discretion without penalty.

B. Property and Equipment - Property and equipment are carried at cost. Depreciation is provided on the straight-line method based on the estimated useful lives of the assets for financial reporting purposes and allowable accelerated methods for tax purposes. Useful lives range from ten years on certain furniture and fixtures and leasehold improvements to three years on computer equipment. Depreciation and accretion expense totaled $488,003 and $443,800 for the years ended December 31, 2010 and 2009, respectively. Expenditures for renewals and betterments are capitalized and expenditures for repairs and maintenance are charged to operations as incurred. Construction in progress at December 31, 2009 consisted primarily of two pieces of equipment that were placed in service in the first quarter of 2010 at a total cost of approximately $23,000.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the fair value is less than the carrying amount of the asset, a loss is recognized for the difference. Equipment with a net book value of approximately $44,000 was considered impaired, and a loss was recognized in 2009.

C. Equipment - In 2004, the Company received funds of $517,935 from the Ohio Department of Development's Third Frontier Action Fund (TFAF) for the purchase of equipment related to the grant's purpose. In a separate contract with the Department of Energy the Company received $27,500 for the purchase of equipment related to the contract's purpose. The Company elected to record the funds disbursed as a contra asset.

Note 2. Summary of Significant Accounting Policies (Continued)

As assets were purchased, the liability initially created when the cash was received was reduced with no revenue recognized or fixed asset recorded on the balance sheet. As of December 31, 2009, the Company had used the entire amount received to purchase equipment. The grant and contract both provide that as long as the Company performs in compliance with the grant/contract, the Company retains the rights to the equipment. The grant was completed in January 2009.

D. Research and Development - Research and development costs are expensed as incurred. Research and development expense for the years ended December 31, 2010 and 2009 was $442,214 and $314,386, respectively. The Company continues to develop innovative transparent conductive oxide systems to further align activities with customer needs, as well as trial materials which resulted in increased research and development expense during 2010. These new research and development endeavors have moved the Company beyond the scope of the current federal and state grants and awards.

E. Intangible Assets - The Company reviews intangible assets for impairment and performs detailed testing whenever impairment indicators are present. If necessary, an impairment loss is recorded for the excess of book cost over fair value. There were no impairment adjustments for the years ended December 31, 2010 and 2009.

Licenses - The Company has secured licenses to produce various superconductive materials for periods up to the expiration of the applicable patents. The license fees are amortized over the expected life of the agreement or applicable patent, which is seventeen years. Cost and accumulated amortization of licenses at December 31, 2010 were $21,000 and $19,006, respectively. Cost and accumulated amortization of licenses at December 31, 2009 were $21,000 and $17,748, respectively. Amortization expense was $1,259 for the years ended December 31, 2010 and 2009. Amortization expense is estimated to be $1,259 in 2011 and $734 in 2012.

Patent - The Company has secured patents for manufacturing processes used in its operations. Costs incurred to secure the patents have been capitalized and are being amortized over the life of the patents. Cost and accumulated amortization of the patents at December 31, 2010 were $67,204 and $19,925 respectively. Cost and accumulated amortization of the patents at December 31, 2009 were $56,201 and $18,096 respectively. Amortization expense was $1,830 for the years ended December 31, 2010 and 2009. Amortization expense is estimated to be at least $1,830 for each of the next five years. An additional patent which had cost at December 31, 2010 and 2009 of $30,735 and $19,728, respectively, was applied for in 2009 and is expected to take up to six years to finalize.

F. Income Taxes - Income taxes are provided for by utilizing the asset and liability method which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax bases of assets and liabilities using presently enacted tax rates. Deferred tax assets are reduced by a valuation allowance which is established when “it is more likely than not” that some portion or all of the deferred tax assets will not be recognized.

Note 2. Summary of Significant Accounting Policies (Continued)

G. Stock Based Compensation - Compensation cost for all stock-based awards is based on the grant date fair value and recognized over the required service (vesting) period. Non cash stock based compensation expense was $203,403 and $381,030 for the years ended December 31, 2010 and 2009, respectively. Unrecognized compensation expense was $724,842 as of December 31, 2010 and will be recognized through 2017. There was no benefit recorded for this compensation cost as the expense primarily relates to incentive stock options that do not qualify for a tax deduction until, and only if, a qualifying disposition occurs.

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

I. Concentrations of Credit Risk - The Company's cash balances, which are at times in excess of federally insured levels, are maintained at a large regional bank and a global investment banking group, and are continually monitored to minimize the risk of loss. The Company grants credit to most customers, who are varied in terms of size, geographic location and financial strength. Customer balances are continually monitored to minimize the risk of loss.

The Company had four major customers in 2010 and 2009, which accounted for revenue of approximately $5,800,000 and $4,200,000, respectively. These customers totaled approximately $403,000 and $372,000 of trade accounts receivable at December 31, 2010 and 2009, respectively. The largest customer represented approximately 27% of total revenue in 2010 and approximately 25% of total revenue in 2009. In January 2011 one of these customers announced it was closing its facilities in the first quarter of 2011. The Company has collected all outstanding accounts receivable from this customer at December 31, 2010 and expects to recover the anticipated lower revenue as a result of the loss of this customer with additional revenue from new and existing customers.

J. 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 period. Significant estimates include the allowance for doubtful accounts and valuation allowance on deferred tax assets. Actual results could differ from those estimates.

K. Fair Value of Financial Instruments - The estimated fair value of amounts reported in the financial statements have been determined using available market information and valuation methodologies, as applicable (see Note 11).

Note 2. Summary of Significant Accounting Policies (Continued)

L. Revenue Recognition - Revenue from product sales is recognized upon shipment to customers. Provisions for discounts and rework costs for returns are established when products are shipped based on historical experience. Customer deposits represent cash received in advance of revenue earned.

Revenue from contract research provided for third parties is recognized on the percentage of completion method. Contract research revenue is recognized during the period in which qualifying expenses are incurred for the research that is performed as set forth under the terms of the grant award agreements.

M. Accounts Receivable - The Company extends unsecured credit to customers under normal trade agreements, which require payment within 30 days. Accounts greater than 90 days past due, which amounted to $0 as of December 31, 2010 and 2009, are considered delinquent. The Company does not charge interest on delinquent trade accounts receivable. Unless specified by the customer, payments are applied to the oldest unpaid invoice. Accounts receivable are presented at the amount billed.

Management estimates an allowance for doubtful accounts, which was approximately $16,000 as of December 31, 2010 and 2009. This estimate is based upon management's review of delinquent accounts and an assessment of the Company's historical evidence of collections. Specific accounts are charged directly to the reserve when management obtains evidence of a customer's insolvency or otherwise determines that the account is uncollectible.

Note 3. Inventories

Inventories consist of the following at December 31:

	2010	2009
Raw materials	$ 338,971	$ 371,060
Work-in-process	866,853	506,288
Finished goods	188,602	204,026
	1,394,426	1,081,374
Less reserve for obsolete inventory	50,000	49,597
	$ 1,344,426	$ 1,031,777

Note 4. Note Payable

During 2006, the Company was approved for a 166 Direct Loan from the Ohio Department of Development in the amount of $400,000. These funds were received in July of 2008 and were used for the purchase of production equipment and to reduce the Company's capital lease obligations on certain equipment. The term of the loan is 84 months at a fixed interest rate of 3%. There is also a 0.25% annual servicing fee to be charged monthly on the outstanding principal balance. The Company is making monthly servicing fee, interest and principal payments of approximately $6,000. The loan principal balance will be fully amortized at the end of the term in August 2015. The loan is collateralized by the project equipment. As of December 31, 2010 the loan had a balance of $317,219. The future minimum payment, year by year, with the present value of such payments, as of December 31, 2010, is as follows:

2011	$	73,649
2012		73,486
2013		73,319
2014		73,146
2015		48,665
Total minimum note payments		342,265
Less amount representing interest		25,046
Present value of minimum note payments		317,219
Less current portion		64,292
Note payable, net of current portion	$	252,927

On December 21, 2010, the Company issued a Promissory Note (the "Note") to The Huntington National Bank, as Lender. The Note is collateralized by the Company's inventories, equipment and accounts receivable. This Note matures on April 15, 2011 and replaced a note previously signed on December 14, 2009. As of December 31, 2010 and December 31, 2009 there was no outstanding balance on the Note.

Among other items, the Note provides for the following:

- At no time shall the outstanding balance of the principal sum of the Note exceed the lesser of (1) $500,000 or (2) an amount equal to the sum of 80% of Eligible Accounts plus the lesser of (A) 50% of Eligible inventory or (B) $200,000.

- Interest on the Note is subject to change from time to time based on changes in an independent index (LIBOR). The index at the inception of the Note was 0.261% per annum. The interest rate to be applied to the unpaid principal balance during the term will be at a rate of 2.75 percentage points over the index.

- Accrued interest is payable monthly. The outstanding principal and accrued interest owed on the Note matures on April 15, 2011.

Note 5. Lease Obligations

Operating

The Company leases its facilities and certain office equipment under agreements classified as operating leases expiring at various dates through 2015. Rent expense, which includes various monthly rentals for the years ended December 31, 2010 and 2009 totaled $159,979 and $149,230, respectively. Future minimum lease payments at December 31, 2010 are as follows:

2011	$ 112,711
2012	112,324
2013	112,324
2014	71,789
2015	1,600
	$ 410,748

Capital

The Company also leases certain equipment under capital leases. Future minimum lease payments, by year, with the present value of such payments, as of December 31, 2010 are as follows:

2011	$ 477,035
2012	306,756
2013	207,987
2014	58,272
2015	11,794
Total minimum lease payments	1,061,844
Less amount representing interest	156,306
Present value of minimum lease payments	905,538
Less current portion	399,780
Capital lease obligations, net of current portion	$ 505,758

Note 5. Lease Obligations (continued)

The equipment under capital lease at December 31 is included in the accompanying balance sheets under the following captions:

	2010	2009
Machinery and equipment	$ 2,048,048	$ 1,985,901
Less accumulated depreciation	553,661	217,589
Net book value	$ 1,494,387	$ 1,768,312

These assets are amortized over a period of three to ten years using the straight-line method and amortization is included in depreciation expense.

Note 6. Purchase Commitments

Equipment purchase commitments approximated $370,000 at December 31, 2010 and $140,000 at December 31, 2009.

In addition, estimated purchase commitments for inventories approximated $676,000 and $769,000 (see Note 2A) at December 31, 2010 and 2009, respectively.

Note 7. Common and Preferred Stock

Common Stock

In 2010, proceeds of $19,175 were received from the exercise of 12,000 stock options. The exercise price for these options ranged from $1.55 to $2.125. The aggregate intrinsic value of these options was $19,715. Also in 2010, proceeds from 190,833 warrants exercised were $490,799. The exercise price for these warrants ranged from $2.50 to $2.88.

In 2009, 10,250 stock options were exercised resulting in proceeds of $21,206. The exercise price for these options ranged from $1.55 to $2.125.

Note 7. Common and Preferred Stock (continued)

Preferred Stock

Shares of preferred stock authorized at December 31, 2010 and 2009 and outstanding at December 31, 2010 were as follows:

	Shares Authorized	Shares Outstanding
Cumulative Preferred Stock	10,000	-
Voting Preferred Stock	125,000	-
Non-Voting Preferred Stock	125,000(a)	24,152(b)

(a) Includes 700 shares of Series A Preferred Stock and 100,000 shares of Series B Preferred Stock authorized for issuance.
(b) Series B Preferred Stock outstanding at December 31, 2009 was 24,297 shares.

In January 1996, the Company completed an offering of 70,000 shares of $10 stated value 1995 Series B 10% cumulative non-voting convertible preferred stock. The shares are convertible to common shares at the rate of $5.00 per share. At the Company's option, the Series B shares are redeemable at 103% of the stated value plus the amount of any accrued and unpaid cash dividends.

During 2010, a shareholder converted 145 shares of Series B Preferred Stock into 290 shares of common stock. During 2009, a shareholder converted 133 shares of Series B Preferred Stock into 266 shares of common stock.

On February 15, 2010 the Board of Directors voted not to authorize the payment of a cash dividend on convertible preferred stock, Series B, to shareholders of record as of December 31, 2009. During 2009, a Series B cash dividend of $24,430 was paid to shareholders of record as of December 31, 2008. At December 31, 2010 and 2009 the Company had accrued dividends on Series B preferred stock of $144,912 and $121,793, respectively. These amounts are included in convertible preferred stock, Series B on the balance sheet at December 31, 2010 and 2009.

Earnings Per Share

Basic income (loss) per share is calculated as income available to common stockholders divided by the weighted average of common shares outstanding. Diluted earnings per share is calculated as diluted income available to common stockholders divided by the diluted weighted average number of common shares. Diluted weighted average number of common shares gives effect to all dilutive potential common shares outstanding during the period using the treasury stock method and convertible preferred stock using the if-converted method. Diluted earnings per share exclude all diluted potential shares if their effect is anti-dilutive. For the year ended December 31, 2010, all (156,517) common stock options were anti-dilutive due to the net loss. For the year ended December 31, 2009, all (263,818) common stock options and warrants were anti-dilutive due to the net loss.

Note 7. Common and Preferred Stock (continued)

Following is a summary of employee and director stock options, stock warrants, and preferred stock, Series B at December 31, 2010 and 2009.

	December 31, 2010	December 31, 2009
Options	1,066,250	1,115,750
Warrants	-	557,057
Preferred Series B	24,152	24,297
	1,090,402	1,697,104

The following is provided to reconcile the earnings per share calculations:

	2010	2009
Loss applicable to common shares	$ (7,229)	$ (521,649)
Weighted average common shares outstanding – basic	3,750,376	3,562,960
Effect of dilutions - stock options and warrants	-	-
Weighted average shares outstanding - diluted	3,750,376	3,562,960

Note 8. Stock Option Plans

On June 9, 2006, shareholders approved the Superconductive Components, Inc. 2006 Stock Incentive Plan (the "2006 Plan"), which replaced the 1995 Stock Option Plan ("the 1995 Plan"). The Company adopted the 2006 Plan as incentive to key employees, directors and consultants under which options to purchase up to 600,000 shares of the Company's common stock may be granted, subject to the execution of stock option agreements. Incentive stock options may be granted to key employees of the Company and non-statutory options may be granted to directors who are not employees and to consultants and advisors who render services to the Company. Options may be exercised for periods up to 10 years from the date of grant at prices not less than 100% of fair market value on the date of grant. As of December 31, 2010 there were 585,500 stock options outstanding from the 2006 Plan which expire at various dates through January 2, 2019.

On September 29, 1995, the Company adopted the 1995 Stock Option Plan (the "1995 Plan") as incentive to key employees, directors and consultants. As of December 31, 2010 there were 480,750 stock options outstanding from the 1995 Plan which expire at various dates through December 16, 2015. The Company adopted the 1995 Plan as incentive to key employees, directors and consultants under which options to purchase up to 900,000 shares of the Company's common stock may be granted, subject to the execution of stock option agreements.

Note 8. Stock Option Plans (continued)

The cumulative status at December 31, 2010 and 2009 of options granted and outstanding, as well as options which became exercisable in connection with the Stock Option Plans is summarized as follows:

Employee Stock Options

	Stock Options	Weighted Average Exercise Price	Weighted Average Contractual Term (yrs)	Aggregate Intrinsic Value
Outstanding at January 1, 2009	362,750	$ 2.14		
Granted	450,000	6.00		
Exercised	(6,250)	2.03		
Forfeited	(10,250)	3.05		
Outstanding at December 31, 2009	796,250	$ 4.31		
Granted	-	-		
Exercised	(11,000)	1.55		
Forfeited	(1,500)	2.88		
Outstanding at December 31, 2010	783,750	$ 4.35	5.9	$ -
Options exercisable at December 31, 2009	369,325	$ 2.52	3.9	$ 305,464
Options exercisable at December 31, 2010	411,800	$ 2.94	3.9	$ 167,055
Options expected to vest	371,950	$ 5.91	8.2	$ -

Non-Employee Director Stock Options

	Stock Options	Weighted Average Exercise Price	Weighted Average Contractual Term (yrs)	Aggregate Intrinsic Value
Outstanding at January 1, 2009	233,500	$ 2.54		
Granted	90,000	6.00		
Exercised	(4,000)	2.13		
Expired	-	-		
Forfeited	-	-		
Outstanding at December 31, 2009	319,500	$ 3.52		
Granted	-	-		
Exercised	(1,000)	2.13		
Expired	(36,000)	2.97		
Forfeited	-	-		
Outstanding at December 31, 2010	282,500	$ 3.60	3.4	$ -
Options exercisable at December 31, 2009	259,500	$ 2.95	3.8	$ 104,325
Options exercisable at December 31, 2010	252,500	$ 3.31	3.4	$ 10,125
Options expected to vest	30,000	$ 6.00	3.3	$ -

Note 8. Stock Option Plans (continued)

Information related to the weighted average fair value of stock options activity for the year ended December 31, 2010 is as follows:

	Stock Options		Weighted Average Exercise Price
Employee Stock Options			
Nonvested options at January 1, 2010	426,925	$	5.86
Granted	-		-
Exercised	-		-
Forfeited	(400)		3.25
Vested	(54,575)		5.51
Nonvested options at December 31, 2010	371,950	$	5.91
Non-Employee Director Stock Options			
Nonvested options at January 1, 2010	60,000	$	6.00
Granted	-		-
Forfeited	-		-
Expired	-		-
Vested	(30,000)		6.00
Nonvested options at December 31, 2010	30,000	$	6.00

On January 2, 2009, the Stock Option and Compensation Committee (the "Committee") of the Board of Directors of the Company approved the grant of options to purchase a total of 450,000 shares of the Company's common stock, effective January 2, 2009, to the Company's Chief Executive Officer and three other executive officers. The Committee also approved the grant of options to purchase 90,000 shares to the four non-employee board members. Pursuant to the terms of the agreements, the options have an exercise price of $6.00 per share, the closing price of the Company's common stock as reported on the OTC Bulletin Board regulated quotation service on the grant date.

Exercise prices range from $1.00 to $6.00 for options at December 31, 2010. The weighted average option price for all options outstanding was $4.15 with a weighted average remaining contractual life of 5.3 years at December 31, 2010. The weighted average option price for all options outstanding was $4.08 with a weighted average remaining contractual life of 5.8 years at December 31, 2009.

Note 8. Stock Option Plans (continued)

The weighted average fair values at date of grant for options granted during 2009 was $3.84, and was estimated using the Black-Scholes option valuation model with the following weighted average assumptions:

Expected life in years	9.2(a)
Interest rate	2.5%(b)
Volatility	56.02%(c)
Dividend yield	0%(d)

(a) – Determined using historical exercise and past vesting termination patterns.
(b) – Determined using the interpolated yield on U.S. Treasury 5 year Note.
(c) – Determined using implied volatility, after consideration of historical volatility.
(d) – Determined using constant dividend yield during the expected term of option.

Note 9. Warrants Issued and Vested

There were no common stock warrants outstanding at December 31, 2010. The cumulative status at December 31, 2009, of warrants issued and vested is summarized as follows:

Issued	Vested	Consideration	Issue Date	Expiration Date	Warrant Price
150,000	150,000	Subordinated Notes Payable	01/2000	01/2010	$ 2.50(a)
122,918	122,918	Private Equity Offering	05/2004	05/2010	2.88(b,c,d)
17,500	17,500	Consulting Services	05/2004	05/2010	2.88(b.c,e)
246,639	246,639	Private Equity Offering	10/2005	10/2010	3.00(b)
20,000	20,000	Revolving Promissory Note	11/2004	11/2010	2.50(b,c)

(a) – At fair market value; exercised during 2010.
(b) – Above fair market value.
(c) – Expiration date extended from 2009 to 2010 on May 1, 2009 which resulted in non-cash financing expense of $76,387 in 2009 as presented on the Statement of Operations.
(d) – 23,333 common stock warrants exercised during 2010.
(e) – Exercised during 2010.

Note 10. Income Taxes

Deferred tax assets and liabilities result from temporary differences in the recognition of income and expense for tax and financial reporting purposes. Significant components of the Company's deferred tax assets and liabilities are as follows at December 31.

	2010	2009
Deferred tax assets		
NOL Carryforwards	$ 1,518,000	$ 1,553,000
Stock based compensation	82,000	130,000
UNICAP	25,000	26,000
Allowance for doubtful accounts	6,000	5,000
Reserve for obsolete inventories	18,000	17,000
Reserve for asset retirement	9,000	-
Property and equipment	(76,000)	(72,000)
	1,582,000	1,659,000
Valuation allowance	(1,426,000)	(1,503,000)
Net	$ 156,000	$ 156,000

A valuation allowance has been recorded against the realizability of the net deferred tax asset resulting in the recording of the asset in the accompanying financial statements of $156,000 at December 31, 2010 and 2009. The valuation allowance totaled $1,426,000 and $1,503,000 at December 31, 2010 and 2009, respectively.

The Company has net operating loss carryforwards available for federal and state tax purposes of approximately $4,300,000 and $4,600,000, at December 31, 2010 and 2009, respectively, which expire in varying amounts through 2029.

For the years ended December 31, 2010 and 2009, a reconciliation of the statutory rate and effective rate for the provisions for income taxes consists of the following:

	Percentage	
	2010	2009
Federal statutory rate	35.0%	34.0%
State/city tax	(130.9)	(11.5)
Non-deductible expense	576.8	(4.7)
Reconcile deferred tax	616.7	0.0
Rate change effect	(203.3)	0.0
Valuation allowance	(969.0)	(7.2)
Other	(40.2)	0.0
Effective rate	(114.9) %	10.6%

Note 10. Income Taxes (continued)

Components of income taxes are as follows:

	2010	2009
Current	$ (9,000)	$ 97,000
Deferred:		
NOL utilization/expiration	35,000	345,000
Other temporary differences	42,000	(165,000)
Change in valuation allowance	(77,000)	(336,000)
Total	$ (9,000)	$ (59,000)

The Company has no unrecognized tax benefits and therefore, there is no anticipated effect on the Company's effective tax rate. Any tax penalties or interest expense will be recognized in income tax expense. No interest and penalties related to unrecognized tax benefits were accrued at December 31, 2010 and 2009.

The Company is open to federal and state tax audits until the applicable statute of limitations expire. There are currently no federal or state income tax examinations underway for the Company. The tax years 2007 through 2010 remain open to examination by the major taxing jurisdictions in which we operate. The Company does, however, have prior year net operating losses which remain open for examination.

Note 11. Fair Value of Financial Instruments

The fair value of financial instruments represents the price that would be received to sell an asset or paid to transfer a liability (an exit price), and not the price that would be paid to acquire an asset or received to assume a liability (an entry price). Significant differences can arise between the fair value and carrying amount of financial instruments that are recognized at historical cost amounts.

The following methods and assumptions were used by the Company in estimating fair value disclosures for financial instruments:

- Cash and cash equivalents, short-term debt and current maturities of long-term debt: Amounts reported in the balance sheet approximate fair market value due to the short maturity of these instruments.

- Long-term capital lease obligations: Amounts reported in the balance sheet approximate fair value as the interest rates on these obligations range from 5.9% to 7.8%, which approximates current fair market rates.

- Long-term note payable obligation: Amounts reported in the balance sheet approximate fair value as the interest rate on the obligation is 3%, which approximates current fair market rates.

Note 12. Asset Retirement Obligation

Included in machinery and equipment is various production equipment, which per the Company’s building lease, is required to be removed upon termination of the related lease. Included in accrued expenses in the accompanying balance sheet is the asset retirement obligation that represents the expected present value of the liability to remove this equipment. There are no assets that are legally restricted for purposes of settling this asset retirement obligation.

Following is a reconciliation of the aggregate retirement liability associated with the Company’s obligation to dismantle and remove the machinery and equipment associated with its lease:

Balance at January 1, 2009	$	12,346
Increase in present value of the obligation (accretion expense in the corresponding amount charged against earnings)		6,624
Balance at December 31, 2009	$	18,970
Increase in present value of the obligation (accretion expense in the corresponding amount charged against earnings)		6,624
Balance at December 31, 2010	$	25,594

Note 13. Subsequent Events

On January 6, 2011, the Company issued a Promissory Note (the ”Promissory Note”) in the amount of not more than $840,000 to The Huntington National Bank, as Lender. The Promissory Note is collateralized by the Company’s inventories, equipment and accounts receivable.

Among other items, the Promissory Note provides for the following:

- Interest on the Promissory Note is subject to change from time to time based on changes in an independent index (LIBOR). The index at the inception of the Promissory Note was 0.261% per annum. The interest rate to be applied to the unpaid principal balance will be at a rate of 2.75 percentage points over the index. Under no circumstance will the interest rate be less than 4.00% per annum or more than the maximum rate allowed by applicable law.

- Accrued interest is payable monthly. The outstanding principal and accrued interest matures on December 31, 2012.

During 2010, the Company applied and was approved for a 166 Direct Loan in the amount of $744,250 with the Ohio Department of Development (ODOD). ODOD also recommended that the Ohio Tax Credit Authority approve a tax credit equal to 45 percent of employee income tax withholdings resulting from the project for five years. This credit has an estimated value of $86,000 during the entire term. ODOD also is prepared to offer funding from the Rapid Outreach Grant for up to $25,000 for costs associated with the acquisition and installation of machinery and equipment. This loan was finalized in February of 2011. The term of the loan is 84 months at a fixed interest rate of 3%. There is also a 0.25% annual servicing fee to be charged monthly on the outstanding principal balance. The loan is to be amortized over 84 months beginning on the first day of the calendar month immediately following the first full calendar month after the initial disbursement of the loan proceeds, which is expected during the second or third quarter of 2011. The loan is collateralized by the project equipment.

During 2010, the Company also applied and was approved for a 166 Direct Loan through the Advanced Energy Program with The Ohio Air Quality Development Authority (OAQDA) for approximately $1.4 million. This loan was finalized in February of 2011. The term of the loan is 84 months at a fixed interest rate of 3%. There is also a 0.25% annual servicing fee to be charged monthly on the outstanding principal balance. The loan is to be amortized over 84 months beginning on the first day of the calendar month immediately following the first full calendar month after the initial disbursement of the loan proceeds, which is expected during the second or third quarter of 2011. The loan is collateralized by the project equipment. Together, these loans can fund approximately 70% of the current capital requirements of approximately $3 million to support the Company’s planned growth.

On February 21, 2011, the Board of Directors voted to authorize the payment of a cash dividend in the amount of $24,152 on convertible preferred stock, Series B, to shareholders of record as of December 31, 2010.

Exhibit 23

Consent of Independent Registered Public Accounting Firm

We consent to the incorporation by reference in Registration Statements No.333-97583 and No. 333-67212 on Forms S-8 of our report dated February 28, 2011, relating to the financial statements of SCI Engineered Materials, Inc. appearing in this Annual Report on Form 10-K of SCI Engineered Materials, Inc for the year ended December 31, 2010.

Crowe Horwath LLP

Columbus, Ohio
February 28, 2011

Consent of Independent Registered Public Accounting Firm

We hereby consent to the incorporation by reference in the Registration Statement on Form S-8, Registration Numbers 333-97583 and 333-67212, of SCI Engineered Materials, Inc. of our report dated February 17, 2010, relating to the 2009 financial statements which appear in the Company's Form 10-K for the year ended December 31, 2010.

/s/ Maloney + Novotny LLC

Canton, Ohio
February 28, 2011

Exhibit 24

POWER OF ATTORNEY

Each of the undersigned officers and/or directors of SCI Engineered Materials, Inc., an Ohio corporation (the "Company"), hereby appoints Daniel Rooney and Michael A. Smith as his or her true and lawful attorneys-in-fact, or any of them individually with power to act without the other, as his or her true and lawful attorney-in-fact, in his or her name and on his or her behalf, and in any and all capacities stated below, to sign and to cause to be filed with the Securities and Exchange Commission the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010, and any and all amendments thereto, hereby granting unto said attorneys, and to each of them, full power and authority to do and perform in the name and on behalf of the undersigned, in any and all such capacities, every act and thing whatsoever necessary to be done in and about the premises as fully as each of the undersigned could or might do in person, hereby granting to each such attorney full power of substitution and revocation, and hereby ratifying all that any such attorney or his substitute may do by virtue hereof.

IN WITNESS WHEREOF, the undersigned have executed this Power of Attorney in counterparts if necessary, effective as of February 28, 2011.

Signature	*Title*
/s/ Daniel Rooney Daniel Rooney	President, Chief Executive Officer and Chairman of the Board of Directors and Director (principal executive officer)
/s/ Gerald S. Blaskie Gerald S. Blaskie	Vice President and Chief Financial Officer (principal financial officer and principal accounting officer)
/s/ Robert H. Peitz Robert H. Peitz	Director
/s/ Walter J. Doyle Walter J. Doyle	Director
/s/ Robert J. Baker, Jr. Robert J. Baker, Jr.	Director
/s/ Edward W. Ungar Edward W. Ungar	Director

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Daniel Rooney, certify that:

1. I have reviewed this annual report on Form 10-K of SCI Engineered Materials, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2011

/s/ Daniel Rooney
Daniel Rooney
Chairman of the Board of Directors,
President and Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Gerald S. Blaskie certify that:

1. I have reviewed this annual report on Form 10-K of SCI Engineered Materials, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant’s other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and

5. The registrant’s other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: February 28, 2011

/s/ Gerald S. Blaskie
Gerald S. Blaskie
Vice President and Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of SCI Engineered Materials, Inc. (the "Company") on Form 10-K for the period ending December 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Daniel Rooney, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Daniel Rooney
Daniel Rooney
President and Chief Executive Officer of
SCI Engineered Materials, Inc.
February 28, 2011

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of SCI Engineered Materials, Inc. (the "Company") on Form 10-K for the period ending December 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Gerald S. Blaskie, Vice President and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and result of operations of the Company.

/s/ Gerald S. Blaskie
Gerald S. Blaskie
Vice President and Chief Financial Officer of
SCI Engineered Materials, Inc.
February 28, 2011