

BIOLARGO, INC.  
Form 10-Q  
August 14, 2018

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

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**FORM 10-Q**

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

**For the quarterly period ended June 30, 2018.**

**or**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number 000-19709**

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**BIOLARGO, INC.**

*(Exact name of registrant as specified in its charter)*



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

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

The number of shares of the Registrant's Common Stock outstanding as of August 10, 2018 was 130,545,731 shares.

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**BIOLARGO, INC.**

**FORM 10-Q**

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Table of Contents**PART I – FINANCIAL INFORMATION****Item 1. Financial Statements****BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****AS OF DECEMBER 31, 2017 AND JUNE 30, 2018**

	<b>DECEMBER 31, 2017</b>	<b>JUNE 30, 2018 (Unaudited)</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$990,457	\$651,061
Accounts receivable, net of allowance of \$2,500 and \$3,500, at December 31, 2017 and June 30, 2018	94,413	89,977
Inventories	53,973	25,639
Prepaid expenses and other current assets	20,000	56,625
Total current assets	1,158,843	823,302
Leasehold improvements and equipment, net of depreciation	108,865	122,362
Other non-current assets	32,530	35,213
Deferred offering cost	195,182	186,731
Total assets	\$1,495,420	\$1,167,608
<b>Liabilities and stockholders' deficit</b>		
Current liabilities:		
Accounts payable and accrued expenses	\$224,105	\$254,657
Convertible notes payable	5,248,847	782,214
Discount on convertible notes payable, net of amortization	(1,257,182)	(93,382)
Total current liabilities	4,215,770	943,489
Long-term liabilities:		
Line of credit	—	390,000
Convertible notes and note payable	1,539,271	872,500
Discount on convertible notes and note payable and line of credit, net of amortization	(850,000)	(393,930)
Total liabilities	4,905,041	1,812,059

## COMMITMENTS, CONTINGENCIES (Note 11)

## STOCKHOLDERS' EQUITY (DEFICIT):

Convertible Preferred Series A, \$.00067 Par Value, 50,000,000 Shares Authorized, no Shares Issued and Outstanding, at December 31, 2017 and June 30, 2018	—	—
Common stock, \$.00067 Par value, 200,000,000 and 400,000,000 shares authorized, 104,164,465 and 128,359,007 shares issued, at December 31, 2017 and June 30, 2018	69,871	86,150
Additional paid-in capital	97,093,144	106,167,819
Accumulated deficit	(101,204,846)	(107,329,788)
Accumulated other comprehensive loss	(62,489 )	(61,356 )
Total Biolargo, Inc. and Subsidiaries stockholders' equity (deficit)	(4,104,320 )	(1,137,175 )
Non-controlling interest (Note 9)	694,699	492,724
Total stockholders' equity (deficit)	(3,409,621 )	(644,451 )
Total liabilities and stockholders' equity (deficit)	\$1,495,420	\$1,167,608

*See accompanying notes to unaudited consolidated financial statements.*

Table of Contents**BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****AND COMPREHENSIVE LOSS****FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2017 AND 2018****(UNAUDITED)**

	<b>THREE-MONTHS</b>		<b>SIX-MONTHS</b>	
	<b>JUNE</b>	<b>JUNE</b>	<b>JUNE</b>	<b>JUNE</b>
	<b>30, 2017</b>	<b>30, 2018</b>	<b>30, 2017</b>	<b>30, 2018</b>
Revenues				
Product revenue	\$99,978	\$315,553	\$145,995	\$539,950
Service revenue	—	11,185	—	49,817
Total revenue	99,978	326,738	145,995	589,767
Cost of revenue				
Cost of goods sold	(73,399 )	(194,000 )	(95,929 )	(328,464 )
Cost of service	—	(6,912 )	—	(35,640 )
Gross profit	26,579	125,826	50,066	225,663
Selling, general and administrative expenses	1,162,018	1,316,605	2,217,073	2,486,218
Research and development	324,280	425,576	715,616	947,306
Amortization and depreciation	6,515	12,536	14,439	22,859
Operating loss:	(1,466,234 )	(1,628,891 )	(2,897,062 )	(3,230,720 )
Other (expense) income:				
Interest expense	(1,119,273 )	(1,728,799 )	(2,072,829 )	(2,561,207 )
Debt conversion expense	—	(275,534 )	—	(275,534 )
Grant income	11,361	33,314	70,149	37,983
Total other expense:	(1,107,912 )	(1,971,019 )	(2,002,680 )	(2,798,758 )
Net loss	(2,574,146 )	(3,599,910 )	(4,899,742 )	(6,029,478 )
Net loss attributable to noncontrolling interest	(173,911 )	(95,331 )	(237,167 )	(201,975 )
Net loss attributable to common shareholders	\$(2,400,235 )	\$(3,504,579 )	\$(4,662,575 )	\$(5,827,503 )
Net loss per share attributable to common shareholders:				
Loss per share attributable to shareholders – basic and diluted	\$(0.03 )	\$(0.03 )	\$(0.05 )	\$(0.05 )
	97,770,161	118,748,451	94,718,273	111,760,954

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Weighted average number of common shares  
outstanding:

Comprehensive loss:

Net loss	\$(2,574,146 )	\$(3,599,910 )	\$(4,899,742 )	\$(6,029,478 )
Foreign currency translation	32,150	13,325	(15,986 )	1,133
Comprehensive loss	(2,541,966 )	(3,586,585 )	(4,915,728 )	(6,028,345 )
Comprehensive loss attributable to noncontrolling interest	(173,911 )	(95,331 )	(237,167 )	(201,975 )
Comprehensive loss attributable to common stockholders	\$(2,368,085 )	\$(3,491,254 )	\$(4,678,561 )	\$(5,826,370 )

*See accompanying notes to unaudited consolidated financial statements.*



Table of Contents**BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT  
FOR THE SIX MONTHS ENDED JUNE 30, 2018**

(UNAUDITED)

	Common stock		Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive loss		Non- controlling interest	Total
	Shares	Amount						
Balance, December 31, 2017	104,164,465	\$ 69,871	\$ 97,093,144	\$(101,204,846)	\$ (62,489 )	\$ 694,699	\$(3,409,621)	
Conversion of principal due on notes	19,298,723	12,939	6,215,280	—	—	—	6,228,219	
Issuance of common stock for services	1,448,257	976	445,512	—	—	—	446,488	
Issuance of common stock for interest	1,919,806	1,341	492,486	—	—	—	493,827	
Financing fee in stock	252,385	168	84,905	—	—	—	85,073	
Sale of stock for cash	1,275,371	855	379,948	—	—	—	380,803	
Warrant exercise price reduction for cash	—	—	148,853	—	—	—	148,853	
Stock option compensation expense	—	—	696,001	—	—	—	696,001	
Warrants and beneficial conversion feature issued as discount on convertible notes payable, note payable and line of credit	—	—	314,251	—	—	—	314,251	
Deemed dividend	—	—	297,439	(297,439 )	—	—	—	

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Net loss	—	—	—	(5,827,503 )	—	(201,975 )	(6,029,478)
Foreign currency translation	—	—	—	—	1,133	—	1,133
Balance, June 30, 2018	128,359,007	\$86,150	\$106,167,819	\$(107,329,788)	\$(61,356 )	\$492,724	\$(644,451 )

*See accompanying notes to unaudited consolidated financial statements.*

Table of Contents**BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS  
FOR THE SIX MONTHS ENDED JUNE 30, 2017 AND 2018****(UNAUDITED)**

	<b>JUNE</b>	<b>JUNE</b>
	<b>30, 2017</b>	<b>30, 2018</b>
Cash flows from operating activities		
Net loss	\$(4,899,742)	\$(6,029,478)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock option compensation expense	515,959	696,001
Common stock issued for interest and fees for services from consultants	504,263	930,315
Interest expense related to amortization of the discount on convertible notes payable	1,723,396	2,019,193
Debt conversion expense	—	275,534
Deferred offering cost expense	—	8,451
Bad debt expense	15,000	1,000
Depreciation and amortization expense	14,439	22,859
Changes in assets and liabilities:		
Accounts receivable	(25,111 )	3,436
Inventory	(2,461 )	28,334
Prepaid expenses and other current assets	(8,706 )	(39,308 )
Accounts payable and accrued expenses	144,335	30,552
Officer bonus	(80,000 )	—
Deposit	50,000	—
Net cash used in operating activities	\$(2,048,628)	\$(2,053,111)
Cash flows from investing activities		
Leasehold improvements	\$—	\$(26,356 )
Net cash used in investing activities	\$—	\$(26,356 )
Cash flows from financing activities		
Proceeds from line of credit	\$250,000	\$390,000
Proceeds from convertible notes	225,000	462,500
Proceeds from conversion inducement	—	356,781
Proceeds from warrant exercise-price reduction	—	148,854
Proceeds from sale of stock to Lincoln Park Capital	—	380,803
Purchase of Clyra shares	(40,000 )	—
Proceeds from exercise of warrants	153,000	—
Net cash provided by financing activities	\$588,000	\$1,738,938
Effect of foreign currency translation	(15,986 )	1,113
Net change in cash and cash equivalents	\$(1,476,614)	\$(339,396 )
Cash and cash equivalents at beginning of period	\$1,910,153	\$990,457

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Cash and cash equivalents at end of period	\$433,539	\$651,061
Supplemental disclosures of cash flow information		
Cash paid during the period for:		
Interest	\$4,487	\$5,489
Income taxes	\$5,350	\$5,719
Non-cash investing and financing activities:		
Fair value of common stock issued for financing commitments	\$—	\$85,073
Fair value of warrants issued in conjunction with convertible notes payable	\$225,000	\$314,251
Deemed dividend	\$—	\$297,439
Fair value of stock issued for equipment	\$—	\$10,000
Exercise of stock options	\$1,677	\$—
Conversion of notes into shares of common stock	\$530,000	\$5,595,904

*See accompanying notes to unaudited consolidated financial statements*

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BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

**Note 1. Business and Liquidity**

**Description of Business**

We are an innovation company driven by our mission to “make life better” by developing breakthrough platform technologies, nurturing and building businesses around the intellectual property, while providing capital and support along the journey from “cradle” to “maturity”. We currently have two segments generating operational revenue: (i) Odor-No-More, selling odor and volatile organic compound (“VOC”) control products and services, and (ii) BioLargo Engineering, Science & Technologies, LLC (“BLEST”), providing professional engineering services to third party clients as well as working on our product development projects. We have a research and development facility in Canada, and consolidate our financials with our partially owned subsidiary, Clyra Medical Technologies, Inc., a company focused on commercializing our technologies in the medical field (see Note 9).

**Liquidity / Going Concern**

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying consolidated financial statements, for the six months ended June 30, 2018 we had a net loss of \$6,029,478, and used \$2,053,111 cash in operations, and at June 30, 2018, had negative working capital of \$120,187, current assets of \$823,302, and an accumulated stockholders’ deficit of \$107,329,788. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies and achieve profitable operations by licensing or otherwise commercializing products incorporating our technologies. The consolidated financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Our total cash balance was \$651,061 at June 30, 2018. We had revenues of \$589,767 in the six months ended June 30, 2018, which amount was not sufficient to fund our operations. We believe our current cash position is insufficient to maintain our

current level of operations and research/development, and that we will be required to raise substantial additional capital to continue our operations and fund our future business plans. We intend to continue to raise money through private securities offerings for the foreseeable future, and through our agreement with Lincoln Park (see Note 4).

At times in the past we have not had enough cash or sources of capital to pay our accounts payable and expenses as they arise, and have relied on the issuance of stock options and common stock, as well as extended payment terms with our vendors, to continue to operate. We will be required to raise substantial additional capital to expand our operations, including without limitation, hiring additional personnel, additional scientific and third-party testing, costs associated with obtaining regulatory approvals and filing additional patent applications to protect our intellectual property, and possible strategic acquisitions or alliances, as well as to meet our liabilities as they become due for the next 12 months.

The unaudited consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to Rule 8-03 of Regulation S-X under the Securities Act of 1933, as amended. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. For some of our activities, we are still operating in the early stages of the sales and distribution process, and therefore our operating results for the six months ended June 30, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018, or for any other period. These unaudited consolidated financial statements and notes should be read in conjunction with the Company's audited consolidated financial statements and accompanying notes included in the Annual Report on Form 10-K for the year ended December 31, 2017 filed with the Securities and Exchange Commission (the "SEC") on March 14, 2018.

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BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

**Note 2. Summary of Significant Accounting Policies**

In the opinion of management, the accompanying balance sheet and related statements of operations, cash flows, and stockholders' deficit include all adjustments, consisting only of normal recurring items, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America.

**Principles of Consolidation**

The consolidated financial statements include the accounts of the Company, its majority owned subsidiaries, and Clyra. Management believes Clyra's financial statements are appropriately consolidated with that of the Company after reviewing the guidance of ASC Topic 810, "Consolidation", because the Company owns 46.3% of its outstanding voting stock at June 30, 2018, and two members of BioLargo's board of directors are two of three members of Clyra's board of directors (see Note 9). All intercompany accounts and transactions have been eliminated.

**Foreign Currency**

The Company has designated the functional currency of Biolargo Water, Inc., our Canadian subsidiary, to be the Canadian dollar. Therefore, translation gains and losses resulting from differences in exchange rates are recorded in accumulated other comprehensive income.

**Cash and Cash Equivalents**

The Company considers all highly liquid investments with maturities of three months or less when acquired to be cash equivalents. Substantially all cash equivalents are held in short-term money market accounts at one of the largest financial institutions in the United States. Our cash account balances are typically greater than the Federal Deposit

Insurance Corporation insurance limit of \$250,000 per owner per bank, and during such times, we are exposed to credit loss for amounts in excess of insured limits in the event of non-performance by the financial institution. We do not anticipate non-performance by our financial institution.

Clyra Medical is not a wholly owned subsidiary. Our cash balance held in Clyra and BioLargo and other subsidiaries are reflected in the following table:

	<b>December</b>	<b>June</b>
	<b>31, 2017</b>	<b>30, 2018</b>
Biolargo, Inc. and wholly owned subsidiaries	\$ 461,914	\$467,258
Clyra Medical Technologies, Inc.	528,543	183,803
Total	\$ 990,457	\$651,061

**Accounts Receivable**

Trade accounts receivable are recorded net of allowances for doubtful accounts. Estimates for allowances for doubtful accounts are determined based on payment history and individual customer circumstances. The allowance for doubtful accounts as of December 31, 2017 and June 30, 2018 was \$2,500 and \$3,500, respectively.



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BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Credit Concentration

We have a limited number of customers that account for significant portions of our revenue. During the six months ended June 30, 2017 and 2018, we had three and two customers that each accounted for more than 10% of consolidated revenues in the respective periods, as follows:

	<b>June</b>		<b>June</b>	
	<b>30,</b>		<b>30,</b>	
	<b>2017</b>		<b>2018</b>	
Customer A	17 %		43 %	
Customer B	16 %		15 %	
Customer C	14 %		<10 %	

In addition, our customers include many of the largest solid waste handling companies in the United States. We generally do business with these companies through “national purchasing agreements” entered into with the company, and then sell our products and services to their local operations such as transfer stations and landfills. Although none of those individual locations arose to more than 10% of our consolidated revenues during the six months ended June 30, 2018, two of these national companies accounted for 37% of our total revenues.

We had five customers that each accounted for more than 10% of consolidated accounts receivable at December 31, 2017 and three customers at June 30, 2018 as follows:

	<b>December</b>		<b>June</b>	
	<b>31, 2017</b>		<b>30,</b>	
			<b>2018</b>	
Customer A	12	%	<10	%
Customer B	19	%	<10	%

Customer C	12	%	<10	%
Customer D	10	%	<10	%
Customer E	10	%	<10	%
Customer F	<10	%	13	%
Customer G	<10	%	12	%
Customer H	<10	%	10	%

**Inventory**

Inventory is stated at the lower of cost and net realizable value using the average cost method. All inventory is related to our Odor-No-More business segment. Inventory consisted of:

	<b>December</b>	<b>June</b>
	<b>31, 2017</b>	<b>30,</b> <b>2018</b>
Raw material	\$ 34,104	\$23,515
Finished goods	19,869	2,124
Total	\$ 53,973	\$25,639

**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, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ from those estimates. Estimates are used when accounting for stock-based transactions, debt transactions, deemed dividends, allowance for bad debt, asset depreciation and amortization, among others.

The methods, estimates and judgments we use in applying these most critical accounting policies have a significant impact on the results of our consolidated financial statements.

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BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

**Share-based Payments**

For stock and stock options issued to consultants and other non-employees for services, the Company measures and records an expense as of the earlier of the date at which either: a commitment for performance by the non-employee has been reached or the non-employee's performance is complete. The equity instruments are measured at the current fair value, and for stock options, the instruments are measured at fair value using the Black Scholes option model.

For equity instruments issued and outstanding where performance is not complete, but the instrument has been recorded, those instruments are measured again at their then current fair market values at each of the reporting dates (they are "marked-to market") until the performance and the contract are complete.

**Warrants**

The Unit Offerings of our convertible promissory note and a Series A stock purchase warrant are accounted for under the fair value and relative fair value method.

The warrant is first analyzed per its terms as to whether it has derivative features or not. If the warrant is determined to be a derivative, then it is measured at fair value using the Black Scholes Option Model, and recorded as a liability on the balance sheet. The warrant is re-measured at its then current fair value at each subsequent reporting date (it is "marked-to-market").

If the warrant is determined to not have derivative features, it is recorded into equity at its fair value using the Black Scholes option model, however, limited to a relative fair value based upon the percentage of its fair value to the total fair value including the fair value of the convertible note.

The convertible note is recorded at its fair value, limited to a relative fair value based upon the percentage of its fair value to the total fair value including the fair value of the warrant. Further, the convertible promissory note is examined for any intrinsic beneficial conversion feature (“BCF”) of which the convertible price of the note is less than the closing stock price on date of issuance. If the relative fair value method is used to value the convertible promissory note and there is an intrinsic BCF, a further analysis is undertaken of the BCF using an effective conversion price which assumes the conversion price is the relative fair value divided by the number of shares the convertible debt is converted into by its terms. The adjusted BCF value is accounted for as equity.

The warrant and BCF relative fair values are also recorded as a discount to the convertible promissory notes. As present, these equity features of the convertible promissory notes have recorded a discount to the convertible notes that is substantially equal to the proceeds received.

### **Non-Cash Transactions**

We have established a policy relative to the methodology to determine the value assigned to each intangible we acquire, and/or services or products received for non-cash consideration of our common stock. The value is based on the market price of our common stock issued as consideration, at the date of the agreement of each transaction or when the service is rendered or product is received.

### **Revenue Recognition**

We adopted ASU 2014-09, “Revenue from Contracts with Customers”, Topic 606, on January 1, 2018. The guidance focuses on the core principle for revenue recognition.

The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps:

Step 1: Identify the contract(s) with a customer.

Step 2: Identify the performance obligations in the contract.



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BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Step 3: Determine the transaction price.

Step 4: Allocate the transaction price to the performance obligations in the contract.

Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

We have revenue from two subsidiaries, Odor-No-More and BLEST. Odor-No-More identifies its contract with the customer through a purchase order whether in writing or verbal, in which the details of the contract are defined including the transaction price and method of shipment. The only performance obligation is to create and ship the product and each product has separate pricing. Odor-No-More recognizes revenue at a point in time when the order for its goods are shipped if its agreement with the customer is FOB Odor-No-More's warehouse facility, and when goods are delivered to its customer if its agreement with the customer is FOB destination. Revenue is recognized with a reduction for sales discounts, as appropriate and negotiated in the customer's purchase order.

BLEST identifies services to be performed in a written contract, which specifies the performance obligations and the rate at which the services will be billed. Each service is separately negotiated and priced. Revenue is recognized over a period of time as services are performed and completed. BLEST's contracts typically call for invoicing on a time and materials basis. To date, there have been no discounts or other financing terms for the contracts.

In the future, we may generate revenues from royalties or license fees from our intellectual property. In the event we do so, we anticipate a licensee would pay a license fee in one or more installments and ongoing royalties based on their sales of products incorporating or using our licensed intellectual property. Upon entering into a licensing agreement, we will determine the appropriate method of recognizing the royalty and license fees.

Government Grants

We have been awarded multiple research grants from the Canadian National Research Institute – Industrial Research Assistance Program (NRC-IRAP) and the National Science and Engineering Research Council of Canada (NSERC). The grants received are considered other income and are included in our consolidated statements of operations. We received our first grant in 2015 and have been awarded over 50 grants totaling approximately \$1,600,000. Some of the funds from these grants are given directly to third parties (such as the University of Alberta or a third-party research scientist) to support research on our technology. The grants have terms generally ranging between six and eighteen months and support a majority, but not all, of the related research budget costs. This cooperative research allows us to utilize (i) a depth of resources and talent to accomplish highly skilled work, (ii) financial aid to support research and development costs, (iii) independent and credible validation of our technical claims.

The grants typically provide for (i) recurring monthly amounts, (ii) reimbursement of costs for research talent for which we invoice to request payment, and (iii) ancillary cost reimbursement for research talent travel related costs. All awarded grants have specific requirements on how the money is spent, typically to employ researchers. None of the funds may be used for general administrative expenses or overhead in the United States. These grants have substantially increased our level of research and development activities in Canada. We continue to apply for Canadian government and agency grants to fund research and development activities. Not all of our grant applications have been awarded, and no assurance can be made that any pending grant application, or any future grant applications, will be awarded.

While the FASB has issued a proposed Accounting Standards Update, Not-for-Profit Entities - (Topic 958): “Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made”, there has been no guidance related to for profit entities such as BioLargo. In reviewing Topic 606, “Revenue from Contracts with Customers”, and its potential application to the Canadian government grants, the Management concluded that these grants do not meet the requirements for revenue recognition. Specifically, these grants typically provide reimbursement for research personnel working on the BioLargo technology. For some grants, funds are given directly to third parties for research on our technology and are not controlled by the Company. In this structure, the grants are not revenue, but rather a reimbursement.

### **Business Segment Information**

In 2017, the Company operated with three business segments. In 2018, given the increased operations of the engineering division formed in late 2017, we determined that it should be considered our fourth business segment. This decision was based on the manner in which the chief operating decision maker now manages the engineering division, including resource allocation and performance assessment.

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## BIOLARGO, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Our four business segments include: (i) Odor-No-More, which is engaged in developing and selling odor and VOC control products and services; (ii) BLEST, which provides professional engineering services; (iii) Clyra, which is engaged in developing medical products utilizing our technology, with an emphasis in the medical field and advanced wound care; and (iv) our corporate operations (labeled in the below table as “BioLargo/Other”), which includes certain functional roles that do not engage in revenue generating activities, such as general corporate and administrative functions, including finance, human resources, marketing, legal, and research and development.

The segment information for the three and six months ended June 30, 2017 and 2018, is as follows:

	<b>Three months June 30,</b>		<b>Six months June 30,</b>	
	<b>2017</b>	<b>2018</b>	<b>2017</b>	<b>2018</b>
<b>Revenues</b>				
Odor-No-More	\$99,978	\$315,553	\$145,995	\$539,950
BLEST	—	11,185	—	49,817
Consolidated revenue	\$99,978	\$326,738	\$145,995	\$589,767
<b>Cost of goods/services</b>				
Odor-No-More	\$(73,399 )	\$(194,000 )	\$(95,929 )	\$(328,464 )
BLEST	—	(6,912 )	—	(35,640 )
Consolidated costs of goods/services	\$(73,399 )	\$(200,912 )	\$(95,929 )	\$(364,104 )
<b>Net loss</b>				
Odor-No-More	\$(100,000 )	\$(53,688 )	\$(275,000 )	\$(253,688 )
BLEST	—	(70,339 )	—	(116,726 )
Clyra	(347,490 )	(177,641 )	(484,572 )	(376,362 )
BioLargo/Other	(2,126,656)	(3,298,242)	(4,140,170)	(5,282,702)
Consolidated net loss	\$(2,574,146)	\$(3,599,910)	\$(4,899,742)	\$(6,029,478)

The segment information as of December 31, 2017 and June 30, 2018, is as follows:

**December    June**



	<b>31, 2017</b>	<b>30, 2018</b>
Assets, net		
Odor-No-More	\$210,725	\$260,421
BLEST	—	131,558
Clyra	528,543	183,803
BioLargo/Other	726,152	591,826
Consolidated assets, net	\$1,495,420	\$1,167,608

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**Earnings (Loss) Per Share**

We report basic and diluted earnings (loss) per share (“EPS”) for common and common share equivalents. Basic EPS is computed by dividing reported earnings by the weighted average shares outstanding. Diluted EPS is computed by adding to the weighted average shares the dilutive effect if stock options and warrants were exercised into common stock. For the six months ended June 30, 2017 and 2018, the denominator in the diluted EPS computation is the same as the denominator for basic EPS due to the anti-dilutive effect of the warrants and stock options on the Company’s net loss.

**Recent Accounting Pronouncements**

In June 2018, The FASB issued Accounting Standards Update No. 2018-07, “Compensation - Stock Compensation (topic 718): Improvements to Nonemployee Share-Based Payment Accounting”. The amendments in this update expand the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. An entity should apply the requirements of Topic 718 to nonemployee awards except for specific guidance on inputs to an option pricing model and the attribution of cost (that is, the period of time over which share-based payment awards vest and the pattern of cost recognition over that period). The amendments specify that Topic 718 applies to all share-based payment transactions in which a grantor acquires goods or services to be used or consumed in a grantor’s own operations by issuing share-based payment awards. The amendments also clarify that Topic 718 does not apply to share-based payments used to effectively provide (1) financing to the issuer or (2) awards granted in conjunction with selling goods or services to customers as part of a contract accounted for under Topic 606, Revenue from Contracts and Customers. The amendments in this update are effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Management has not concluded its evaluation of the guidance. Its initial analysis is that it does not believe the new guidelines will substantially impact the company’s financial statements.

In May 2017, the FASB issued Accounting Standards Update No. 2017-09, “Compensation – Stock Compensation (topic 718): Scope of Modification Accounting”. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. An entity should account for the effects of a modification unless all the following are met: (i) the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the modified award is the same as the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used)

of the original award immediately before the original award is modified, (ii) The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified and (iii) the classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. The amendments in this Update are effective for all entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Management has analyzed the new guideline and it has not substantially impacted its accounting for stock compensation awards upon adoption in the current period.

### **Note 3. Change in Derivative Liability Treatment**

Biolargo adopted Accounting Standards Update (“ASU”) No. 2017-11 as of July 1, 2017. With this adoption, we eliminated the derivative liability, and the changes in the fair value of the derivative liability, related to negative covenants in multiple warrants issued that required a reduction of warrant exercise price under certain circumstances. The Company made a cumulative effect adjustment to the consolidated balance sheet as of January 1, 2017, which adjusted the beginning balance in the accumulated deficit account by \$663,560. The comparable unaudited prior year periods for the three and six months ended June 30, 2017 are being presented to reflect the adoption of this ASU for all interim periods in 2017.

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**Note 4. Lincoln Park Financing**

On August 25, 2017, we entered into a stock purchase agreement (“LPC Purchase Agreement”) with Lincoln Park Capital Fund, LLC (“Lincoln Park”), pursuant to which Lincoln Park agreed to purchase from us at our request up to an aggregate of \$10,000,000 of our common stock (subject to certain limitations) from time to time over a period of three years. Concurrently, we entered into a registration rights agreement with Lincoln Park (“LPC RRA”), pursuant to which we were required to file with the Securities and Exchange Commission (“SEC”) a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, the shares of common stock that have been or may be issued to Lincoln Park under the LPC Purchase Agreement. The registration statement was filed, and on September 22, 2017, it was deemed effective by the SEC. The LPC Purchase Agreement allows us, from time to time and at our sole discretion, to direct Lincoln Park to purchase shares of our common stock, subject to limitations in both volume and dollar amount. The volume of shares is limited to a maximum of 50,000 shares if our stock closes at less than \$0.50 per share, 75,000 if it closes from \$0.50 to \$0.74 per share, 100,000 if it closes from \$0.75 to \$1.24 per share, and 200,000 if it closes at or above \$1.25 per share. The maximum dollar amount for any single purchase is \$500,000. There are no trading volume requirements under the LPC Purchase Agreement, and we alone control the timing and amount of any sales of our common stock to Lincoln Park. The purchase price of the shares that may be sold to Lincoln Park under the Purchase Agreement is the lower of (i) the lowest sale price on the date of purchase, or (ii) the average of the three lowest closing prices in the prior 12 business days. The purchase price per share will be equitably adjusted for any reorganization, recapitalization, non-cash dividend, stock split, or other similar transaction occurring during the business days used to compute such price. We may at any time in our sole discretion terminate the LPC Purchase Agreement without fee, penalty or cost upon one business day notice. There are no restrictions on future financings, rights of first refusal, participation rights, penalties or liquidated damages in the LPC Purchase Agreement or LPC RRA other than a prohibition on entering into a “Variable Rate Transaction,” as defined in the Purchase Agreement. Lincoln Park may not assign or transfer its rights and obligations under the Purchase Agreement.

In consideration for entering into the LPC Purchase Agreement, on August 25, 2017, we issued to Lincoln Park 488,998 shares of common stock as an “initial commitment fee.” For no additional consideration, when and if Lincoln Park purchases (at the Company’s discretion) any portion of the \$10,000,000 aggregate commitment, we are required to issue up to 488,998 shares, pro-rata, as “additional commitment shares”. For example, if we elect, at our sole discretion, to require Lincoln Park to purchase \$25,000 of our stock, then we would issue 1,222 additional commitment shares, which is the product of \$25,000 (the amount we have elected to sell) divided by \$10,000,000 (total amount we can sell Lincoln Park pursuant to the LPC Purchase Agreement) multiplied by 488,998 (the total number of additional commitment shares). The additional commitment shares will only be issued pursuant to this formula as and when we elect at our discretion to sell stock to Lincoln Park.

From inception of the contract in August 2017 through June 30, 2018, we elected to sell Lincoln Park shares of our common stock for which we received \$891,888, and issued Lincoln Park 2,431,751 shares, and 43,611 “additional commitment shares”. We recorded the stock sale in our equity statement and the additional shares issued as a fee for the transaction was offset against the shares issued.

During the six-months ended June 30, 2018, we elected to sell to Lincoln Park 1,256,751 shares of our common stock for which we received \$380,803 in gross and net proceeds. As a result of these purchases, we issued Lincoln Park 18,260 “additional commitment” shares pursuant to the LPC Purchase Agreement.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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**Note 5. Debt Obligations**

The following table summarizes our debt obligations outstanding as of December 31, 2017 and June 30, 2018.

	<b>December</b>	<b>June</b>
	<b>31, 2017</b>	<b>30, 2018</b>
<b>Current liabilities</b>		
Convertible notes payable		
One-year convertible notes, mature July 18, 2018 *	\$280,000	\$280,000
Convertible notes, mature June 1, 2018	4,468,847	—
Nine-month convertible note, matures September 18, 2018	500,000	447,975
Nine-month convertible note, matures October 16, 2018 *	—	54,239
Total convertible notes payable	\$5,248,847	\$782,214
<b>Long-term liabilities:</b>		
Line of credit, matures September 1, 2019	\$—	\$390,000
Convertible notes payable		
Convertible note, matures July 20, 2019	\$440,000	\$440,000
Convertible notes, mature June 17, 2019	283,571	—
Convertible notes, mature December 31, 2019	292,000	75,000
Note payable, matures March 8, 2023 (or on demand 60 days' notice)	—	50,000
Convertible notes, mature June 20, 2020	523,700	125,000
Convertible notes, mature April 20, 2021		100,000
Convertible notes, mature June 15, 2021	—	82,500
Total convertible notes payable	\$1,539,271	\$872,500
Total	\$6,788,118	\$2,044,714

\* Subsequent to June 30, 2018 these notes were converted to common stock (see Note 12 "Subsequent Events").

See our Annual Report on Form 10-K for the year ended December 31, 2017, for a complete description of the debt obligations set forth in the above table.

**Early Conversion of Unit Notes**

Prior to their maturity dates, we issued 17,255,811 shares of our common stock in satisfaction of \$4,626,238 of convertible promissory notes issued in our “unit” offerings at varying conversion prices, maturing on the following dates:

	Debt
	converted
	to stock
Current liabilities	
Convertible notes, mature June 1, 2018	\$3,646,967
Long-term liabilities	
Convertible notes, mature June 17, 2019	283,571
Convertible notes, mature December 31, 2019	217,000
Convertible notes, mature June 20, 2020	478,700
Total debt converted May 2018	\$4,626,238

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These conversions were voluntary on the part of the noteholders and prior to the various maturity dates on notes that were issued in prior “unit” offerings conducted by the Company (2015 Unit Offering, Winter 2016 Unit Offering, and Summer 2017 Unit Offering). We offered these noteholders incentives to convert their notes early. Noteholders with conversion prices of \$0.25 and \$0.30 were offered incentive shares equal to one and one-half times the number of shares issuable for the payment of interest that would accrue from the last interest payment date of March 20, 2018, through the maturity of the note, at a fixed price of \$0.25 per share (for example, a note that would have yielded \$1,000 in interest, would receive 1,000 times 1.5 divided by 0.25 equals 6,000 incentive shares). We offered holders of notes with conversion prices higher than \$0.30 the ability to reduce their conversion price to \$0.30 by paying additional funds equal to six or twenty percent of their original investment (6% for notes with original conversion prices of \$0.35, and 20% for notes with original conversion prices of \$0.55 and \$0.57). The additional funds did not increase the amount of the note payable, nor did the reduced conversion price affect the number of shares purchasable under the warrant issued with their “unit” investment. Holders of 40 notes elected to pay an aggregate \$356,781 to reduce the conversion prices of their notes to \$0.30. As a result of the reduction in conversion prices, an additional 2,749,197 shares were issuable pursuant to the notes upon conversion. The fair value of these additional shares was \$632,315. Additional interest expense of \$275,534 is recorded as part of the debt conversion and is the amount by which the fair value of the additional shares exceeded the cash received by the Company. Holders of 41 notes with original conversion prices of \$0.30 and \$0.25 elected to convert early and received 966,318 additional “incentive shares” for their agreement to do so.

**Conversion of Unit Notes**

On June 1, 2018, we (BioLargo, Inc., the “Company”) elected to convert the \$821,880 outstanding promissory notes remaining in our 2015 Unit Offering on their June 1, 2018 maturity date into 2,488,819 shares of our common stock. Of the shares issued, 2,411,004 were issued in satisfaction of principal amounts due on notes with conversion prices of \$0.25, \$0.35, and \$0.55, and 77,815 were issued in satisfaction of \$19,725 of accrued and unpaid interest.

**Convertible Note, matures September 18, 2018 (Vista Capital)**

On December 18, 2017, we received \$500,000 pursuant to a securities purchase agreement (the “Vista Purchase Agreement”) and a registration rights agreement (the “Vista RRA”) with Vista Capital Investments, LLC (“Vista Capital”), and issued a Note (the “Vista Note”) in the aggregate principal amount of \$500,000 at 5% annual interest, which was originally convertible into shares of common stock of the Company at \$0.394 per share, subject to the terms, and



certain limitations and conditions, set forth in the Vista Purchase Agreement and Vista Note. The Vista Note matures on September 18, 2018. The Company reserved 1,269,036 shares of common stock for issuance upon conversion of the Vista Note.

Pursuant to the Vista Purchase Agreement, the Company issued 250,000 shares of common stock to Vista Capital as a commitment fee at \$0.39 per share and \$98,500 is recorded as a discount on convertible notes and will amortize to interest expense over the term of the note.

Pursuant to the Vista RRA, the Company agreed to file a registration statement with the SEC registering all shares of common stock into which the Vista Note is convertible, and the 250,000 shares issued as a commitment fee. The Vista Purchase Agreement requires additional shares be issued for the commitment fee in the event the closing price of our common stock on the date the registration statement is deemed effective is lower than the closing price on December 18, 2017, (which was \$0.41). In such event, additional shares would be issued such that the aggregate shares issued have the same value as the 250,000 shares issued on December 18, 2017. The beneficial conversion feature resulted in a \$20,305 relative fair value recorded as a discount. The discount will be amortized monthly to interest expense through September 18, 2018.

Vista Capital represented to the Company, among other things, that it was an “accredited investor” (as such term is defined in Rule 501(a) of Regulation D under the Securities Act of 1933, as amended). The Vista Note, Vista Purchase Agreement, and Vista RRA contain customary representations, warranties, agreements and conditions including indemnification rights and obligations of the parties. The Vista Note contains a price protection provision such that if we issue a security with any term more favorable to the holder of such security that was not similarly provided in the Vista Note, then we shall notify Vista Capital of such additional or more favorable term and such term, at its option, shall become a part of the Vista Note. As a result of our sale of common stock at \$0.25, the conversion price of the Vista Note was reduced from \$0.394 to \$0.25.

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In June 2018, Vista Capital elected to convert \$52,025 of the outstanding principal balance of the Vista Note and we issued 208,100 shares, plus shares for interest that had accrued through the date of conversion. As of June 30, 2018, the outstanding balance on the Vista Note is \$447,975.

**FirstFire Investment (was scheduled to mature October 16, 2018)**

On January 16, 2018, we entered into a securities purchase agreement (the “FirstFire Purchase Agreement”) and a registration rights agreement (the “FirstFire RRA”) with FirstFire Global Opportunity Fund, LLC (“FirstFire”), and issued a convertible promissory note (the “FirstFire Note”) in the aggregate principal amount of \$150,000 at 5% annual interest, which is convertible into shares of common stock of the Company at \$0.394 per share, subject to the terms, and certain limitations and conditions set forth in the FirstFire Purchase Agreement and FirstFire Note. FirstFire may convert the FirstFire Note at any time. The FirstFire Note was scheduled to mature on October 16, 2018. In June 2018, FirstFire elected to convert \$95,761 of the outstanding principal balance of the FirstFire Note and we issued 383,047 shares. As of June 30, 2018, the FirstFire Note outstanding balance is \$54,239. Subsequent to June 30, 2018, FirstFire elected to convert the remaining amount due on its note (see Note 12).

Pursuant to the FirstFire Purchase Agreement, the Company issued 75,000 shares of common stock to FirstFire as a commitment fee (the “FirstFire Commitment Shares”) at \$0.39 per share and \$29,250 is recorded as a discount on convertible notes and will amortize to interest expense over the term of the note.

Under the Note and FirstFire Purchase Agreement, the Company has reserved 394,949 shares of common stock for issuance upon conversion of the Note. Pursuant to the FirstFire RRA, the Company agreed to file a registration statement with the SEC registering all shares of common stock into which the FirstFire Note is convertible, and the FirstFire Commitment Shares. The FirstFire Purchase Agreement allows for an adjustment to the number of FirstFire Commitment Shares in the event the closing price of our common stock, on the earlier of the date the registration statement is deemed effective and 20 trading days following the six-month anniversary of the FirstFire Note, is lower than the closing price on January 16, 2018 (which was \$0.39). In such event, additional shares would be issued to FirstFire such that the aggregate FirstFire Commitment Shares issued have the same value as the shares issued on January 16, 2018.

Pursuant to the requirements set forth in the registration rights agreements, we filed a registration statement with the SEC which was deemed effective as of February 8, 2018. On February 8, 2018, our common stock last traded at \$0.3147 per share. Because the last traded price of our common stock on the date the registration statement was deemed effective was less than the price of our common stock on the dates of the FirstFire Purchase Agreements, at their option, we are required to issue additional “commitment shares”. FirstFire exercised that right, and we issued 36,536 additional shares of our common stock and \$11,498 is recorded as additional discount on convertible notes and will amortize to interest expense over the term of the note.

FirstFire represented to the Company, among other things, that it was an “accredited investor” (as such term is defined in Rule 501(a) of Regulation D under the Securities Act of 1933, as amended). The FirstFire Note, FirstFire Purchase Agreement, and the FirstFire RRA contain customary representations, warranties, agreements and conditions including indemnification rights and obligations of the parties. The FirstFire Note contains a price protection provision such that if we issue a security with any term more favorable to the holder of such security that was not similarly provided in the FirstFire Note, then the Company shall notify FirstFire of such additional or more favorable term and such term, at its option, shall become a part of the FirstFire Note. As a result of our sale of common stock at \$0.25, the conversion price of the FirstFire Note was reduced from \$0.394 to \$0.25.

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**Line of credit, matures September 1, 2019**

On March 1, 2018, we received \$390,000 pursuant to a line of credit, accruing interest at a rate of 18% per annum, for which we have pledged our inventory and accounts receivable as collateral. Interest is paid quarterly, and, at the option of the holder, payable in either (i) cash, (ii) our common stock, calculated based on the 20-day average closing price, or (iii) options to purchase our common stock, priced at the 20-day average closing price, the number of shares doubled, and expiring 10 years from the date of grant. The holder of the line of credit has the right to call due the outstanding principal amount on 30-days' notice at any time after September 1, 2019.

Each investor, for no additional consideration, received a warrant to purchase our common stock. (See Note 7). The warrant allows for the purchase of the number of common shares equal to the investment amount (e.g., one warrant share for each dollar invested).

**Two-Year Convertible Note, matures July 20, 2019**

On July 20, 2017, the Company accepted \$400,000 and issued a promissory note with a 10% original issue discount in the principal amount of \$440,000, matures July 20, 2019 and accrues interest at 12%. The note originally provided that interest was to be paid quarterly beginning October 1, 2017, in either cash, common stock, or an option to purchase common stock, in the holder's discretion. On January 25, 2018, the interest provisions in the note were modified such that the 12% annual simple interest is due at maturity.

At maturity, the principal amount of the note and any accrued and unpaid interest automatically converts, at the holder's option, into either BioLargo common shares at \$0.42 per share, 2,000 shares of Clyra Medical Technologies common stock held by BioLargo, or any combination thereof. The fair value of the beneficial conversion feature resulted in a \$171,429 recorded on our consolidated balance sheet as a discount on convertible notes payable, net of current portion. The discount will be amortized monthly as interest expense through July 20, 2019.

**Note payable, matures March 8, 2020**

On March 8, 2018, we received \$50,000 and entered into a note payable. The note is due on upon demand from the noteholder, with sixty days' notice. The demand may not be made before June 30, 2018, and in the absence of the demand, the maturity date is March 8, 2023. In lieu of interest, we issued the note holder a warrant to purchase 150,000 shares of our common stock at an exercise price of \$0.35. The warrant expires February 28, 2023. The shares available for purchase vest in increments of 6,250 shares per month. (See Note 7.)

**Convertible Notes, mature June 20, 2020 (Summer 2017 Unit Offering)**

On May 24, 2017, we commenced a private securities offering (titled the "Summer 2017 Unit Offering") which offered the sale of \$1,500,000 of "Units," each Unit consisting of a convertible promissory note and stock purchase warrant. Concurrently, we issued Pricing Supplement No. 1 setting the initial unit/conversion price at \$0.42 per share, and the initial warrant exercise price at \$0.65 per share. The promissory notes issued to investors mature June 20, 2020, and bear interest at the rate of 12% per annum on the amount invested. Any interest due will be paid quarterly in arrears in cash or shares of common stock. If paid by the issuance of common stock, interest is paid at a conversion price equal to the average closing price of the Company's common stock over the 20 trading days prior to the interest payment due date. The principal amount of the note may be paid by the issuance of shares of common stock, or cash, upon maturity at the Company's election. Promissory notes may be converted at any time by the investor, at maturity by the Company, or by the Company prior to maturity, so long as the following conditions are met: (i) the Shares issued as payment are registered with the SEC; and (ii) the Company's common stock closes for ten consecutive trading days at or above three times the Unit price.

In addition to the convertible promissory note, each investor received a warrant allowing for the purchase of the number of shares of BioLargo common stock equal to the investment amount divided by the unit/conversion price (e.g., one warrant share for each share of common stock which the investor is eligible to receive through conversion of the note). (See Note 7.) The warrants expire on June 20, 2022. The Company may "call" the warrants, requiring the investor to exercise their warrants within 30 days or forever lose the rights to do so, only if the following conditions have been met: (i) the underlying Shares are registered with the SEC and (ii) the Company's common stock closes for 10 consecutive trading days at or above two times the exercise price.

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Through December 31, 2017, we had received \$523,700 in investments in the Summer 2017 Unit Offering, from ten accredited investors, all pursuant to Pricing Supplement No. 1. No investments were received pursuant to a second pricing supplement issued on December 11, 2017, setting the unit price at \$0.394 per share. On February 22, 2018, we issued Pricing Supplement No. 3, setting the Unit price to \$0.30 and the warrant exercise price at \$0.48. Prior to the offering's termination on March 26, 2018, we received \$80,000 in investments from two accredited investors pursuant to this third pricing supplement.

The offering documents assured the investors that in the event a subsequent pricing supplement offered a lower conversion or exercise price, prior investors would be given those favorable terms. Because we issued a third pricing supplement lowering the Unit price to \$0.30 per share, the unit price for the prior investors was lowered to \$0.30. As a result, the number of warrant shares available for purchase by each investor increased. (See Note 7.)

**Convertible Note, matures April 20, 2021 (Spring 2018 Unit Offering)**

On March 26, 2018, we commenced a private securities offering (titled the "Spring 2018 Unit Offering") which offered the sale of \$1,500,000 of "Units," each Unit consisting of a convertible promissory note and stock purchase warrant. Concurrently, we issued Pricing Supplement No. 1 setting the initial unit/conversion price at \$0.30 per share, and the initial warrant exercise price at \$0.48 per share. The promissory notes issued to investors mature April 20, 2021, and incurs interest at the rate of 12% per annum on the amount invested. Interest due will be paid quarterly in arrears in cash or shares of common stock. If paid by the issuance of common stock, interest is paid at a conversion price equal to the average closing price of the Company's common stock over the 20 trading days prior to the interest payment due date. The principal amount of the note may be paid by the issuance of shares of common stock, or cash, upon maturity at the Company's election. Promissory notes may be converted at any time by the investor, at maturity by the Company, or by the Company prior to maturity, so long as the following conditions are met: (i) the shares issued as payment are registered with the SEC; and (ii) the Company's common stock closes for ten consecutive trading days at or above three times the Unit price.

In addition to the convertible promissory note, each investor will receive a warrant allowing for the purchase of the number of shares of BioLargo common stock equal to the investment amount divided by the unit/conversion price (e.g., one warrant share for each share of common stock which the investor is eligible to receive through conversion of the note). (See Note 7.)

Through March 31, 2018, we had received one investment for \$100,000, and issued a warrant to purchase 333,333 shares. This investment was received from an entity owned/controlled by a member of our board of directors. We did not receive any investments in this offering during the three months ended June 30, 2018.

**Convertible Note, matures June 15, 2021 (OID Note)**

On June 15, 2018, we received \$75,000 and we issued a convertible promissory note (titled the “OID Note”) for 100% of the funds received, or \$82,500. The convertible promissory note is convertible into shares of the company’s common stock at a conversion price of \$0.30 per share. The original issuance discount totaled \$7,500, recorded as a discount on convertible notes on our balance sheet. The discount will be amortized and recorded to interest expense over the term of the note. The convertible promissory note matures June 15, 2021 and incurs interest at the rate of 15% per annum on the OID Note. Interest due will be paid quarterly in arrears in shares of common stock, paid at a conversion price equal to the average closing price of the Company’s common stock over the 20 trading days prior to the interest payment due date. The OID Note is convertible by the investor at any time, and convertible by the Company (i) at maturity, (ii) in the event the Company’s stock price closes at two times the conversion price for 20 consecutive days, provided that either the shares underlying the convertible note are registered with the SEC, or more than six months has elapsed since the date of the investment.

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**Note 6. Share-Based Compensation**

**Common Stock**

On May 2, 2017, pursuant to an employment agreement with the Company's president, Dennis Calvert (see Note 12), we issued Mr. Calvert 1,500,000 shares of common stock, subject to a "lock-up agreement" whereby the shares remain unvested unless and until the earlier of (i) a sale of the Company, (ii) the successful commercialization of the Company's products or technologies as demonstrated by its receipt of at least \$3,000,000 in cash, or the recognition of \$3,000,000 in revenue, over a 12-month period from the sale of products and/or the license of technology, and (iii) the Company's breach of the employment agreement resulting in his termination. The Company will expense the fair value of the stock if and when it is probable that any of the conditions above are met.

**Stock Options**

During the six months ended June 30, 2017 and 2018, we recorded an aggregate \$515,959 and \$696,001, respectively, in selling general and administrative expense related to the issuance of stock options.

**2018 Equity Incentive Plan**

On June 22, 2018, the BioLargo, Inc. 2018 Equity Incentive Plan ("2018 Plan") was adopted as a means of providing our directors, key employees and consultants additional incentive to provide services. Both stock options and stock grants may be made under this plan for a period of 10 years. It is set to expire on its terms on June 22, 2028. Our Board of Director's Compensation Committee administers this plan. As plan administrator, the Compensation Committee has sole discretion to set the price of the options. The plan authorizes the following types of awards: (i) incentive and non-qualified stock options, (ii) restricted stock awards, (iii) stock bonus awards, (iv) stock appreciation rights, (v) restricted stock units, and (vi) performance awards. The total number of shares reserved and available for awards pursuant to this Plan as of the date of adoption of this 2018 Plan by the Board is forty million shares. The



number of shares available under the 2018 Plan can increase up to 5% each year at the discretion of the board.

On June 29, 2018, we issued options to purchase 296,976 shares of our common stock at an exercise price of \$0.43 per share to members of our board of directors for services, to employees in lieu of salary, and to consultants for services, pursuant to the 2018 Plan. The fair value of these options totaled \$127,700 and is recorded as selling, general and administrative expenses.

Activity for our stock options under the 2018 Plan for the six months ended June 30, 2018 is as follows:

<b>As of June 30, 2018:</b>	<b>Options Outstanding</b>	<b>Exercise Price per share</b>	<b>Weighted Average Price per share</b>
Inception, June 22, 2018			
Granted	296,976	\$ 0.43	\$ 0.43
Expired	—	—	—
Balance, June 30, 2018	296,976	\$ 0.43	\$ 0.43

**2007 Equity Incentive Plan**

On September 7, 2007, and as amended April 29, 2011, the BioLargo, Inc. 2007 Equity Incentive Plan (“2007 Plan”) was adopted as a means of providing our directors, key employees and consultants additional incentive to provide services. Both stock options and stock grants were made under this plan for a period of 10 years. It expired on its terms on September 7, 2017. The Board’s Compensation Committee administers this plan. As plan administrator, the Compensation Committee has sole discretion to set the price of the options.

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## BIOLARGO, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## (UNAUDITED)

On June 19, 2017, the date of our annual stockholders' meeting, we recorded the issuance of options to purchase an aggregate 40,000 shares of our common stock to the non-employee members of our Board of Directors, pursuant to the terms of the 2007 Equity Plan which calls for an annual automatic issuance. The exercise price of \$0.43 equals the price of our common stock on the grant date. The fair value of these options totaled \$15,600 and was recorded as selling, general and administrative expense.

On February 10, 2017, we extended the engagement agreement with our Chief Financial Officer, retroactive to October 1, 2016. The sole consideration for the one-year extension was the issuance of an option to purchase 300,000 shares of our common stock, at an exercise price of \$0.69 per share which was equal to the closing price of our common stock on the date of grant. The option expires February 10, 2027, and vests over the term of the engagement with 125,000 shares having vested as of February 10, 2017, and the remaining shares to vest 25,000 shares monthly beginning March 1, 2017, and each month thereafter, so long as his agreement is in full force and effect. The fair value of the option totaled \$207,000. During the six months ended June 30, 2017, we recorded \$155,250 as selling, general and administrative expense on our statement of operations. The remaining fair value balance vested monthly through September 30, 2017.

Activity for our stock options under the 2007 Plan for the six months ended June 30, 2017 and 2018 is as follows:

<b>As of June 30, 2017:</b>	<b>Options Outstanding</b>	<b>Exercise Price per share</b>	<b>Weighted Average Price per share</b>
Balance, December 31, 2016	9,916,586	\$0.23-1.89	\$ 0.44
Granted	340,000	0.39 -0.69	0.65
Expired	—	—	—
Balance, June 30, 2017	10,256,586	\$0.23-1.89	\$ 0.44

**Weighted  
Average**

<b>As of June 30, 2018:</b>	<b>Options Outstanding</b>	<b>Exercise Price per share</b>	<b>Price per share</b>
Balance, December 31, 2017	9,831,586	\$0.23–1.89	\$ 0.44
Granted	—	—	—
Expired	(70,000 )	1.45 –1.89	1.79
Balance, June 30, 2018	9,761,586	\$0.23–1.65	\$ 0.43

**Options issued Outside of the 2007 Equity Incentive Plan**

During the six-months ended June 30, 2018, we issued options to purchase 1,008,268 shares of our common stock at exercise prices ranging between \$0.23 – \$0.43 per share to vendors and to members of our board of directors in exchange for unpaid obligations for their services. The fair value of the options totaled \$260,671 and is recorded as selling, general and administrative expenses.

During the six-months ended June 30, 2017, we issued options to purchase 820,879 shares of our common stock at exercise prices ranging between \$0.43 – \$0.67 per share to vendors and to members of our board of directors in exchange for unpaid obligations for their services. The fair value of the options totaled \$277,074 and is recorded as selling, general and administrative expenses.

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On May 2, 2017, pursuant to his employment agreement, we granted to Mr. Calvert, an option (the “Option”) to purchase 3,731,322 shares of the Company’s common stock. The Option shall be a non-qualified stock option, exercisable at \$0.45 per share, which represents the market price of the Company’s common stock as of the date of the agreement, exercisable for ten years from the date of grant and vesting in equal increments on the anniversary of the agreement for five years. Notwithstanding the foregoing, any portion of the Option which has not yet vested shall be immediately vested in the event of, and prior to, a change of control, as defined in the Calvert Employment Agreement. The Option contains the other terms standard in option agreements issued by the Company, including provisions for a cashless exercise. The fair value of this option totaled \$1,679,095 and will be amortized monthly through May 2, 2022. During the six months ended June 30, 2017, we recorded \$27,985 and during the six months ended June 30, 2018 we recorded \$167,910 of selling, general and administrative expense.

*Exercise of Stock Option*

On April 30, 2017, the Company’s president, Dennis Calvert, delivered a notice of exercise of 3,866,630 shares pursuant to his stock option agreement dated April 30, 2007. The exercise price was \$0.18 per share, and the Company issued 2,501,937 shares, calculated by multiplying the difference between the market price of \$0.51 and the exercise price of \$0.18 with the number of shares exercised, and dividing that amount by the market price. No cash consideration was tendered with respect to the exercise. The remaining 3,866,629 shares available for purchase under the option agreement expired unexercised.

Pursuant to a “lock-up agreement” dated April 30, 2017, Mr. Calvert agreed to restrict the sales of the shares received until the earlier of (i) the consummation of a sale (in a single transaction or in a series of related transactions) of the Company by means of a sale of (a) a majority of the then outstanding common stock (whether by merger, consolidation, sale or transfer of common stock, reorganization, recapitalization or otherwise) or (b) all or substantially all of its assets; and (ii) the successful commercialization of the Company’s products or technologies as demonstrated by its receipt of at least \$3,000,000 in cash, or the recognition of \$3,000,000 in revenue, over a 12-month period from the sale of products and/or the license of technology; and (iii) the Company’s breach of the employment agreement between the Company and Calvert dated May 2, 2017 and resulting in Calvert’s termination.

Activity of our stock options issued outside of the 2007 Equity Incentive Plan for the six months ended June 30, 2017 and 2018 is as follows:

<b>As of June 30, 2017:</b>	<b>Options Outstanding</b>	<b>Exercise Price per share</b>		<b>Weighted Average Price per share</b>
Balance, December 31, 2016	20,148,766	\$0.18–	1.00	\$ 0.43
Granted	4,552,201	0.43 –	0.67	0.47
Expired	3,866,629	0.18		0.18
Exercised	(3,866,630 )	0.18		0.18
Balance, June 30, 2017	16,967,708	\$0.18–	1.00	\$ 0.41

<b>As of June 30, 2018:</b>	<b>Options Outstanding</b>	<b>Exercise Price per share</b>		<b>Weighted Average Price per share</b>
Balance, December 31, 2017	20,018,408	\$0.25–	1.00	\$ 0.51
Granted	1,008,268	0.23 –	0.43	0.26
Expired	(2,400,000 )	0.99		0.99
Balance, June 30, 2018	18,626,676	\$0.25–	1.00	\$ 0.45

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## BIOLARGO, INC. AND SUBSIDIARIES

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For employees, we recognize compensation expense for stock option awards on a straight-line basis over the applicable service period of the award, which is the vesting period. Share-based compensation expense is based on the grant date fair value estimated using the Black-Scholes Option Pricing Model. The following methodology and assumptions were used to calculate share-based compensation for the six months ended June 30:

	<b>2017</b>		<b>2018</b>	
	<b>Non Plan</b>	<b>2007 Plan</b>	<b>Non Plan</b>	<b>2018 Plan</b>
Risk free interest rate	2.29- 2.40%	2.31- 2.40%	2.43–2.91%	2.91 %
Expected volatility	578 - 601%	578 - 601%	548 –563%	548 %
Expected dividend yield	—	—	—	—
Forfeiture rate	—	—	—	—
Expected life in years	7	7	7	7

Expected price volatility is the measure by which our stock price is expected to fluctuate during the expected term of an option. Expected volatility is derived from the historical daily change in the market price of our common stock, as we believe that historical volatility is the best indicator of future volatility.

The risk-free interest rate used in the Black-Scholes calculation is based on the prevailing U.S. Treasury yield as determined by the U.S. Federal Reserve. We have never paid any cash dividends on our common stock and do not anticipate paying cash dividends on our common stock in the foreseeable future.

Historically, we have not had significant forfeitures of unvested stock options. A significant number of our stock option grants are fully vested at issuance or have short vesting provisions. Therefore, we have estimated the forfeiture rate of our outstanding stock options as zero.

**Note 7. Warrants**

**Reduction of Warrant Exercise Price**

During the three months ended June 30, 2018, certain holders of outstanding warrants to purchase common stock received in prior unit offerings paid us cash in exchange for a reduction of the exercise price in their warrant(s). In the aggregate, we received \$148,854 from holders of 37 warrants which allow for the purchase of an aggregate 4,326,358 shares of our common stock. Exercise prices of these warrants were reduced to \$0.30. Management determined that the appropriate accounting treatment for the reduction in the exercise price of the warrants was a capital transaction rather than a contract modification treatment analogous to changes in stock option contracts. As such, the fair market value was equal to the cash received, \$148,854.

**Warrants Issued Concurrently with Spring 2018 Unit Offering**

During the three months ended March 31, 2018, pursuant to the terms of our Spring 2018 Unit Offering (see Note 5), we issued a warrant to purchase up to 333,333 shares of our common stock at an exercise price of \$0.48 per share to the investor in the Spring 2018 Offering. The warrant expires April 20, 2023. The relative fair value of the warrant resulted in \$49,306 recorded as a discount on our convertible notes on our consolidated balance sheet in the period issued.

The Company may “call” the warrants issued in the Spring 2018 Offering, requiring the holder to exercise their warrant within 30 days or forever lose the rights to do so, if the following conditions have been met: (i) the shares of common stock underlying the warrants are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

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**Warrants Issued Concurrently with Line of Credit Offering**

During the three months ended March 31, 2018, pursuant to the terms of our Line of Credit (see Note 5, “Line of Credit, matures September 1, 2019”), we issued warrants to purchase up to an aggregate 390,000 shares of our common stock at an exercise price of \$0.35 per share. These warrants expire March 1, 2023. The relative fair value of these warrants resulted in \$85,002 recorded as a discount on our “convertible notes payable and line of credit” on our consolidated balance sheet in the period issued.

The Company may “call” these warrants, requiring the holder to exercise their warrants within 30 days or forever lose the rights to do so, if the following conditions have been met: (i) the shares of common stock underlying the warrants are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

**Warrants Issued Concurrently with Note Payable**

During the three months ended March 31, 2018, pursuant to the terms of the note payable. (see Note 5, “Note payable, matures March 8, 2020”), we issued warrants to purchase up to an aggregate 150,000 shares of our common stock at an exercise price of \$0.35 per share. At the end of each month 6,250 warrants vest as long as the note payable is outstanding. Although the note matures March 8, 2020, the investor may call the note at any time after June 30, 2018. Thus, a minimum of 25,000 warrants will vest, and the fair value of these warrants totaled \$6,500. Of this amount \$1,625 was recorded as interest expense and the remaining \$4,875 is recorded as a discount on our consolidated balance sheet in the period issued. These warrants expire February 28, 2023.

**Warrants Issued to Summer 2017 Unit Offering Investors**

Pursuant to the Summer 2017 Unit Offering, we issued warrants to purchase the number of shares of stock equal to each investor’s investment amount, divided by the “unit price” set forth in a “pricing supplement”. The offering documents assured the investors that in the event a subsequent pricing supplement offered a lower conversion or exercise price,



prior investors would be given those favorable terms. On February 12, 2018, we issued a third pricing supplement, lowering the unit price to \$0.30. As a result of this reduction, the number of shares purchasable pursuant to warrants issued to prior investors increased by an aggregate 416,478 shares. Additionally, during the three months ended March 31, 2018, we accepted two final investments in the aggregate amount of \$80,000, pursuant to the third pricing supplement, and issued these investors warrants to purchase an aggregate 266,667 shares. The relative fair value of these warrants, including the increase in purchasable shares, resulted in \$103,322 recorded as a discount on our consolidated balance sheet in the period issued.

### **Warrants Issued Concurrently with One Year Convertible Notes**

We have accepted \$250,000 investments and issued one-year OID convertible notes on three occasions: July 8, 2016, December 30, 2016, and July 17, 2017. In addition to the notes, the investors received warrants on each of those three dates to purchase an aggregate 400,000 shares of our common stock. These warrants were initially exercisable at \$0.65 per share (for July 2016 warrants), \$0.70 per share (for December 2016 warrants), and \$0.65 per share (for July 2017 warrants), and expire five years from the date of grant. Each of the warrants contain a provision that the exercise price may be reduced in the event we sell our common stock or issue warrants to third parties at a lower prices, with particular exclusions, the details of which are available in our Form 10-K. The exercise price of these warrants has decreased, and the number of shares increased, on multiple occasions prior to December 31, 2017, most recently on December 11, 2017, at which time the exercise price was reduced to \$0.394 per share, and the number of shares issuable pursuant to the warrants, in the aggregate, increased from the original 1,200,000 shares, to 2,081,216.

On February 22, 2018, we sold shares of our common stock at \$0.25 per share (see Note 4). Since these securities were sold at less than the then previously adjusted \$0.394 warrant exercise price, the exercise price of the warrants were decreased from \$0.394 to \$0.25 per share, and the number of shares issuable pursuant to the warrants increased by an aggregate 1,198,784 shares. The fair value of the warrants issued totaled \$297,439 and is recorded as a deemed dividend in our equity statement for the six months ended June 30, 2018.

We have certain warrants outstanding to purchase our common stock, at various prices, as described in the following table:

	<b>Number of Shares</b>	<b>Price Range</b>
<b>As of June 30, 2017</b>		
Outstanding as of December 31, 2016	20,035,114	\$0.125– 1.00
Issued	990,727	\$0.42 – 0.70
Exercised	(510,000 )	\$0.30
Outstanding as of June 30, 2017	20,515,841	\$0.125– 1.00

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## BIOLARGO, INC. AND SUBSIDIARIES

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**As of June 30, 2018**

Outstanding as of December 31, 2017	22,104,817	\$0.125–	1.00
Issued	2,611,513	\$0.25 –	0.48
Exercised	—	—	
Expired	(2,683,400)		\$0.40
Outstanding as of June 30, 2018	22,032,930	\$0.125–	1.00

The fair value of each award grant is estimated on the date of grant using the Black-Scholes option-pricing model. The determination of expense of warrants issued for services or settlement also uses the option-pricing model. The principal assumptions we used in applying this model were as follows for the six months ended June 30:

	<b>2017</b>	<b>2018</b>
Risk free interest rate	1.83–1.93%	2.54%
Expected volatility	293 –297%	252%
Expected dividend yield	—	—
Forfeiture rate	—	—
Expected life in years	5	5- 10

The risk-free interest rate is based on U.S. Treasury yields in effect at the time of grant. Expected volatilities are based on historical volatility of our common stock.

**Note 8. Accounts Payable and Accrued Expenses**

Accounts payable and accrued expenses included the following:

<b>December</b>	<b>June</b>
<b>31, 2017</b>	<b>30, 2018</b>

Accounts payable and accrued expenses	\$ 88,381	\$ 149,338
Accrued interest	50,748	72,926
Accrued payroll	84,976	32,393
Total accounts payable and accrued expenses	\$ 224,105	\$ 254,657

**Issuance of Common Stock in exchange for payment of payables**

***Payment of Officer Salaries***

On March 31, 2018, we issued 323,030 shares of our common stock at \$0.26 per share in lieu of \$83,665 of accrued and unpaid obligations to two of our officers. The price-per-share was based on the closing price of our common stock on the last day of the month.

On June 29, 2018, we issued 176,947 shares of our common stock at \$0.43 per share in lieu of \$75,968 of accrued and unpaid obligations to two of our officers. The price-per-share was based on the closing price of our common stock on the last day of the month.

***Payment of Consultant Fees***

During the six months ended June 30, 2018, we issued 948,280 shares of our common stock, at prices ranging between \$0.23 - \$0.41 per share, in lieu of \$246,966 of accrued and unpaid obligations to consultants.

During the six months ended June 30, 2017, we issued 307,829 shares of our common stock, at prices ranging between \$0.43 - \$0.52, in lieu of \$493,827 of accrued and unpaid obligations to consultants.

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***Payment of Accrued Interest***

During the six months ended June 30, 2018, we issued 1,919,806 shares of our common stock, at prices ranging between \$0.31 – 0.42 per share, in lieu of accrued interest totaling \$493,783.

During the six months ended June 30, 2017, we issued 683,875 shares of our common stock, at prices ranging between, \$0.41 – \$0.70 per share, in lieu of accrued interest totaling \$337,246.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

**Note 9. Noncontrolling Interest**

**Clyra Medical Technologies**

Our subsidiary Clyra Medical Technologies, Inc. (“Clyra”) was formed to develop and sell medical products containing our technology,. Although we initially owned 100% of this subsidiary, we have issued shares to management and to investors. As of June 30, 2018, we own 46.3% of Clyra’s outstanding shares. Clyra’s three-member board of directors includes BioLargo president Dennis P. Calvert, BioLargo board member (and also an owner of Clyra’s Series A preferred shares) Jack B. Strommen, and Clyra’s president.

Clyra’s Series A preferred shares (“Preferred Shares”) accrue an annual dividend of 8% for a period of five years. Although the dividends began to accrue immediately, Clyra has no obligation to declare a dividend until a product of the company has received a premarket approval by the United States Federal Drug Administration (“FDA”), or for

which a premarket notification pursuant to form 510(k) has been submitted and for which the FDA has given written clearance to market the product in the United States (either, "FDA Approval"). After FDA Approval, annually on December 20, and unless prohibited by California law governing distributions to shareholders, Clyra is required to declare and pay any accruing dividends to holders of Preferred Shares then accrued but unpaid. As the declaration and payment of such dividends is contingent on an uncertain future event, no liability has been recorded for the dividends. The accumulated and undeclared dividend balance as of June 30, 2018 is \$150,000.

Holders of Preferred Shares are entitled to preferential payments in the event of a liquidation, dissolution or winding up of the company, in an amount equal to any accrued and unpaid dividends. After such preference, any remaining assets are distributed pro-rata between holders of Clyra common stock and Preferred Shares as if the Preferred Shares had converted to Clyra common stock. Holders of Preferred Shares may convert the shares to Clyra common stock initially on a one-to-one basis. The conversion formula is subject to change in the event Clyra sells stock at a lower price than the price paid by Sanatio.

On March 31, 2017, Clyra obtained a \$250,000 line of credit from Sanatio Capital LLC, accruing interest at a rate of 10% per annum and a 5% original issue discount. The line of credit was scheduled to mature on March 31, 2019, but was subsequently converted to Clyra stock in full payment (see below).

In April 2017, BioLargo purchased 500 shares of Clyra common stock from a former member of Clyra's management for \$40,000.

In August 2017, Clyra commenced a private offering of its common shares at a price of \$160 per share, and accepted \$1,000,000 in subscriptions. It issued 6,250 shares of its common stock to two investors. Of that amount, BioLargo invested \$250,000 and was issued 1,562.5 shares. On August 4, 2017, Clyra issued 1,690 shares of its common stock at \$160 per share to Sanatio in exchange for payment of the \$270,400 principal and interest outstanding under the line of credit held by Sanatio (see above). Subsequent to the issuance of shares to investors in the offering, and to Sanatio for the conversion of the line of credit, BioLargo owned 15,297.5 shares of Clyra common stock, which is 46.3% of the outstanding stock at Clyra. Two members of BioLargo's board of directors (Dennis P. Calvert and Jack B. Strommen) comprise a majority of the three-member Clyra board of directors. Management has determined that BioLargo does control Clyra after reviewing the guidance of ASC Topic 810, "Consolidation". While BioLargo does not have voting interest control through 50% ownership of Clyra, it does exercise control under the Variable Interest Model. BioLargo is the primary beneficiary since it has the power to direct Clyra's activities that most significantly impact Clyra's performance and it has the obligation to absorb losses or receive benefits (through royalties and licensing) that could be potentially significant to Clyra. BioLargo has consolidated Clyra's operations through June 30, 2018.

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**Note 10. Biolargo Engineering, Science and Technologies, LLC**

In September 2017, we commenced a full-service environmental engineering firm and formed a Tennessee entity named BioLargo Engineering, Science & Technologies, LLC (“BLEST”). In conjunction with the start of this subsidiary, we entered into a three-year office lease in the Knoxville, Tennessee area, and entered into employment agreements with seven scientists and engineers. These agreements and related operational obligations add approximately \$100,000 to our monthly budget for payroll, taxes, benefits, insurance, and other related obligations. The company was capitalized with two classes of membership units: Class A, 100% owned by Biolargo, and Class B, held by management of BLEST, and which initially have no “profit interest,” as that term is defined in Tennessee law. However, over the succeeding five years, the Class B members can earn up to a 30% profit interest. They also have been granted options to purchase up to an aggregate 2,000,000 shares of BioLargo, Inc. common stock. The profit interest and option shares are subject to a five year vesting schedule tied to the performance of the subsidiary, including gross revenue targets that increase over time, obtaining positive cash flow by March 31, 2018 (which was not met), collecting 90% of its account receivables, obtaining a profit of 10% in its first year (and increasing in subsequent years), making progress in the scale-up and commercialization of our AOS system, and using BioLargo research scientists (such as our Canadian team) for billable work on client projects. These criteria are to be evaluated annually by a committee of the company (which includes BioLargo’s president, CFO, and BLEST’s president), beginning September 2018. The details of these transactions were reported on a Form 8-K filed with the SEC on September 8, 2017. Given the significant performance criteria, the Class B units and the stock options will only be recognized in compensation expense if or when the criteria are satisfied. It is still too early to make a determination as to whether BLEST will meet some of the performance criteria. Through June 30, 2018 and as of the end of 2017, BLEST has not met any of the criteria and therefore no portion of the Class B Units and stock options have been earned or vested.

**Note 11. Commitments and Contingencies**

**Calvert Employment Agreement**

On May 2, 2017, the Company entered into an employment agreement with its President and Chief Executive Officer Dennis P. Calvert (the “Calvert Employment Agreement”), replacing in its entirety the previous employment agreement

with Mr. Calvert dated April 30, 2007.

The Calvert Employment Agreement provides that Mr. Calvert will continue to serve as our President and Chief Executive Officer and receive base compensation equal to his current rate of pay of \$288,603 annually. In addition to this base compensation, the agreement provides that he is eligible to participate in incentive plans, stock option plans, and similar arrangements as determined by the Company's Board of Directors, health insurance premium payments for himself and his immediate family, a car allowance of \$800 per month, paid vacation of four weeks per year, and bonuses in such amount as the Compensation Committee may determine from time to time.

The Calvert Employment Agreement provides that Mr. Calvert will be granted an option (the "Option") to purchase 3,731,322 shares of the Company's common stock. The Option shall be a non-qualified stock option, exercisable at \$0.45 per share, which represents the market price of the Company's common stock as of the date of the agreement, exercisable for ten years from the date of grant and vesting in equal increments over five years. Notwithstanding the foregoing, any portion of the Option which has not yet vested shall be immediately vested in the event of, and prior to, a change of control, as defined in the Calvert Employment Agreement. The agreement also provides for a grant of 1,500,000 shares of common stock, subject to the execution of a "lock-up agreement" whereby the shares remain unvested unless and until the earlier of (i) a sale of the Company, (ii) the successful commercialization of the Company's products or technologies as demonstrated by its receipt of at least \$3,000,000 in cash, or the recognition of \$3,000,000 in revenue, over a 12-month period from the sale of products and/or the license of technology, and (iii) the Company's breach of the employment agreement resulting in his termination. The Option contains the other terms standard in option agreements issued by the Company, including provisions for a cashless exercise.

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The Calvert Employment Agreement has a term of five years, unless earlier terminated in accordance with its terms. The Calvert Employment Agreement provides that Mr. Calvert's employment may be terminated by the Company due to his death or disability, for cause, or upon a merger, acquisition, bankruptcy or dissolution of the Company. "Disability" as used in the Calvert Employment Agreement means physical or mental incapacity or illness rendering Mr. Calvert unable to perform his duties on a long-term basis (i) as evidenced by his failure or inability to perform his duties for a total of 120 days in any 360-day period, or (ii) as determined by an independent and licensed physician whom Company selects, or (iii) as determined without recourse by the Company's disability insurance carrier. "Cause" means that Mr. Calvert has (i) engaged in willful misconduct in connection with the Company's business; or (ii) been convicted of, or pled guilty or nolo contendere in connection with, fraud or any crime that constitutes a felony or that involves moral turpitude or theft. If Mr. Calvert's employment is terminated due to merger or acquisition, then he will be eligible to receive the greater of (i) one year's compensation plus an additional one-half year for each year of service since the effective date of the employment agreement or (ii) one year's compensation plus an additional one-half year for each year remaining in the term of the agreement. Otherwise, he is only entitled to receive compensation due through the date of termination.

The Calvert Employment Agreement requires Mr. Calvert to keep certain information confidential, not to solicit customers or employees of the Company or interfere with any business relationship of the Company, and to assign all inventions made or created during the term of the Calvert Employment Agreement as "work made for hire".

**Clyra Consulting Agreement**

Our partially owned subsidiary Clyra (see Note 9) entered into a consulting agreement with Beach House Consulting, LLC, through which Jack B. Strommen will be providing consulting services to Clyra related to its sales and marketing activities once it has received FDA Approval (as defined in Note 9 and the associated agreement) on a product, at which point the agreement provides that Mr. Strommen is to receive \$23,438 per month for a period of four years. This agreement has not started, and the total cash obligation related to the agreement would be \$1,125,024 over four years.

**Note 12. Subsequent Events.**



Management has evaluated subsequent events through the date of the filing of this Quarterly Report and management noted the following for disclosure.

**Conversion of Debt Obligations**

***One-year convertible notes, mature July 18, 2018***

On July 2, 2018, the holders of two one-year notes in the aggregate principal amount of \$280,000, which were due to mature on July 18, 2018, tendered an offer to the Company to convert 100% of the balance due on the outstanding notes into shares of our common stock in lieu of receiving cash. We accepted the offer and agreed to convert the principal balance of \$280,000 and \$8,400 outstanding interest into an aggregate 1,153,600 shares of our common stock, at \$0.25 per share. The notes were issued July 18, 2017, and originally provided for a conversion price of \$0.42 per share.

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## BIOLARGO, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

*Nine-month convertible note, matures October 16, 2018*

On July 16, 2018, the holder of a nine-month note with an original principal amount of \$150,000 maturing October 16, 2018 submitted a notice to convert the remaining principal due on the note of \$54,239. We issued an aggregate 217,960 shares at \$0.25 per share, consisting of 216,950 shares for payment of principal, and 1,010 for payment of accrued interest. As of the date of this Report, this note is paid in full.

Subsequent to these conversions our outstanding debt obligations are as follows:

	<b>June 30,</b>	<b>August 14,</b>
	<b>2018</b>	<b>2018</b>
<b>Current liabilities</b>		
Convertible notes payable		
One-year convertible notes, mature July 18, 2018 *	\$280,000	\$—
Convertible notes, mature June 1, 2018	—	—
Nine-month convertible note, matures September 18, 2018	447,975	447,975
Nine-month convertible note, matures October 16, 2018 *	54,239	—
Total convertible notes payable	\$782,214	\$447,975
<b>Long-term liabilities:</b>		
Line of credit, matures September 1, 2019	\$390,000	\$390,000
Convertible notes payable		
Convertible note, matures July 20, 2019	440,000	440,000
Convertible notes, mature December 31, 2019	75,000	75,000
Note payable, matures March 8, 2023 (or on demand 60 days' notice)	50,000	50,000
Convertible notes, mature June 20, 2020	125,000	125,000
Convertible notes, mature April 20, 2021	100,000	100,000
Convertible notes, mature June 15, 2021	82,500	82,500
Total convertible notes payable	\$872,500	\$872,500
Total	\$2,044,714	\$1,710,475



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

This quarterly report on Form 10-Q contains forward-looking statements. These forward-looking statements involve risks and uncertainties, including statements regarding BioLargo’s capital needs, business plans and expectations. Such forward-looking statements involve risks and uncertainties regarding BioLargo’s ability to carry out its planned development and production of products. Forward-looking statements are made, without limitation, in relation to BioLargo’s operating plans, BioLargo’s liquidity and financial condition, availability of funds, operating and exploration costs and the market in which BioLargo competes. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as “may”, “will”, “should”, “expect”, “plan”, “intend”, “anticipate”, “believe”, “estimate”, “predict”, “potential” or “continue”, the negative of such terms or other comparable terminology. Actual events or results may differ materially. In evaluating these statements, you should consider various factors, including the risks outlined in our Form most recent annual report on Form 10-K, and, from time to time, in other reports BioLargo files with the SEC. These factors may cause BioLargo’s actual results to differ materially from any forward-looking statement. BioLargo disclaims any obligation to publicly update these statements, or disclose any difference between its actual results and those reflected in these statements. The information constitutes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Given these uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

Unless otherwise expressly stated herein, all statements, including forward-looking statements, set forth in this Form 10-Q are as of June 30, 2018, unless expressly stated otherwise, and we undertake no duty to update this information.

As used in this report, “we” and “Company” refers to (i) BioLargo, Inc., a Delaware corporation; (ii) its wholly-owned subsidiaries BioLargo Life Technologies, Inc., a California corporation, Odor-No-More, Inc., a California corporation, BioLargo Water USA, Inc., a California corporation, BioLargo Development Corp., a California corporation, BioLargo Maritime Solutions, Inc., a California corporation, BioLargo Engineering, Science & Technologies, LLC, a Tennessee limited liability company, and Canadian subsidiary BioLargo Water, Inc.; and (iii) Clyra Medical Technologies, Inc. (“Clyra”), a partially owned subsidiary.

The following discussion and analysis should be read in conjunction with our unaudited consolidated financial statements and the related notes to the consolidated financial statements included elsewhere in this report.

**Our Business- A Sustainable Technology Incubator**

BioLargo, Inc. is an innovation company driven by our mission is to “make life better” by developing breakthrough platform technologies, nurturing and building businesses around the intellectual property, while providing capital and support along the journey from “cradle” to “maturity”. Our business strategy is straightforward: we invent or acquire technologies that we believe have the potential to be disruptive in large commercial markets; we incubate these technologies to advance and promote their commercial success as we leverage our considerable scientific, engineering, and entrepreneurial talent; we then monetize these technical assets through a variety of business structures that may include licensure, joint venture, sale, spin off, or by deploying direct to market strategies. We seek to unlock the value of our portfolio of underlying technologies to both advance our purposeful mission while we create value for our stockholders.

Our first significant commercial success is currently unfolding for our CupriDyne Clean odor and volatile organic compound (“VOC”) control products, sold through our subsidiary, Odor No More, Inc. Sales are increasing as we focus on serving the solid waste handling and wastewater treatment industries. We are gearing up for rapid growth as the product is experiencing more widespread market adoption.

Our second commercial operation provides professional engineering services, through our subsidiary BioLargo Engineering, Science & Technologies, LLC (“BLEST”). Through BLEST, we provide a menu of professional engineering and consulting services to compliment and nurture our technologies as well as serve clients on a fee-for-service basis.

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In addition to our two operating subsidiaries, we have technologies and products in the development pipeline progressing towards commercialization, including our Advanced Oxidation System (“AOS”), that we target to have commercially ready in 2019, and our medical products, which will be ready for commercialization as soon as we pass Food and Drug Administration (“FDA”) clearance.

We believe our current success with our industrial odor and VOC control products serves to validate our overall business strategy which is focused on technology-based products and services capable of disrupting the status quo in their applicable industry market segment. We believe that the future of our medical and clean water technologies has similar and also very large market opportunities ahead as they are introduced commercially.

**Industrial Odor and VOC Control – CupriDyne Clean**

Our CupriDyne Clean industrial products reduce and eliminate tough odors and VOC’s in various industrial settings, delivered through misting systems, sprayers, water trucks and similar water delivery systems. We believe the product is the number one performing odor-control product in the market, and we offer substantial savings to our customers when they use our product and services.

**Market Opportunity Validated**

Revenues from sales of our CupriDyne Clean products continue to expand. We are now selling product to four of the largest solid waste handling companies in the country, and also have secured multiple flagship clients in the wastewater treatment industry.

Many of our customers have adopted CupriDyne Clean as a replacement for a non-performing competitive product. We are realizing systematic adoption by our very large corporate customers. Our experience has helped refine our value proposition and assemble a comprehensive menu of products and services. Our success in this market has validated the market opportunity for our products and services and encourages us to continue investing in infrastructure and sales and marketing to increase revenues in these very large markets. We estimate there are approximately 2,000 active landfills<sup>1</sup> and 8,000 transfer stations<sup>2</sup> in the United States and 15,000 waste water treatment agencies<sup>3</sup>. While all may not have ongoing odor problems or neighbor complaints, many of the facilities have needed for a disruptive odor solution like CupriDyne Clean.

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<sup>1</sup> “Municipal Solid Waste Landfills - Economic Impact Analysis for the Proposed New Subpart to the New Source Performance Standards” (2014), by U.S. Environmental Protection Agency Office of Air and Radiation and Office of

Air Quality Planning and Standards.

<sup>2</sup> The top 5 Waste Management companies in the US, as of 2011, operated 624 transfer stations, and 565 landfills. “Municipal Solid Waste Landfills - Economic Impact Analysis for the Proposed New Subpart to the New Source Performance Standards” (2014), by U.S. Environmental Protection Agency Office of Air and Radiation and Office of Air Quality Planning and Standards. This is a ratio of 1:4 (landfill to transfer stations). The estimated number of transfer stations is this ratio multiplied by the approximate 1,900 total landfills, and rounded.

<sup>3</sup> <sup>1</sup>“Failure to Act, The Economic Impact of Current Investment Trends in Water and Wastewater Treatment Infrastructure” (2011), by American Society of Civil Engineers and Economic Development Research Group.

Figure includes treatment facilities owned and operated by municipalities, as well as those owned and/or operated by private entities contracting with municipalities.

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***Turn-key Full-service Solutions***

At the request of our clients, we have begun offering a menu of services to landfills, transfer stations, and wastewater treatment facilities. These services include ongoing maintenance and on-site support services to assist our clients in the design and continued use of the various systems that deliver our product in the field (such as misting systems at landfills, transfer stations, and wastewater treatment facilities). We have recently begun providing engineering design, construction and installation services related to the various water-based delivery systems used to deploy our products. Our engineering team at BLEST has been instrumental in supporting these operations. We have applied for licensure from the California Contractors State License Board (“CSLB”). We currently have more than 30 “design build” bids out to clients for CupriDyne Clean delivery systems.

We have recently hired two employees that hold licenses from the California Contractors State License Board (“CSLB”) and are in the process of transferring these licenses to our Odor-No-More subsidiary. Upon completion we will hold a General Contractors license, a Plumbing Contractors license and a Low Voltage Electrical Contractors license. We plan to test for and secure a High Voltage Electrical Contractors license in the near term. These licenses will allow us to offer a full-service solution to our current and future customers within the state of California.

***Regional Adoption***

Sales of our CupriDyne Clean products and related services were initially made at the local level. We would demonstrate our product to the manager of operations at a particular transfer station or landfill, and he or she would ultimately decide whether to use our products. If owned by a national company, in some instances we have been required to obtain official “vendor” status with the company and sign a “national purchasing agreement”. Doing so required a tremendous amount of effort and time. Some of these accounts are now introducing us to their regional managers who have the ability to direct the facilities in their region to use our product. In the second quarter of 2018, we received direction from one such regional manager to begin servicing all the locations within his region. We are in advanced discussions with six additional area managers for the same client and anticipate we will begin servicing these additional regions prior to the end of the year.

We believe that “regional adoption” is a scalable approach for the larger solid waste handling companies that, with sufficient resources, we can implement nationwide. Based on our experience that trend will continue and we need to invest in more personnel to meet these expanding and very large market opportunities.

***Wastewater Treatment Facilities***



We have begun selling products and services to wastewater treatment facilities in our local markets. Our clients are prominent municipal agencies and have indicated a desire to expand the use of our products and services to additional locations in their service areas. As a result of our success in the field, a client featured our product as an example of 'Best Practices' for the waste water treatment industry at a national water quality conference hosted by the Water Environment Federation. We anticipate overall longer selling cycles given the technical sophistication of the customers in this market, and believe significant capital and high levels of service will be required for our ultimate success. We are highly encouraged and are evaluating various strategies to maximize our marketing and selling proposition into this mature and well-established market.

***Infrastructure and Capital Needs for Odor-No-More***

We recognize the scope of the opportunity for CupriDyne Clean and related services, and understand the task of building the personnel and infrastructure to become a disruptive company in the solid waste industry. In the United States, we currently operate out of two locations – Southern California, and Tennessee. We expect to expand our manufacturing and staffing in our Tennessee operation as we achieve critical mass in that region. In the meantime, as a result of the rapid adoption we are experiencing in our local Southern California market, we are focused on adding staff and infrastructure to meet the obvious need for our products and services. Since January 1, 2018, we have added five people in both sales and support roles.

We believe that a significant number of personnel will be required to fully service the solid waste handling and wastewater treatment industries. We plan to expand as adequate capital to fund these needs becomes available.

**Full Service Environmental Engineering**

In September 2017 we formed a subsidiary for the purpose of offering full service environmental engineering to third parties, and to provide engineering support services to our internal teams to accelerate the commercialization of our AOS technologies. Its website is found at [www.BioLargoEngineering.com](http://www.BioLargoEngineering.com).

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The subsidiary, BioLargo Engineering, Science & Technologies, LLC (“BLEST”), opened its office in Oak Ridge (a suburb of Knoxville Tennessee), and entered into employment agreements with seven scientists and engineers who collectively have over two hundred years of experience in diverse engineering fields. The team is led by Randall Moore, who served as Manager of Operations for Consulting and Engineering for the Knoxville office of CB&I Environmental & Infrastructure and was formerly a leader at The Shaw Group, Inc., a Fortune 500 global engineering firm. The other team members are also former employees of CB&I and Shaw. The team is highly experienced across multiple industries and they are considered experts in their respective fields, including chemical engineering, wastewater treatment (including design, operations, data gathering and data evaluation), process safety, energy efficiency, air pollution, design and control, technology evaluation, technology integration, air quality management & testing, engineering management, permitting, industrial hygiene, applied research and development, air testing, environmental permitting, HAZOP review, chemical processing, thermal design, computational fluid dynamics, mechanical engineering, mechanical design, NEPDES permitting, RCRA/TSCA compliance and permitting, project management, storm water design & permitting, marine engineering, AutoCAD, bench chemistry, continuous emission monitoring system operator, data handling and evaluation and decommissioning and decontamination of radiological and chemical contaminated facilities.

Our engineering team has focused its efforts in two areas. First, servicing third party clients in similar roles as to what they did at CB&I and Shaw, and throughout their well-established careers. Second, they are working to scale-up, engineer and commercialize our AOS water treatment technologies, as well as support other technology and product development efforts within the BioLargo family of companies, including our industrial odor control solutions (CupriDyne Clean). By way of example, the team has recently engineered and designed a portable misting system requested by a large waste handling company. BLEST will also pursue new inventions and be available to provide engineering support where needed for any commercial opportunities that are presented by and through any and all operating units of BioLargo.

### ***Business Development at BLEST***

The selling cycle for BLEST to new outside clients can be anywhere from a few months up to nine months or longer. The nature of their work with outside clients is highly constrained by relationships, reputation, budgeting, bidding and client timing. In light of the long selling cycle that is prevalent in this industry, we are highly encouraged by the most recent developments that have taken months to mature and now appear to be well in process to begin generating financial results. A few noteworthy examples are:

During the first quarter of 2018, BLEST secured a new relationship and was retained to serve as “Owner’s Engineer” for a proposed \$687 million integrated biofuels production project to be built on the east coast. The proposed facility would convert hundreds of tons per day of municipal solid wastes and plastics into high-grade fuels and paraffin waxes, while diverting hundreds of thousands of tons of waste from landfills per year. Our team’s initial role in this project is to provide the project’s ownership team with consulting engineering support as the project becomes finalized. BLEST is now under contract to be paid for approximately \$195,000 of engineering services rendered for the pre-project phase. We expect our role to expand once the client acquires a final piece of real property necessary for the

project and additional funding. Assuming it moves ahead, we anticipate that the scope of our services will significantly expand to an important multi-year role in the project's overall engineering management. We believe this project will require rapid and detailed response and require that we increase of our Oak Ridge staff to fully meet the demands of the project.

BLEST has recently secured a time and materials contract to perform a compliance review of a leading natural gas utility in Tennessee's operating, maintenance, and emergency response activities, and to ensure the overall integrity of the facilities review relating to new rules established by the U.S. Department of Transportation Pipeline and Hazardous Materials Safety Administration (PMMSA) regulation pertaining to the use of natural underground storage of natural gas. The BLEST effort will involve preparing a program implementation plan, conducting a risk assessment, and preparing operational and maintenance procedures to prevent and mitigate facility natural gas leaks and failures caused by corrosion, chemical damage, mechanical damage, or other material deficiencies in piping, tubing, casing, valves, and associated facilities. The work is estimated not to exceed \$35,000.

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BLEST has recently been notified that as a result of its recent audit work on to assist a leading healthcare products company in transitioning to the 2015 revision of the ISO 14001 standard for environmental management systems (EMS) it is being awarded another small project from the client. The new time and materials project involves preparing a detailed GAP analysis, and subsequently updating the client's EMS procedures to reflect the significant changes to the new EMS standard which places new emphasis on upper management involvement, the life cycle of products and services, emergency preparedness and response, and sustainability. There is also a new focus on evaluating risks and opportunities and integrating this assessment into the EMS program.

BLEST recently began a time and materials contract of work estimated not to exceed \$100,000 to plan and test to demonstrate that emissions from an energetic materials incinerator at a large U.S. military installation on the East coast are meeting EPA regulatory standards. An "energetic materials incinerator" allows the military to safely dispose propellants, explosives, and munitions that have aged beyond their shelf life. This facility must meet numerous emission standards including regulations that limit emissions of chemical compounds called "dioxins" and "furans", which are tightly regulated chemicals in nearly every developed country.

BLEST has recently been notified that it is to receive a time and materials contract to provide regulatory analysis of the ongoing plant expansion for a chemical company based in the port areas west of Houston, Texas.

BLEST has expanded its services offering as a direct result of a recently acquired new equipment called a custom-fabricated Rotary Thermal Apparatus ("RTA") which expands the capabilities of the company to outside clients and creates host of new business opportunities. The RTA has proven indispensable in providing data directly applicable to the design of thermal treatment systems (i.e. incinerators, thermal desorbers, catalytic oxidation units, etc.). The RTA can also prove useful in the development of various chemical production processes and optimization of process reactions. And last but not least, the RTA can be used by BLEST to conduct treatability studies (more on that below) on contaminated solids (i.e. soils, sludges, slurries) for its clients, providing design data to engineers to develop procedures, predict outcomes and control costs for remediation projects (including soil remediation). The RTA opens up an area of practice for BLEST that includes an entire subset of remediation technologies, including thermal oxidation, thermal desorption, thermal vitrification and thermally enhanced chemical fixation. We expect the acquisition of this equipment to result in new contracts that we otherwise would not be able to execute effectively.

**BioLargo Water and the Advanced Oxidation System - AOS**

BioLargo Water is our wholly owned subsidiary located on campus at the University of Alberta that has been primarily engaged in the research and development of our Advanced Oxidation System (AOS). The AOS is a water treatment device in development that generates a series of highly oxidative species of iodine and other molecules that, because of the proprietary configuration and inner constituents of the AOS, allow the AOS to eliminate pathogenic organisms and organic contaminants with extreme efficacy while consuming very little electricity.

The key value proposition of the AOS is its ability to eliminate a wide variety of contaminants with high performance while consuming extremely low levels of input electricity – a trait made possible by the complex set of highly oxidative iodine compounds generated within the AOS reactor. Our proof-of-concept studies and case studies have generated results that project the AOS will be more cost- and energy-efficient than commonly used advanced water treatment technologies such as UV, electro- chlorination, and ozonation. This value proposition sets the AOS technology above other water treatment options, as we believe the AOS may allow safe and reliable water treatment for significantly lower cost compared to its competitors and may even enable advanced water treatment in applications where it otherwise would have been prohibitively costly.

The AOS has the potential to allow reliable and cost-effective water treatment in numerous industries and applications where high-level disinfection or elimination of hard-to-treat organic contaminants is required. We are first targeting commercialization of the AOS in three key industries: 1) livestock processing wastewater treatment and reuse; 2) municipal wastewater tertiary treatment; 3) oil and gas process affected water treatment, remediation, and/or reuse. These industries were chosen as a result of extensive market research which highlighted them as areas where current water treatment technologies fall short of industry needs, and/or where the AOS has the potential to provide economic advantages over incumbent water treatment technologies.

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Our AOS was the result of breakthroughs in both advanced iodine electrochemistry and advances in materials engineering, and its invention led to BioLargo's co-founding of a multi-year industrial research chair whose goal was to solve the contaminated water issues associated with the Canadian Oil Sands at the University of Alberta Department of Engineering in conjunction with the top five oil companies in Canada, the regional water district, and various environmental agencies of the Canadian government. Based on recovering oil prices and our ongoing work in Canada, we recently reinitiated discussions with a number of stakeholders in the oil sands industry to support the completion of AOS development for oil and gas water treatment and to discuss the initiation of pre-commercial and commercial pilots for our AOS to help treat and remediate oil sands process-affected water ("OSPW") found in tailings ponds in the Canadian oil sands, an application that currently has no good economically viable solution. We have recently applied for significant grant funding to re-initiate our work to help treat OSPW and other oil and gas wastewaters using the AOS, and we will be notified about the status of our funding application in the coming months.

Our work is continually progressing to support a number of commercial applications, with a key focus on wastewater treatment, food processing, agriculture, and oil and gas. We are also at the early stages of evaluating opportunities in in the storm drain recapture/recycling, and drinking water. Our AOS is an award-winning invention that is supported by science and engineering financial support and grants from various federal and provincial funding agencies in Canada such as NSERC, NRC- IRAP, and Alberta Innovates and in the USA by the Metropolitan Water District and National Water Research Institute.

### *Recent AOS Milestones*

The most important advances in AOS development in recent months have been 1) the planning and design of two confirmed pre-commercial field pilot projects, and 2) design and engineering advances and changes to the AOS in preparation for piloting and scale-up for industrial flow-rates and conditions. Two pre-commercial pilots have been confirmed and are planned to take place in Fall of 2018. The first is a pre-commercial pilot to treat poultry wastewater on-site at a poultry producer's facility in Alberta, where the AOS will be assessed for its ability to eliminate bacteria and other contaminants from the wastewater effectively and cost-efficiently and to establish operating costs (OPEX) and capital costs (CAPEX) in a field setting. The pilot is intended to demonstrate the AOS' ability to disinfect and decontaminate water at high flow-rates, allowing for recycling, reuse, and/or safe water discharge. Moreover, continuous treatment and recycling of the processed water in this pilot project will allow for a comprehensive assessment of the long-term economic advantage (both operating and capital costs) and conservation benefits of the AOS for both energy and water, in comparison with conventional wastewater treatment technologies. Ultimately, we expect the results of this pilot to lay an important foundation for the technical and business case that convinces future customers to purchase the AOS. The second is a pre-commercial pilot where the AOS will be used on-site at a Californian brewery as a polishing step treatment regimen to eliminate bacteria and enable wastewater discharge in compliance with Californian regulatory standards. Again, this pilot will help establish not only the efficacy of the AOS in a field setting, but also the OPEX and CAPEX of the system which will be used in preparation of future pilots, trials, and sales of the AOS. These pilot projects represent an important step for our AOS technology, as well as for our company. We are confident in our disruptive water treatment technology and have proven its treatment capabilities in the lab ad nauseum. However, pilot projects for the AOS, as with any technology, are crucial to prove its reliability to industry stakeholders as well the capital cost and operating costs of our technology at-scale. These data will be critical to pave the way for future market adoption. As a reminder, we have many other pilots in

evaluation to support this same cause.

Several advances and improvements to the AOS have also been made in recent months with the purpose of preparing the technology for pre-commercial piloting, commercial piloting, and subsequent mass production, as well as to prepare it for scale-up to allow industrial flow rates. These advancements have largely been proprietary physical improvements to the AOS, including the transitioning of the AOS to using inner substrates more amenable to mass-production and greater flow rates and pressures. Management believes it will continue to advance the scale-up to higher volume throughputs of water flow and enhances the AOS ability to be more compact and longer lasting in the field. This work is not complete, but management believes it does represent a significant step forward to achieving high throughput quality results. Importantly, we have also designed and begun assembling our own proprietary water treatment train that will be used in pilots for the AOS and that will pave the way for complete wastewater treatment in industrial settings.

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To support the planned pilots for the AOS, BioLargo Water has secured public funding from the Government of Canada, including a CA\$235,000 grant from the Industrial Research Assistance Program (NRC-IRAP) to fund our first on-site pilot project in the Canadian poultry industry. We have also submitted and are currently submitting applications for a series of substantial government grants (totaling more than \$4M USD) to fund all our development and piloting efforts in wastewater, food processing and oil and gas applications.

Our engineering team in Tennessee is actively preparing a process engineering package for the AOS system. Major components of the package will include: design basis, process flow diagrams, piping and instrumentation diagrams, process control strategy document and materials of construction specifications. This work is underway.

**Advanced Wound Care - Clyra Medical**

We formed Clyra Medical Technologies, Inc. (“Clyra”) to commercialize our technology in the medical products industry, which we believe can be disruptive to many competing product lines. Our initial product designs focus in the “advanced wound care” field, which includes traumatic injury, diabetic ulcers, and chronic hard-to-heal wounds. We are presently seeking approval for an advanced wound care product and have recently filed an application with the U.S. Food & Drug Administration (“FDA”) premarket notification of a medical device under Section 510(k) of the Food, Drug, and Cosmetic Act.

Our advanced wound care products combine broad-spectrum antimicrobial capabilities with iodine’s natural and well-understood metabolic pathway to promote healing. Our products are highly differentiated from existing antimicrobials in multiple ways - by the gentle nature in which they can perform, reduced product costs, extended antimicrobial activity, and biofilm efficacy. In addition, iodine has no known acquired microbial resistance, unlike many competing products. We believe the future markets for some of our product designs may also include infection control and wound therapy for chronic wounds. We also intend to pursue and study the use of our technology as a compliment to regenerative tissue therapy.

We have three patent applications pending for medical products, and are preparing additional applications. While these patent applications are pending, we intend to continue expanding patent coverage as we refine our medical products.

In late 2017, Clyra completed product development on its first design with its advanced wound care technology, and retained Emergo, a global leader in the medical device regulatory field, to prepare and submit to the U.S. Food & Drug Administration (“FDA”) premarket notification of a medical device under Section 510(k) of the Food, Drug, and Cosmetic Act. The 510(k) notification was submitted to the FDA’s Center for Devices and Radiological Health (“CDRH”). The submission was subsequently referred by the CDRH to the FDA Office of Combination Products



(“OCP”), which has jurisdiction to classify a product as a drug, device, biological product, or combination product. We asked the OCP for a determination whether our product should be regulated as a medical device, drug, or combination product, and the OCP replied requesting significant additional information. The responses required to respond to the OCP requests for additional information would have required a substantial investment of time and money and as a consequence, we are not presently pursuing approval of this first product. Rather than proceed with premarket clearance for the product at this time, we chose to submit a second product for premarket notification under Section 510(k) in late June of 2018. While we remain confident that we will ultimately receive premarket clearance for this second product, we can make no assurance or prediction as to success of these efforts, and must wait patiently for the process with the FDA to conclude. The company has numerous medical device product designs that it intends to pursue as resources permit.

Clyra’s management is actively engaged in arranging for clinical work and is in discussions with a number of potential strategic partners. It also continues to actively work on the development of new products. It recently added Julian Bejarano, PhD to its executive team as an expert scientific researcher with more than 11 years of experience leading fundamental and applied research projects related to materials science and nanotechnology. In particular, Dr. Bejarano has six years of experience in projects related to biomaterials for regenerative medicine and multifunctional nanoparticles for controlled drug delivery. He holds a Materials Engineering degree and a Masters in Materials Engineering from the Universidad del Valle, Colombia. He also holds a PhD in Engineering Sciences with emphasis in Materials Science from the Universidad de Chile, Chile. Dr. Bejarano was a visiting researcher during his PhD studies at the Institute of Biomaterials at the University of Erlangen-Nuremberg, Germany. Following his doctorate studies, Dr. Bejarano was a postdoctoral fellow at the Advanced Center for Chronic Diseases in Chile for three years and Research Advisor for the Group of Polymer Engineering at the Universidad de Chile. Moreover, he has outstanding skills in project management, R&D, and innovation. His projects have been focused on the development and characterization of composites materials based on metals, polymers and ceramics, synthesis of multifunctional nanoparticles, encapsulation of therapeutic agents, and biological evaluation of materials. His findings in materials research have been published by prestigious international journals and he has presented at several international events related to biomaterials and materials science.

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**Community**

We believe it is part and parcel to our mission to make life better by supporting various socially important causes and events, and believe that doing so is a great way to help share our vision and purpose behind BioLargo, as well as our technologies. In addition to our sponsorship of scholarships with the Environmental Research and Education Foundation (EREF.org) and the National Water Research Institute (NWRI), we are often invited to be presenters and have even enjoyed recognition as award winners at multiple industry-related conferences. These include recent events such as the Metropolitan Water District of Southern California's Agriculture and Industry Relations Committee meeting; Bluetech Week in San Diego sponsored by The Maritime Alliance; an international trade mission hosted by the Canadian Embassy and Consulate in Beijing and Guangzhou that was sponsored by NRC-IRAP (National Research Council of Canada). We are honored to be the title sponsor along with Metropolitan Water District of Southern California at Sustain OC's upcoming Water Solutions 2 conference held at UC Irvine's Applied Innovation Center in Irvine, California. We have also hosted a seminar at Fresno State to share with their community the latest developments of our AOS for the treatment of livestock processing water as well as the advances of CupriDyne Clean for livestock odor control. We are also honored to provide sponsorship support at the EREF Fall Classic Fund Raising Event to further their mission to fund and direct scientific research and educational initiatives for waste management practices to benefit industry participants and the communities they serve. We were honored guests at this year's Clarke Prize Awards event sponsored by the National Water Research Institute, a highly prestigious event where NWRI honors the outstanding individual residing in the U.S. who has implemented exceptional water science research/and or policy development to solve real-world water challenges. We recently co-sponsored a Water Environment & Reuse Foundation ("WERF") onsite technical symposium where more than 80 technical leaders from around the United States joined together to discuss the current events and technical guidelines for water reuse, a growing trend in drought burdened and densely populated urban areas.

**Results of Operations—Comparison of the three and six months ended June 30, 2017 and 2018**

**Revenue**

Our revenue from product sales for the three and six months ended June 30, 2018 increased by 216% and 270%, respectively, compared with the three and six months ended June 30, 2017. Our \$315,553 in revenues from product sales for the three months ended June 30, 2018 was a 41% increase in revenue over the prior three-month period. These increases are due to increased client adoption of our CupriDyne Clean Industrial Odor Control products and an increase in volume of sales of our Specimen Transport Solidifier pouches to the U.S. military.

Sales of our CupriDyne Clean products generated approximately 60% and 57% of our revenue from product sales in the three and six months ended June 30, 2018, which is a comparable percentage to our year ended December 31,

2017 results. The majority of these sales are to leading waste handling companies with whom we have “National Purchasing Agreements”. Our CupriDyne Clean sales revenue increased due to an increase in the volume of sales resulting from continued market penetration and ongoing marketing and sales efforts. We continue to receive extremely positive feedback from our customers about our service, our product’s effectiveness, and its cost savings. To meet this demand, we are continuing to hire sales and support staff. Given the continued expansion with our national accounts, we continue to expect higher sales volume for the remainder of 2018. We do not yet have enough history or sales volume to identify trends or uncertainties related to our CupriDyne Clean sales, although we are discovering that landfills and transfer stations in colder climates generally have less of a need for odor control products during winter months. We suspect that this fact will affect our product sales during colder months, although the extent of that effect is yet unknown and difficult to predict given the continued increase in market adoption we are experiencing.

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Sales of our Specimen Transport Solidifier pouches to the U.S. Defense Logistics Agency generated approximately 40% and 43% of our revenue in the three and six months ended June 30, 2018. Sales of this product increased by approximately \$114,000 and \$200,000 for the three and six months ended June 30, 2018 compared to the same period for 2017. These sales were primarily through our distributor Downeast Logistics. The vast majority of sales of our Specimen Transport Solidifier pouches are made through a bid process in response to a request for bids to which any qualified government vendor can respond. Although the number of these bids was higher in the six months ended June 30, 2018 as compared with the same period in 2017, we do not know if this trend will continue, and cannot know in advance the frequency or size of such requests from the U.S. Government, or whether our bids will be successful. As such, we are uncertain as to our future revenues of this product through this system.

Our engineering segment generated approximately \$11,000 in revenue for the three months ended June 30, 2018. As this division started in the fourth quarter of 2017, the six months ended June 30, 2017 does not provide a comparison. For the six months ended June 30, 2018, revenue totaled approximately \$50,000. Our engineering division is working closely with our odor control division to submit proposals for the design, build and installation of misting odor control systems at client transfer station and landfills. As of the date of this Report, dozens of such proposals are outstanding. In addition to these proposals, our engineer division has multiple proposals out with other third parties to provide engineering and other services. Although we expect our engineering division to increase revenues in the future, we are unable to predict if they will have success in winning client contracts.

**Cost of Goods Sold and Services**

Our cost of goods sold includes costs of raw materials, contract manufacturing, and other direct expenses related to the manufacturing of our products. As a percentage of gross sales, our costs of goods was 61% in the three and six months ended June 30, 2018, versus 73% and 66% in the three and six months ended June 30, 2017. The decrease in our cost of goods is primarily attributed to our higher volume of sales and the resulting increased purchasing power with our component suppliers.

Our cost of services includes costs of employee time, a portion of overhead, and, when applicable, cost of subcontractors.

**Selling, General and Administrative Expense**

Our Selling, General and Administrative (“SG&A”) expenses include both cash and non-cash expenses. Our SG&A increased approximately \$115,000 (10%) and \$230,000 (10%) in the three and six months ended June 30, 2018 compared to the same periods in 2017. The largest components of our selling, general and administrative expenses included:

	Three months ended		Six months ended	
	June 30, 2017	2018	June 30, 2017	2018
Salaries and payroll related	\$394,412	\$562,298	\$720,605	\$971,562
Professional fees	133,776	185,694	327,194	377,670
Consulting	276,925	191,685	474,255	354,385
Office expense	157,996	260,646	346,867	470,334
Sales and marketing	49,861	63,310	91,517	117,415

Our SG&A expenses are increasing due primarily to the expansion of our business, both in terms of product sales and market adoption, and through the increase of service offerings. For example, the formation of our engineering subsidiary and hiring of associated personnel in the second half of 2017 resulted in increased legal and accounting fees, additional office expense related to the new office in Tennessee, and additional salaries and payroll, reflected in the three and six months ended June 30, 2018, but not for the same periods in 2017. As sales increase, we have added sales and support personnel. Our consulting fees decreased in the three and six months ended June 30, 2018 due a reduction in the use of outside business development firms during that period.

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**Research and Development**

Research and development expenses increased \$101,297 (31%) and \$231,690 (32%) for the three and six months ended June 30, 2018, as compared to the same periods in 2017. These expenses increased in part as a result of the formation of our engineering subsidiary, where we have accelerated the work related to the scale-up, engineering and testing of our AOS technology.

**Interest expense**

Interest expense increased \$1,046,912 (94%) and \$925,764 (45%) for the three and six months ended June 30, 2018, as compared to the same periods in 2017. Our interest expense increased for primarily two reasons. First, from June 30, 2017 through June 30, 2018, our outstanding debt balance increased by approximately \$2,000,000. Second, during the three months ended June 30, 2018, we recorded \$275,534 interest expense related to the early conversion of promissory notes.

We recently have reduced our liabilities by over \$5,800,000 through the conversion of debt to common stock, and thus in future periods we expect our interest expense to decrease significantly (by approximately \$150,000 per quarter, assuming no new additional debt).

**Net Loss**

Net loss increased \$1,147,727 (45%) and \$1,251,699 (26%) for the three and six months ended June 30, 2018, as compared to the same periods in 2017. The net loss was somewhat offset by an increase in revenue, nevertheless, the net loss increased mainly due to the increased interest expense and to increased research and development expense. The net loss per share did not change as the increase in net loss was offset by the increase in common shares outstanding. Although our sales continue to increase, we expect to continue to incur a net loss for the foreseeable future. (See Part I, Item II, "Our Business", above.)

**Liquidity and Capital Resources**

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Our total cash and cash equivalents was \$651,061 at June 30, 2018, a decrease of approximately \$339,000 since December 31, 2017. We

had revenues of \$589,767 in the six months ended June 30, 2018. Our gross profits are not sufficient to fund our operations. We have been required to financially support the operations of our subsidiaries, none of which are operating at a positive cash flow.

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying consolidated financial statements, for the six months ended June 30, 2018 we had a net loss of \$6,029,478, used \$2,053,111 cash in operations, and at June 30, 2018 had negative working capital of \$120,187, current assets of \$823,302, and an accumulated stockholders' deficit of \$107,329,788. As of June 30, 2018, we had \$2,044,714 in principal amounts due on various debt obligations, of which \$334,239 was subsequently converted to common stock, and one note, in the amount of \$447,975, is scheduled to mature September 18, 2018. At our current stock prices, we cannot compel the conversion of the note into stock and are examining alternatives to refinance the obligation. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies, and achieve profitable operations by licensing or otherwise commercializing products incorporating our technologies. The consolidated financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

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Only one subsidiary, Clyra, has financing in place to fund operations for the immediate future. It is important to note that Clyra intends to pursue direct investment to support its further product development and go to market strategy. Sales of our CupriDyne Clean products are increasing, and our engineering subsidiary has begun generating revenue, but we do not expect those divisions to support the general corporate overhead in the immediate future. As such, we will be required to raise substantial additional capital to continue our operations and fund our future business plans. We are continuing our efforts to raise capital through our purchase agreement with Lincoln Park (see Note 4, of the Notes to the Consolidated Financial Statements), a current private securities offering (see Note 5, of the Notes to the Consolidated Financial Statements), and in association with our plan to uplist our stock to Nasdaq. We are reluctant to utilize the Lincoln Park instrument when our stock price is below \$0.25 because doing so would trigger the reduction of warrant exercise prices on some outstanding warrants. During the six months ended June 30, 2018, we received \$380,803 from sales of stock to Lincoln Park, and an aggregate \$852,500 net proceeds from our private securities offerings (including Lincoln Park).

In addition to our financing arrangement with Lincoln Park, and the private securities offerings discussed above, we are continuing to explore alternatives for our current and longer-term financial requirements, including additional raises of capital from investors in the form of convertible debt or equity, a fully underwritten public offering associated with our plan to uplist our stock to Nasdaq, and significant grant funding from government sources. It is unlikely that we will be able to qualify for bank or other financial institutional debt financing until such time as our operations are considerably more advanced and we are able to demonstrate the financial strength to provide confidence for a lender, which we do not currently believe is likely to occur for at least the next 12 months or more.

If we are unable to raise sufficient capital, we may be required to curtail some of our operations, including efforts to develop, test, market, evaluate and license our technologies and products. If we were forced to curtail aspects of our operations, there could be a material adverse impact on our financial condition and results of operations.

## **Critical Accounting Policies**

Our unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. Preparation of these statements requires management to make judgments and estimates. Some accounting policies have a significant impact on amounts reported in these financial statements. A summary of significant accounting policies and a description of accounting policies that are considered critical may be found in our Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on March 14, 2018, in the Notes to the Consolidated Financial Statements and the Critical Accounting Estimates sections. In addition, refer to Note 2 to the consolidated interim consolidated financial statements included in Part I, Item 1 of this report.

The methods, estimates, and judgments the Company uses in applying these most critical accounting policies have a significant impact on the results of the Company reports in its consolidated financial statements.



It the Company's policy to expense share based payments as of the date of grant in accordance with Auditing Standard Codification Topic 718 "Share-Based Payment." Application of this pronouncement requires significant judgment regarding the assumptions used in the selected option pricing model, including stock price volatility and employee exercise behavior. Most of these inputs are either highly dependent on the current economic environment at the date of grant or forward-looking expectations projected over the expected term of the award. As a result, the actual impact of adoption on future earnings could differ significantly from our current estimate.

### **Recent Accounting Pronouncements**

See Note 2, "Recent Accounting Pronouncements", to the Consolidated Financial Statements.

### **Item 4. Controls and Procedures**

We conducted an evaluation, under the supervision and with the participation of management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Report.

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Our procedures have been designed to ensure that the information relating to our company, including our consolidated subsidiaries, required to be disclosed in our SEC reports is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow for timely decisions regarding required disclosure. However, our Company is continuing to grow and evolve in 2018, as we have added a new accounting manager for Odor No More and the engineering division and implemented more detailed reviews of the accounting records. In late 2017, we added an engineering division operating in Tennessee. The volume of our product sales continues to grow, increasing strain on our accounting systems. And, our operations do not yet generate enough cash to fund operations, and thus we rely on financing activities to maintain our level of operations and fund our anticipated growth. These activities put stress on our overall controls and procedures. Although we have made some improvements, our chief executive officer and chief financial officer have concluded that as of the evaluation date our disclosure controls and procedures were not effective, due to the material weakness identified below.

It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). 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 the 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 our assets that could have a material effect on the financial statements.

Under the supervision and with the participation of our management, including our chief executive officer and the chief financial officer, we have established internal control procedures in accordance with the guidelines established in the 2013 Framework —Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). Recognizing the dynamic nature and growth of the Company’s business during the prior 12 months, including the addition of an engineering division, growth of the core operations, and the increase in the number of employees, management has recognized the strain on the overall internal control environment. As a result, management has concluded that its internal controls over financial reporting are not effective. Management identified a material weakness with respect to deficiencies in its financial closing and reporting procedures. Management believes this is due to a lack of resources. Management intends to add accounting personnel and operating staff and more sophisticated systems in order to improve its reporting procedures and internal controls, subject to available capital. A material weakness is a significant deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected. Although management believes progress was made related to remediating the material weakness noted at December 31, 2017 by adding a new accounting manager and implementing more detailed reviews of the accounting records, it believes additional changes will be necessary to

alleviate its concerns as the company grows. There was no further change in our internal control over financial reporting that occurred during the six-month period covered by this Report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Our management, including our chief executive officer and chief financial officer, does not expect that our disclosure controls or our internal control over financial reporting, or any system we design or implement in the future, 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 control system's objectives will be met. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

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**PART II**

**OTHER INFORMATION**

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

**Stock Issued for Services**

During the three months ended June 30, 2018, we issued 733,821 shares of common stock in lieu of fees for service provided by consultants, resulting in a grant date fair value of \$210,548. Of the shares issued, 309,390 were issued under the Company's 2018 Equity Incentive Plan and registered with the SEC on Form S-8.

During the three months ended June 30, 2018, we issued 1,302,734 shares of common stock as payment for interest due on unit offering notes, resulting in a grant date fair value of \$328,760.

**FirstFire Global Opportunity Fund Investment**

On January 16, 2018, we entered into a securities purchase agreement (the "FirstFire Purchase Agreement") and a registration rights agreement (the "FirstFire RRA") with FirstFire Global Opportunity Fund, LLC ("FirstFire"), and issued a convertible promissory note (the "FirstFire Note") in the aggregate principal amount of \$150,000 at 5% annual interest, which is convertible into shares of common stock of the Company at \$0.394 per share, subject to the terms, and certain limitations and conditions set forth in the FirstFire Purchase Agreement and FirstFire Note.

Pursuant to the FirstFire Purchase Agreement, the Company issued 75,000 shares of common stock to FirstFire as a commitment fee (the "FirstFire Commitment Shares").

We filed a registration statement with the SEC on February 8, 2018, that was deemed effective on February 8, 2018, registering 394,949 shares to be sold by FirstFire. In June 2018, FirstFire elected to convert \$95,761 of the outstanding principal balance of the FirstFire Note and we issued 383,047 shares as payment of principal, and an

additional 11,902 in payment of interest. Subsequent to June 30, 2018, FirstFire elected to convert the remainder of its note to stock, and we issued 217,960 shares as payment of principal and interest to satisfy that obligation. The 217,960 shares were not registered with the SEC.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

## **Item 5. Other Information**

### **Uplist of Common Stock to NASDAQ**

On July 25, 2018, we submitted an application for listing on The Nasdaq Capital Market, commonly known as NASDAQ. We believe that listing our common stock on a national exchange will offer a series of benefits to both the company and our stockholders, including making our stock more attractive to a larger pool of investors, removing restrictions that currently prohibit many investors from purchasing our stock (because it is currently traded on the OTCQB), increasing liquidity for our stockholders, and through increased financial and governance requirements, by enhancing the Company's profile to potential investors. If successful, the company's stockholders will also benefit from expanded awareness by inclusion in a number of indexes that are tracked by buy-side institutions and that will increase the likelihood of analyst coverage.

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We do not currently meet certain Nasdaq listing requirements, including \$5,000,000 in stockholder equity and a minimum bid price of \$4.00 per share. We have engaged a New York based investment banking firm to underwrite a public offering to raise the capital necessary for us to meet the stockholder equity requirement, and have scheduled a special meeting of our stockholders on September 26, 2018 to approve an amendment to our Certificate of Incorporation that would effectively raise the price of our common stock to meet the minimum bid price requirement. We intend to work on these requirements in tandem with our listing application. There is no assurance that Nasdaq will approve our listing application even if we meet all of its initial listing requirements, and we will not proceed with the contemplated underwritten offering or reverse stock split if we are not assured that our stock will be listed on a national exchange.

**Issuance of Stock Options in exchange for payment of payables**

During the three months ended June 30, 2018, we issued options to purchase 685,809 shares of our common stock at exercise prices ranging between \$0.23 – \$0.43 per share to employees, vendors and to members of our board of directors in exchange for unpaid obligations for their services. The fair value of the options totaled \$226,807 and is recorded as selling, general and administrative expenses.

**Sales of Registered Stock to Lincoln Park**

During the three months ended June 30, 2018, we sold to Lincoln Park (see Note 4) 606,751 shares of our common stock, and received \$212,583 in proceeds. Associated with these sales, we issued Lincoln Park 10,394 “additional commitment shares.”

**Convertible Note, matures June 15, 2021 (OID Note)**

On June 15, 2018, we received \$75,000 and we issued a convertible promissory note (titled the “OID Note”) for 100% of the funds received, or \$82,500. The convertible promissory note is convertible into shares of the company’s common stock at a conversion price of \$0.30 per share. The original issuance discount totaled \$7,500, recorded as a discount on convertible notes on our balance sheet. The discount will be amortized and recorded to interest expense over the term of the note. The convertible promissory note matures June 15, 2021 and incurs interest at the rate of 15% per annum on the OID Note. Interest due will be paid quarterly in arrears in shares of common stock, paid at a conversion price equal to the average closing price of the Company’s common stock over the 20 trading days prior to the interest payment due date. The OID Note is convertible by the investor at any time, and convertible by the Company (i) at maturity, (ii) in the event the Company’s stock price closes at two times the conversion price for 20 consecutive days, provided that either the shares underlying the convertible note are registered with the SEC, or more than six months has elapsed since the date of the investment.

**Amendment to Bylaws**

On August 14, 2018, our board of directors amended our bylaws to modify Section 1.4 such that the holders of one-third of the Company's outstanding shares of each class of stock entitled to vote at a stockholder meeting shall be present in person or by proxy in order to constitute a quorum. Prior to the amendment, Section 1.4 required holders of one-half the outstanding shares of each class of stock entitled to vote at a stockholder meeting be present in person or by proxy in order to constitute a quorum.

**Item 6. Exhibits**

The exhibits listed in the Exhibit Index following the signature pages of this Quarterly Report on Form 10-Q are filed with, or furnished with, or incorporated by reference in, this Quarterly Report on Form 10-Q.

**SIGNATURES**

Pursuant to the requirements 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.

BIOLARGO, INC.

Date: August 14, 2018 By: /s/ DENNIS P. CALVERT  
Dennis P. Calvert

Chief Executive Officer

Date: August 14, 2018 By: /s/ CHARLES K. DARGAN, II  
Charles K. Dargan II  
Chief Financial Officer





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<b><u>Exhibit</u></b>	<b><u>Exhibit Description</u></b>	<b><u>Incorporated by Reference</u></b>	<b><u>Herein</u></b>
<b><u>Number</u></b>		<b><u>Filed</u></b>	<b><u>Date</u></b>
3.1	<u>Amended and Restated Certificate of Incorporation for BioLargo, Inc. filed March 16, 2007</u>	Form 10-KSB	5/21/2007
3.2	<u>Certificate of Amendment to Certificate of Incorporation, filed May 25, 2018</u>	Pos Am	6/22/2018
3.3	<u>Bylaws of BioLargo, Inc., as amended and restated</u>	Form 10-KSB	5/23/2003
3.4*	<u>Amendment to bylaws</u>	N/A	
4.1	<u>Form of Convertible Promissory Note issued in 2015 Unit Offering</u>	Form 10-K	3/31/2015
4.2	<u>Form of Series A Stock Purchase Warrant issued in 2015 Unit Offering</u>	Form 10-K	3/31/2015
4.3	<u>Form of Stock Options issued in exchange for reduction in accounts payable.</u>	Form 10-K	3/31/2015
4.4	<u>Amended and Restated Articles of Incorporation of Clyra Medical Technologies, Inc.</u>	Form 8-K	1/6/2016
4.5	<u>Form of Warrant issued to One Year Note holder in July 2016</u>	Form 10-Q	8/15/2016
4.6	<u>Form of Note Issued in Winter 2016 Unit Offering</u>	Form S-1	1/25/2017
4.7	<u>Form of Warrant Issued in Winter 2016 Unit Offering</u>	Form S-1	1/25/2017
4.8	<u>Form of Warrant issued to One Year Note holder dated December 30, 2016</u>	Form S-1	1/25/2017
4.9	<u>Option to purchase common stock issued to Dennis P. Calvert dated May 2, 2017</u>	Form 8-K	5/4/2017
4.10	<u>Form of Note issued in Summer 2017 Offering</u>	Form 10-Q	8/14/2017
4.11	<u>Form of Warrant issued in Summer 2017 Offering</u>	Form 10-Q	8/14/2017
4.12	<u>Form of One-Year Note issued July 2017</u>	Form 10-Q	8/14/2017
4.13	<u>Form of Warrant issued to One-Year Noteholder July 2017</u>	Form 10-Q	8/14/2017
4.14	<u>\$440,000 convertible note, matures July 20, 2019</u>	Form 10-Q	8/14/2017
4.15	<u>Purchase Agreement, dated as of August 25, 2017 by and between BioLargo, Inc. and Lincoln Park Capital Fund, LLC</u>	Form 8-K	8/31/2017

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4.16	<u>Registration Rights Agreement, dated as of August 25, 2017, by and between BioLargo, Inc. and Lincoln Park Capital Fund, LLC</u>	Form 8/31/2017 8-K
4.17	<u>Securities Purchase Agreement, dated as of December 14, 2017 by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 12/22/2017 8-K
4.18	<u>Registration Rights Agreement, dated as of December 14, 2017, by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 12/22/2017 8-K
4.19	<u>Note, dated as of December 14, 2017, by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 12/22/2017 8-K
4.20	<u>Amendment, dated as of December 18, 2017, by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 12/22/2017 8-K
4.21	<u>Stock Option dated December 31, 2017, issued to Chief Financial Officer Charles K. Dargan II</u>	Form 1/3/2018 8-K

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4.22	<u>Line of credit, matures September 1, 2019</u>	Form 10-Q	5/14/2018
4.23	<u>Warrant issued with Line of credit that matures September 1, 2019</u>	Form 10-Q	5/14/2018
4.24	<u>\$50,000 convertible note, matures March 8, 2020</u>	Form 10-Q	5/14/2018
4.25	<u>Form of convertible notes that mature April 20, 2021 (Spring 2018 Offering)</u>	Form 10-Q	5/14/2018
4.26	<u>Form of warrant issued with convertible notes that mature April 20, 2021 (Spring 2018 Offering)</u>	Form 10-Q	5/14/2018
4.27	<u>Amendment to \$440,000 convertible notes that matures July 20, 2019</u>	Form 10-Q	5/14/2018
4.28	<u>2018 Equity Incentive Plan</u>	Form S-8	6/22/2018
4.29	<u>Notice of Restricted Stock Unit Award under 2018 Equity Incentive Plan</u>	Form S-8	6/22/2018
4.30	<u>Restricted Stock Unit Award Agreement under 2018 Equity Incentive Plan</u>	Form S-8	6/22/2018
4.31	<u>Notice of Stock Option Grant under 2018 Equity Incentive Plan</u>	Form S-8	6/22/2018
4.32	<u>Stock Option Award Agreement under 2018 Equity Incentive Plan</u>	Form S-8	6/22/2018
10.1†	<u>February 10, 2017 extension to Engagement Extension Agreement with Charles K. Dargan, II.</u>	Form 8-K	2/14/2017
10.2†	<u>Employment Agreement with Dennis P. Calvert dated May 2, 2017.</u>	Form 8-K	5/4/2017
10.3†	<u>Lock-Up Agreement with Dennis P. Calvert dated April 30, 2017</u>	Form 8-K	5/4/2017
10.4†	<u>Lock-Up Agreement with Dennis P. Calvert dated May 2, 2017.</u>	Form 8-K	5/4/2017
10.5†	<u>Engagement Agreement extension dated December 31, 2017, between BioLargo, Inc. and Charles K. Dargan, II</u>	Form 8-K	1/3/2018
31.1*	<u>Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and Rules 13(a)-14 and 15(d)-14 under the Securities Exchange Act of 1934</u>		
31.2*	<u>Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and Rules 13(a)-14 and 15(d)-14 under the Securities Exchange Act of 1934</u>		
32*	<u>Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.</u>		
101.INS**	XBRL Instance		
101.SCH**	XBRL Taxonomy Extension Schema		
101.CAL**	XBRL Taxonomy Extension Calculation		
101.DEF**	XBRL Taxonomy Extension Definition		
101.LAB**	XBRL Taxonomy Extension Labels		
101.PRE**	XBRL Taxonomy Extension Presentation		

\* Filed herewith

\*\* Furnished herewith

† Management contract or compensatory plan, contract or arrangement

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