ATOSSA GENETICS INC
Form 10-Q
November 13, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2017

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: 001-35610

ATOSSA GENETICS INC.

(Exact name of registrant as specified in its charter)

Delaware	**26-4753208**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
107 Spring Street **Seattle, WA**	**98104**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (206) 325-6086

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

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

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

The number of shares of the registrant's common stock, $0.015 par value per share, outstanding at November 13, 2017 was 26,522,741.

ATOSSA GENETICS INC.

FORM 10-Q

QUARTERLY REPORT

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PART I. FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

ATOSSA GENETICS INC.

CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	September 30, 2017	December 31, 2016
Assets		
Current assets		
Cash and cash equivalents	$2,733,663	$3,027,962
Restricted cash	55,000	55,000
Prepaid expenses	157,406	171,601
Other accounts receivable	4,040	
Total current assets	2,950,109	3,254,563
Furniture and equipment, net	14,435	55,119
Intangible assets, net	561,354	640,440
Other assets	108,723	194,250
Total assets	$3,634,621	$4,144,372
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	$380,399	$254,320
Accrued expenses	50,542	16,964
Payroll liabilities	627,587	769,899
Other current liabilities	13,295	6,083
Total current liabilities	1,071,823	1,047,266
Commitments and contingencies (note 13)		
Stockholders' equity		
Preferred stock - $.001 par value; 10,000,000 shares authorized, no shares issued or outstanding		
Common stock - $.015 par value; 75,000,000 shares authorized, 14,022,741 and 3,786,913 shares issued and outstanding, as of September 30, 2017 and December 31, 2016, respectively	210,341	56,804

Additional paid-in capital	65,785,758	60,344,050
Accumulated deficit	(63,433,301)	(57,303,748)
Total stockholders’ equity	2,562,798	3,097,106
Total liabilities and stockholders’ equity	$3,634,621	$4,144,372

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

ATOSSA GENETICS INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	For the Three Months Ended September 30,		For The Nine Months Ended September 30,	
	2017	2016	2017	2016
Operating expenses:				
Research and development	$742,450	$85,000	$2,110,846	$403,963
General and administrative	1,313,477	1,473,435	3,528,189	5,040,939
Total operating expenses	2,055,927	1,558,435	5,639,035	5,444,902
Operating loss	(2,055,927)	(1,558,435)	(5,639,035)	(5,444,902)
Change in fair value of common stock warrants	(128,300)		(280,747)	
Warrant financing expense			(192,817)	
Other income (expense), net	(283)	1,763,124	(16,954)	1,599,667
Income (loss) before income taxes	(2,184,510)	204,689	(6,129,553)	(3,845,235)
Income taxes				
Net income (loss)	$(2,184,510)	$204,689	$(6,129,553)	$(3,845,235)
Deemed dividends attributable to Series A Preferred Stock			(2,568,132)	
Net income (loss) applicable to common stockholders	$(2,184,510)	$204,689	$(8,697,685)	$(3,845,235)
Income (loss) per common share - basic and diluted	$(0.18)	$0.07	$(1.10)	$(1.44)
Weighted average shares outstanding, basic and diluted	12,411,145	3,024,393	7,886,210	2,665,904

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

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ATOSSA GENETICS, INC.

CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(UNAUDITED)

	Series A Convertible Preferred Stock			**Common Stock**		**Additional**		**Total**
	Shares	**Amount**	**Additional Paid-in Capital**	**Shares**	**Amount**	**Paid-in Capital**	**Accumulated Deficit**	**Stockholders' Equity**
Balance at December 31, 2016	**—**	**$—**	**$—**	**3,786,913**	**$56,804**	**$60,344,050**	**$(57,303,748)**	**$3,097,106**
Issuance of common stock in Class A units, net of issuance costs of $65,816				1,194,000	17,910	811,774		829,684
Allocation of Class A unit proceeds to warrant liability						(328,350)		(328,350)
Issuance of Series A convertible preferred stock in Class B units, net of issuance costs of $267,231	3,502	4	3,234,769					3,234,773
Allocation of Series A convertible preferred stock to warrants and beneficial conversion feature			(2,568,132)			1,284,066		(1,284,066)
Deemed Dividends on Series A			2,568,132			(2,568,132)		

convertible preferred stock								
Conversion of Series A convertible preferred stock to common stock	(3,502)	(4)	(3,234,769)	4,669,329	70,040	3,164,733		
Reclassification of warrant liability upon exercise of common stock warrants				1,490,833	22,362	1,870,798		1,893,160
Issuance of common stock upon warrant exercise for cash				2,881,666	43,225	706,008		749,233
Amortization of commitment shares						(59,558)		(59,558)
Compensation cost for stock options granted to executives and employees						560,369		560,369
Net loss							(6,129,553)	(6,129,553)
Balance at September 30, 2017		**$**	**$**	**14,022,741**	**$210,341**	**$65,785,758**	**$(63,433,301)**	**$2,562,798**

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

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ATOSSA GENETICS INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	For the Nine Months Ended September 30, 2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$(6,129,553)	$ (3,845,235)
Compensation cost for stock options granted	560,369	650,053
Loss on disposal of intangible asset	17,695	163,333
Depreciation and amortization	102,074	227,387
Change in fair value of common stock warrants	280,747	
Warrant financing expense	192,817	
Changes in operating assets and liabilities:		
Change in restricted cash		220,000
Prepaid expenses	14,195	72,542
Other assets	25,831	131,176
Accounts payable	126,079	(617,094)
Payroll liabilities	(142,312)	(524,288)
Accrued expenses	33,578	(451,196)
Other current liabilities	7,212	(45,242)
Net cash used in operating activities	(4,911,268)	(4,018,564)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of furniture and equipment		(5,023)
Net cash used in investing activities		(5,023)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of Class A and Class B Units, net of issuance costs	3,871,636	
Proceeds from exercise of warrants	745,333	
Proceeds from issuance of common stock, net of issuance costs		4,695,869
Net cash provided by financing activities	4,616,969	4,695,869
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(294,299)	672,282
CASH AND CASH EQUIVALENTS, BEGINNING BALANCE	3,027,962	3,715,895
CASH AND CASH EQUIVALENTS, ENDING BALANCE	$2,733,663	$ 4,388,177
SUPPLEMENTAL DISCLOSURES:		
Interest paid	$	$ 1,304
NONCASH INVESTING AND FINANCING ACTIVITIES:		
Reclassification of warrant liability upon exercise of common stock warrants	$1,893,160	$
Amount receivable for warrant exercise	3,900	

Allocation of Class A and Class B Unit proceeds to warrant liability	1,612,413	
Common stock issued as commitment fee under stock purchase agreement		198,523
Amortization of commitment shares	$59,558	$ 26,470

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

ATOSSA GENETICS INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

NOTE 1: NATURE OF OPERATIONS

Atossa Genetics Inc. (the “Company”) was incorporated on April 30, 2009 in the State of Delaware. The Company was formed to develop and market medical devices, laboratory tests and therapeutics to address breast health conditions. The Company’s fiscal year ends on December 31. The Company is focused on development of its pharmaceutical and drug delivery programs.

NOTE 2: GOING CONCERN

The Company’s consolidated financial statements are prepared using Generally Accepted Accounting Principles in the United States of America applicable to a going concern, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. The Company has incurred net losses and negative operating cash flows since inception. For the nine months ended September 30, 2017, the Company recorded a net loss of approximately $6.1 million and used approximately $4.9 million of cash in operating activities. As of September 30, 2017, the Company had approximately $2.7 million in cash and cash equivalents and working capital of approximately $1.9 million. The Company has not yet established an ongoing source of revenue sufficient to cover its operating costs and allow it to continue as a going concern. The ability of the Company to continue as a going concern is dependent on the Company obtaining adequate capital to fund operating losses until it becomes profitable. The Company can give no assurances that any additional capital that it is able to obtain, if any, will be sufficient to meet its needs, or that any such capital will be obtained on acceptable terms. If the Company is unable to obtain adequate capital, it could be forced to cease operations or substantially curtail its activities. These conditions raise substantial doubt as to the Company’s ability to continue as a going concern. The accompanying consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classification of liabilities should the Company be unable to continue as a going concern.

Management’s plan to continue as a going concern is as follows. In order to continue as a going concern, the Company will need, among other things, additional capital resources. Management’s plans to obtain such resources for the Company include obtaining capital from the sale of its equity securities and short-term borrowings from banks, stockholders or other related party(ies), if needed. However, management cannot provide any assurance that the Company will be successful in accomplishing any of its plans.

As of the date of filing this quarterly report, we expect that our existing resources will be sufficient to fund our planned operations for the next 8-12 months; however, additional capital resources will be needed to fund operations longer-term.

The ability of the Company to continue as a going concern is dependent upon its ability to successfully accomplish the plans described in the preceding paragraphs and eventually to secure other sources of financing and attain profitable operations.

On October 26, 2017, the Company entered into an underwriting agreement with Maxim Group LLC relating to a public offering of common stock which closed on October 30, 2017. The offering generated gross proceeds to the Company of approximately $5.5 million and net proceeds of $5.1 million after deducting underwriting discounts and commission.

NOTE 3: SUMMARY OF ACCOUNTING POLICIES

Basis of Presentation:

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. They do not include all information and notes required by GAAP for complete financial statements. However, except as disclosed herein, there has been no material change in the information disclosed in the Notes to Consolidated Financial Statements included in the Annual Report on Form 10-K of the Company for the year ended December 31, 2016.

In the opinion of management, all adjustments (including normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and nine months ended September 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017.

On August 26, 2016, the Company completed a 1-for-15 reverse stock split of the shares of the Company’s common stock (the “Reverse Stock Split”). As a result of the Reverse Stock Split, every 15 shares of issued and outstanding common stock were combined into one issued and outstanding share of Common Stock, and the par value per share was changed to $.015 per share. No fractional shares were issued because of the Reverse Stock Split and any fractional shares that would otherwise have resulted from the Reverse Stock Split were paid in cash. The number of authorized shares of common stock was not reduced as a result of the Reverse Stock Split. The Company’s common stock began trading on a reverse stock split-adjusted basis on August 26, 2016. All share and per share data included in this report has been retroactively restated to reflect the Reverse Stock Split.

Use of Estimates:

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period. Actual results could differ from those estimates.

Financial Instruments with Characteristics of Both Liabilities and Equity:

During the nine months ended September 30, 2017, the Company issued certain financial instruments, consisting of warrants to purchase common stock, which have characteristics of both liability and equity. Financial instruments such as warrants that are classified as liabilities are fair valued upon issuance and are remeasured at fair value at subsequent reporting periods with the resulting change in fair value recorded in “change in fair value of common stock warrants”. The fair value of warrants is estimated using valuation models that require the input of subjective assumptions including stock price volatility, expected life, and the probability of future equity issuances and their impact to the price protection feature.

Recently Issued Accounting Pronouncements:

In February 2016, Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-02, *Lease Accounting Topic 842.* This ASU requires a lessee to recognize lease assets and liabilities on the balance sheet for all arrangements with terms longer than 12 months. The new standard applies a right-of-use (ROU) model that requires a lessee to record, for all leases with a lease term of more than 12 months, an asset representing its right to use the underlying asset for the lease term and a liability to make lease payments. The lease term is the non-cancellable period of the lease, and includes both periods covered by an option to extend the lease, if the lessee is reasonably certain to exercise that option, and periods covered by an option to terminate the lease, if the lessee is reasonably certain not to exercise that termination option. For leases with a lease term of 12 months or less, a practical expedient is available whereby a lessee may elect, by class of underlying asset, not to recognize an ROU asset or lease liability. A lessee making this accounting policy election would recognize lease expense over the term of the lease, generally in a straight-line pattern. The lessor accounting remains largely consistent with existing U.S. GAAP. The new standard takes effect in 2019 for public business entities. The Company has not adopted the provisions of ASU No. 2016-02. The Company is currently evaluating the impact of adopting ASU 2016-02 on its consolidated financial statements.

In April 2016, the FASB issued ASU No. 2016-09, *Compensation - Stock Compensation,* simplifying the accounting for share-based payment transactions including the income tax consequences, classification of awards as either equity or liabilities and classification on the statements of cash flows. Under the new standard, all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit on the statements of income. We adopted ASU No. 2016-09 effective January 1, 2017. As a result of the adoption of this guidance, we made an accounting policy election to recognize the effect of forfeitures in compensation cost when they occur. There was an immaterial impact on results of operations and financial position and no impact on cash flows at adoption.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows*, amending the presentation of restricted cash within the statement of cash flows. The new guidance requires that restricted cash be included within cash and cash equivalents on the statement of cash flows. The ASU is effective retrospectively for reporting periods beginning after December 15, 2017, with early adoption permitted. The Company has not yet adopted the provisions of ASU No. 2016-18 and does not expect it will have a material impact on the financial statements upon adoption.

In July 2017, the FASB issued ASU 2017-11, *Accounting for Certain Financial Instruments with Down Round Features and Replacement of the Indefinite Deferral for Mandatorily Redeemable Financial Instruments of Certain Nonpublic Entities and Certain Mandatorily Redeemable Noncontrolling Interests with a Scope Exception*. Part I of this ASU addresses the complexity of accounting for certain financial instruments with down round features. Down round features are features of certain equity-linked instruments (or embedded features) that result in the strike price being reduced on the basis of future equity offerings. Current accounting guidance requires financial instruments with down round features to be accounted for at fair value. Part II of the Update applies only to nonpublic companies and is therefore not applicable to the Company. The amendments in Part I of the Update change the classification analysis of certain equity-linked financial instruments (or embedded features) with down round features. When determining whether certain financial instruments should be classified as liabilities or equity instruments, a down round feature no longer precludes equity classification when assessing whether the instrument is indexed to an entity's own stock. As a result, a freestanding equity-linked financial instrument (or embedded conversion option) no longer would be accounted for as a derivative liability at fair value as a result of the existence of a down round feature. For freestanding equity-classified financial instruments, the amendments require entities that present earnings per share (EPS) in accordance with Topic 260 to recognize the effect of the down round feature when it is triggered. That effect is treated as a dividend and as a reduction of income available to common shareholders in basic EPS. This Update is effective for public entities for fiscal years beginning after December 15, 2018. Early adoption is permitted. The Company has not yet determined when it will adopt the provisions of this Update and has not yet determined the impact on its consolidated financial statements upon adoption.

NOTE 4: PREPAID EXPENSES

Prepaid expenses consisted of the following:

	September 30, 2017	December 31, 2016
Prepaid insurance	$ 39,132	$ 121,333
Trade show		20,000
Retainer and security deposits	14,218	14,218
Professional services	81,250	
Financial exchange fees	10,500	
Other	12,306	16,050
Total prepaid expenses	$ 157,406	$ 171,601

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NOTE 5: FURNITURE AND EQUIPMENT

Furniture and equipment consisted of the following:

	September 30, 2017	December 31, 2016
Furniture and equipment	$170,917	$210,528
Less: Accumulated depreciation	(156,482)	(155,409)
Total furniture and equipment, net	$14,435	$55,119

Depreciation expense for the three months ended September 30, 2017 and 2016 was $4,554 and $29,698, respectively, and $22,988, and $92,054, for the nine months ended September 30, 2017 and 2016, respectively.

NOTE 6: INTANGIBLE ASSETS

Intangible assets consisted of the following:

	September 30, 2017	December 31, 2016
Patents	$639,000	$639,000
Software	113,540	113,540
Total intangible assets	752,540	752,540
Less: Accumulated amortization	(191,186)	(112,100)
Total intangible assets, net	$561,354	$640,440

Software amounted to $113,540 as of September 30, 2017 and December 31, 2016. The amortization period for the purchased software is three years. Amortization expense related to software for the three months ended September 30, 2017 and 2016 was $6,759 and $7,857, respectively, and was $26,373 and $23,572, for the nine months ended September 30, 2017 and 2016, respectively.

Patents amounted to $639,000 as of September 30, 2017 and December 31, 2016, and mainly consisted of patents acquired from Acueity on September 30, 2012 in an asset purchase transaction. Patent assets are amortized based on their determined useful life, and tested annually for impairment. The amortization period is from 7 to 12 years. Amortization expense related to patents was $17,571 and $37,253 for the three months ended September 30, 2017 and 2016, respectively and was $52,713 and $111,761 for the nine months ended September 30, 2017 and 2016, respectively.

Future estimated amortization expenses as of September 30, 2017 for the five succeeding years is as follows:

For the years ending December 31,	**Amounts**
2017 (includes the remainder of the year)	$23,952
2018	73,433
2019	70,285
2020	70,285
2021	70,285
Thereafter	253,114
	$561,354

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NOTE 7: PAYROLL LIABILITIES

Payroll liabilities consisted of the following:

	September 30, 2017	December 31, 2016
Accrued bonus payable	$ 423,000	$ 609,337
Accrued vacation	140,384	94,514
Accrued payroll liabilities	64,203	66,048
Total payroll liabilities	$ 627,587	$ 769,899

NOTE 8: STOCKHOLDERS' EQUITY

The Company is authorized to issue a total of 85,000,000 shares of stock consisting of 75,000,000 shares of common stock, par value $0.015 per share, and 10,000,000 shares of preferred stock, par value $0.001 per share. The Company has designated 750,000 shares of Series A Junior Participating Preferred Stock, par value $0.001 per share, and 4,000 shares of Series A convertible preferred stock, par value $0.001 per share through the filings of certificates of designation with the Delaware Secretary of State, none of which are issued and outstanding as of September 30, 2017.

On May 19, 2014, the Company adopted a stockholder rights agreement which provides that all stockholders of record on May 26, 2014 received a non-taxable distribution of one preferred stock purchase right for each share of the Company's common stock held by such stockholder. Each right is attached to and trades with the associated share of common stock. The rights will become exercisable only if one of the following occurs: (1) a person becomes an "Acquiring Person" by acquiring beneficial ownership of 15% or more of the Company's common stock (or, in the case of a person who beneficially owned 15% or more of the Company's common stock on the date the stockholder rights agreement was executed, by acquiring beneficial ownership of additional shares representing 2.0% of the Company's common stock then outstanding (excluding compensatory arrangements)), or (2) a person commences a tender offer that, if consummated, would result in such person becoming an Acquiring Person. If a person becomes an Acquiring Person, each right will entitle the holder, other than the Acquiring Person and certain related parties, to purchase a number of shares of the Company's common stock with a market value that equals twice the exercise price of the right. The initial exercise price of each right is $15.00, so each holder (other than the Acquiring Person and certain related parties) exercising a right would be entitled to receive $30.00 worth of the Company's common stock. If the Company is acquired in a merger or similar business combination transaction at any time after a person has become an Acquiring Person, each holder of a right (other than the Acquiring Person and certain related parties) will be entitled to purchase a similar amount of stock of the acquiring entity.

2016 Issuances of Additional Shares to Aspire Capital

On November 11, 2015, we terminated our prior agreement with Aspire Capital Fund, LLC ("Aspire Capital") and entered into a new common stock purchase agreement. Concurrently with entering into the new purchase agreement, we also entered into a registration rights agreement with Aspire Capital in which we agreed to register 405,747 shares of our common stock.

During the first quarter of 2016, we sold a total of 405,747 shares of common stock to Aspire Capital under the stock purchase agreement dated November 11, 2015 with aggregate gross proceeds to the Company of $2,177,083, or net proceeds of $2,133,973 after deducting costs of the offering.

On May 25, 2016, the Company terminated the November 11, 2015 stock purchase agreement with Aspire Capital and entered into a new common stock purchase agreement with Aspire Capital which provided that, upon the terms and subject to the conditions and limitations set forth therein, Aspire Capital is committed to purchase up to an aggregate of $10.0 million of shares of our common stock over the 30-month term of the purchase agreement, subject to the terms and conditions set forth therein. Concurrently with entering into the purchase agreement, the Company also entered into a registration rights agreement with Aspire Capital, in which the Company agreed to file one or more registration statements, as permissible and necessary to register under the Securities Act of 1933, registering the sale of the shares of our common stock that have been and may be issued to Aspire Capital under the purchase agreement. As part of the stock purchase agreement we issued 49,736 common shares as a commitment fee. The value of the common shares issued as a commitment fee of $198,523 has been reflected as an addition to common stock and additional paid in capital of $746 and $197,777, respectively, which is amortized over the life of the stock purchase agreement. As of the date of filing this Quarterly Report with the SEC no shares of stock have been sold to Aspire Capital under the May 25, 2016 purchase agreement. In connection with our public offering that closed on April 3, 2017, we agreed not to utilize the financing arrangement with Aspire Capital for 90 days after that financing and on June 30, 2017 in connection with the temporary modification of our common stock warrants to allow for the net exercise of those warrants we agreed to extend this stand still for an additional 45 days. As of September 30, 2017, 467,650 shares are available for sale to Aspire Capital under the May 25, 2016 purchase agreement.

2016 Public Offering of Common Stock

In August 2016, the Company completed an underwritten public offering of 1,150,000 shares of common stock at a price per share of $2.50, with gross proceeds of $2,875,000 to the Company, or net proceeds of $2,561,896 after deducting underwriter discounts, commissions, non-accountable expense allowance and expense reimbursement.

2017 Public Offering of Class A and Class B Units Consisting of Common Stock, Series A Convertible Preferred Stock and Warrants

On March 28, 2017, the Company entered into an underwriting agreement with Aegis Capital Corp. relating to a public offering which closed on April 3, 2017. The offering generated gross proceeds to the Company of approximately $4.4 million and net proceeds of approximately $3.9 million after deducting underwriting discounts and commissions and other offering expenses paid by the Company.

The offering included 664,000 Class A Units at a public offering price of $0.75 per Class A Unit, which consisted of 664,000 shares of common stock and warrants to purchase 664,000 shares of common stock. The offering also included 3,502 Class B Units at a public offering price of $1,000 per Class B Unit, which consisted of 3,502 shares of Series A convertible preferred stock convertible into a total of 4,669,329 shares of common stock and warrants to purchase 4,669,329 shares of common stock. In addition, the underwriter exercised the over-allotment to purchase an additional 530,000 shares of common stock and warrants to purchase 530,000 shares of common stock, which are included in the gross proceeds of $4.4 million. The warrants had a per share exercise price of $0.9375, were exercisable immediately and were scheduled to expire five years from the date of issuance.

As of September 30, 2017, all of the warrants issued in the April 3, 2017 offering have been exercised and are no longer outstanding and all of the shares of Series A convertible preferred stock have been converted into shares of common stock.

Accounting Treatment

The Company allocated the proceeds from the sale of the Class A and Class B units to the separate securities issued. The Company determined that, on the date of issuance, the warrants were not considered indexed to its own stock because the underlying instruments were not “fixed-for-fixed” due to the price protection and fundamental transaction provisions and, therefore, the warrants should be accounted for as liabilities. At the end of each reporting period, the changes in fair value of the warrants during the period are recorded in non-operating income (expense) in the consolidated statement of operations.

The Company allocated the amount representing the fair value of the warrants at the date of issuance separately to the warrant liability and recorded the remaining proceeds as common stock, in the case of the Class A units, or as Series A convertible preferred stock, in the case of the Class B units. Due to the allocation of a portion of the proceeds to the warrants, the Series A convertible preferred stock contained a beneficial conversion feature upon issuance, which was recorded in the amount of $1,284,066 based on the intrinsic value of the beneficial conversion feature. The discount on the Series A convertible preferred stock of $1,284,066 caused by allocation of the proceeds to the warrant was recorded as a deemed dividend upon issuance of the Series A convertible preferred stock. As a result, total deemed dividends of $2,568,132 was recorded upon issuance of the Series A convertible preferred stock, which is reflected as an addition to net loss in the consolidated statement of operations to arrive at net loss applicable to common shareholders.

Exercise of 2017 Warrants

On June 29, 2017, the Company offered to modify the rights of the holders of the warrants issued in the public offering the Company completed on April 3, 2017. The temporary modification included (a) lowering the exercise price of the warrants to $0.26 per share, (b) setting the applicable volume-weighted average price (VWAP) at $0.52 per share, and (c) allowing for temporary cashless exercise of the warrants for all holders that accepted the temporary modification before 8:00 a.m. Eastern daylight time on June 30, 2017. Holders of warrants to purchase a total of approximately 3.0 million shares of Common Stock accepted the offer resulting in the cancellation of those warrants and the issuance by the Company of a total of approximately 1.5 million shares of Common Stock (including shares held in abeyance). The shares of Common Stock are registered under the Securities Act of 1933, as amended. If delivery of the shares of Common Stock pursuant to the foregoing would result in the holder exceeding the 4.99% "Beneficial Ownership Limitation" (as defined in the warrant) then the shares in excess of such 4.99% will be held in abeyance by the Company pending further instruction from the holder. In connection with the temporary modification, the Company agreed to extend the "Lock-up Period" of the underwriting agreement between the Company and Aegis Capital Corp., dated March 28, 2017, by 45 days and the Company agreed not to enter into any further amendments to the warrants during such extended Lock-up Period without the prior written consent of each holder. During the three months ended September 30, 2017, all remaining warrants were exercised for cash so that no warrants issued in the April 3, 2017 financing remain outstanding. Upon exercise of these warrants, the amount of the warrant liability at the date of exercise was reclassified from warrant liability to additional paid-in capital.

The following table summarizes the 2017 liability warrant activity:

	Shares	**Weighted Average Exercise Price**
Outstanding as of December 31, 2016		
Warrants granted	5,863,332	$ 0.9375
Warrants exercised	(5,863,332)	0.26
Outstanding as of September 30, 2017		$

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The Company estimated the fair value of the warrants using the Monte Carlo simulation (MCS) model, which is a type of income approach, where the current value of an asset is expressed as the sum of probable future cash flows across various scenarios and time frames discounted for risk and time. The significant assumptions include timing of future rounds of financing, timing and success rates of oncology clinical trials, and the probability of a merger and acquisition adjusted for a lack of marketability discount. The MCS model also includes a full term and an early conversion scenario that are each weighted at 50% in the final concluded fair value.

Inputs used in the valuation of the warrants at the issuance date of April 3, 2017 and June 30, 2017 are set forth below. All remaining warrants were exercised during the quarter and no warrants issued in the April 2017 financing remain outstanding at September 30, 2017.

Initial valuation		
Common stock price	$0.75	
Exercise price	$0.9375	
Expected Volatility	50	%
Dividend Yield	0	%
Risk-Free Interest Rate	0.79% - 1.88	%
Expected Term (years)	0.24 - 5	
June 30, 2017 valuation		
Common stock price	$0.50	
Exercise price	$0.26	
Expected Volatility	50	%
Dividend Yield	0	%
Risk-Free Interest Rate	0.79-1.88	%
Expected Term (years)	0.08-4.76	

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Outstanding Warrants

As of September 30, 2017, warrants to purchase 380,561 shares of common stock were outstanding including:

	Outstanding Warrants to Purchase Shares	Exercise Price	Expiration Date
2011 private placement	283,470	$ 18.75 - 24.00	May 8, 2018
2014 public offering	77,790	45.00	January 29, 2019
Placement agent fees for Company's offerings	16,135	31.80 - 186.45	March - November, 2018
Outside consulting	3,166	63.60	January 14, 2018
	380,561		

Conversion of Series A Convertible Preferred Stock

During the three months ended September 30, 2017, certain holders of the Series A convertible preferred stock exercised their conversion option and converted an aggregate of 839 shares of Series A convertible preferred stock into 1,118,665 shares of the Company's common stock based on the conversion ratio of 1,333.33 shares of common stock for each share of Series A convertible preferred stock. During the nine months ended September 30, 2017, certain holders of the Series A convertible preferred stock exercised their conversion option and converted an aggregate of 3,502 shares of Series A convertible preferred stock into 4,669,329 shares of the Company's common stock. As of September 30, 2017, no shares of Series A convertible preferred stock are outstanding.

NOTE 9: FAIR VALUE OF FINANCIAL INSTRUMENTS

Pursuant to the accounting guidance for fair value measurement and its subsequent updates, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the "exit price") in an orderly transaction between market participants at the measurement date. The accounting guidance establishes a hierarchy for inputs used in measuring fair value that minimizes the use of unobservable inputs by requiring the use of observable market data when available. Observable inputs are inputs that market participants would use in pricing the asset or liability based on active market data. Unobservable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability based on the best information available in the circumstances.