

Alliqua BioMedical, Inc.  
Form 10-K  
March 02, 2018

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON D.C. 20549**

**FORM 10-K**

**(Mark One)**

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

**For the fiscal year ended: December 31, 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: **001-36278**

**Alliqua BioMedical, Inc.**

(Exact name of registrant as specified in its charter)

**Delaware** **58-2349413**  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

**1010 Stony Hill Road**  
**Yardley, PA**  
(Address of principal executive office) **19067**  
(Zip Code)

Registrant's telephone number, including area code: **(215) 702-8550**

Securities registered pursuant to Section 12(b) of the Exchange Act:

<u>Title of each class</u>	<u>Name of each exchange on which registered</u>
<b>Common Stock, \$0.001 par value</b>	<b>The NASDAQ Stock Market LLC</b>

Securities registered pursuant to Section 12(g) of the Exchange Act: **None**

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the 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 Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer      ☐ Accelerated filer      ☐

Non-accelerated filer      ☐ (Do not check if a smaller reporting company)

Smaller reporting company ☒ Emerging growth company      ☐

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 by Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

The aggregate market value of the voting and non-voting common equity of the registrant held by non-affiliates, computed by reference to the closing sales price of such stock, as of June 30, 2017 was \$13,713,853. (For purposes of determination of the aggregate market value, only directors, executive officers and 10% or greater shareholders have been deemed affiliates.

The number of shares outstanding of the registrant's common stock, par value \$0.001 per share, as of March 1, 2018 was 4,985,212 shares.

**ALLIQUA BIOMEDICAL, INC.**

**TABLE OF CONTENTS**

**PART I**

<u>ITEM 1. BUSINESS</u>	<u>3</u>
<u>ITEM 1A. RISK FACTORS</u>	<u>12</u>
<u>ITEM 1B. UNRESOLVED STAFF COMMENTS</u>	<u>27</u>
<u>ITEM 2. PROPERTIES</u>	<u>27</u>
<u>ITEM 3. LEGAL PROCEEDINGS</u>	<u>27</u>
<u>ITEM 4. MINE SAFETY DISCLOSURES</u>	<u>27</u>

**PART II**

<u>ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u>	<u>27</u>
<u>ITEM 6. SELECTED FINANCIAL DATA</u>	<u>28</u>
<u>ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	<u>28</u>
<u>ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	<u>37</u>
<u>ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>	<u>37</u>
<u>ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>	<u>37</u>
<u>ITEM 9A. CONTROLS AND PROCEDURES</u>	<u>37</u>
<u>OTHER INFORMATION</u>	<u>37</u>

ITEM  
9B.

**PART**  
**III**

<u>ITEM</u> <u>10.</u>	<u>DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE</u>	<u>37</u>
---------------------------	---	-----------

<u>ITEM</u> <u>11.</u>	<u>EXECUTIVE COMPENSATION</u>	<u>38</u>
---------------------------	-------------------------------	-----------

<u>ITEM</u> <u>12.</u>	<u>SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u>	<u>38</u>
---------------------------	---	-----------

<u>ITEM</u> <u>13.</u>	<u>CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE</u>	<u>38</u>
---------------------------	--	-----------

<u>ITEM</u> <u>14.</u>	<u>PRINCIPAL ACCOUNTING FEES AND SERVICES</u>	<u>38</u>
---------------------------	---	-----------

**PART**  
**IV**

<u>ITEM</u> <u>15.</u>	<u>EXHIBITS AND FINANCIAL STATEMENT SCHEDULES</u>	<u>38</u>
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## PART I

*Unless the context otherwise indicates, the terms “we,” “us” and “our” as used in this Annual Report on Form 10-K refer to Alliqua BioMedical, Inc. and its directly and indirectly owned subsidiaries on a consolidated basis.*

## ITEM 1. BUSINESS

## Forward-Looking Statements

This Annual Report on Form 10-K contains “forward-looking statements,” which include information relating to future events, future financial performance, strategies, expectations, competitive environment and regulation. Words such as “may,” “should,” “could,” “would,” “predict,” “potential,” “continue,” “expect,” “anticipate,” “future,” “intend,” “plan,” “believe” and similar expressions, as well as statements in future tense, identify forward-looking statements. Forward-looking statements should not be read as a guarantee of future performance or results and may not be accurate indications of when such performance or results will actually be achieved. Forward-looking statements are based on information we have when those statements are made or our good faith belief as of that time with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in or suggested by the forward-looking statements. Important factors that could cause such differences include, but are not limited to:

- inadequate capital;

the occurrence of any event, change or other circumstances that could cause a failure to consummate the Asset Sale Transaction (as defined below);

an increase in the amount of costs, fees, expenses and other charges related to the Asset Purchase Agreement or Asset Sale Transaction;

risks arising from the diversion of management's attention from our ongoing business operations;

- the uncertainty regarding the adequacy of our liquidity to pursue our complete business objectives;

- our ability to recover the carrying value of some or all of our intangible assets, including goodwill;
- our ability to obtain reimbursement from third party payers for our products;
- our ability to achieve and maintain minimum sales and other requirements under our license agreements;
- our ability to obtain and maintain regulatory approval of our existing products and any future products we may develop;
- our ability to cure or obtain forbearance or waivers for existing covenant defaults under our outstanding indebtedness and to remain in compliance with our debt covenants;
- market acceptance of our existing and future products;
- loss or retirement of our Chief Executive Officer;
- our plans to make significant additional outlays of working capital before we expect to generate significant revenues and the uncertainty regarding when we will begin to generate significant revenues, if we are able to do so;
- an unfavorable decision on product reimbursement;
- adverse economic conditions and/or intense competition;
- loss of a key customer or supplier;
- entry of new competitors and products;
- adverse federal, state and local government regulation;

- technological obsolescence of our products;
- technical problems with our research and products;
- risks of mergers and acquisitions including the time and cost of implementing transactions and the potential failure to achieve expected gains, revenue growth or expense savings;
- price increases for supplies and components;
- the inability to carry out research, development and commercialization plans; and

For a discussion of these and other risks that relate to our business and investing in shares of our common stock, you should carefully review the risks and uncertainties described under the heading “Part I – Item 1A. Risk Factors” and elsewhere in this Annual Report on Form 10-K. The forward-looking statements contained in this Annual Report on Form 10-K are expressly qualified in their entirety by this cautionary statement. We do not undertake any obligation to publicly update any forward-looking statement to reflect events or circumstances after the date on which any such statement is made or to reflect the occurrence of unanticipated events.

## **Our Company**

We are a regenerative technologies company that commercializes differentiated regenerative medical products which assist the body in the repair or replacement of soft tissue. Through our sales and distribution network, together with our proprietary products, we believe we offer solutions that allow clinicians to utilize the latest advances in regenerative technologies to bring improved patient outcomes to their practices. Our contract manufacturing business provides custom hydrogels to the OEM market.

On January 5, 2018, we entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Celularity, Inc. (“Celularity”) pursuant to which we agreed to sell substantially all of our assets to Celularity (the “Asset Sale Transaction”), including certain assets comprising our MIST, Biovance and Interfyl Product lines (the “Purchased Assets”). As consideration for the Purchased Assets, Celularity has agreed to pay us \$29 million in cash. No debt or significant liabilities will be assumed by Celularity in the Asset Sale Transaction.

Under the terms of the Asset Purchase Agreement, we will retain certain specified assets, including, among other things, cash, accounts receivable, and our hydrogel contract manufacturing business, including our SilverSeal and



Hydres product lines.

The transactions contemplated by the Asset Purchase Agreement must be approved by the affirmative vote of a majority of the voting power of issued and outstanding shares of our common stock. In addition to the receipt of our approval of our stockholders, each party's obligation to consummate the Asset Sale Transaction is conditioned upon certain other customary closing conditions. We expect the consummation of the Asset Sale Transaction to be no later than May 31, 2018.

In addition, in order to add capital and to focus on future investments on commercializing our own regenerative technologies, on August 31, 2017, we entered into an Asset Purchase Agreement ("the Argentum Purchase Agreement") with Argentum Medical, LLC. ("Argentum") whereby we agreed to sell to Argentum all of our rights, including (i) all distribution rights, exclusivity rights, intellectual property rights and marketing rights to the TheraBond product line and (ii) the unsold inventory of TheraBond products and work in process previously purchased by us in existence as of the closing, which occurred upon execution and delivery of the Argentum Purchase Agreement. In consideration for the sale of the TheraBond product line and the unsold TheraBond inventory to Argentum by us, Argentum agreed to pay (i) \$3.6 million for the TheraBond product line and certain other agreements between the parties and (ii) up to \$112,000 for the unsold TheraBond inventory upon our completion of our obligations to deliver all remaining and qualifying unsold TheraBond inventory, as specified in the Argentum Purchase Agreement. Of the \$3.6 million of consideration, \$300,000 is deposited in an indemnity escrow account under standard terms and conditions.

### ***Products and Services***

The disclosure in this section describes our commercial wound care portfolio as of December 31, 2017, including the assets we intend to sell under the Asset Purchase Agreement with Celularity.

Our commercial wound care portfolio currently consists of two product categories: wound bed preparation and human biologics. We currently market MIST® Ultrasound Healing Therapy ("MIST Therapy"), which uses painless, noncontact low-frequency ultrasound to promote healing, Biovance® Amniotic Membrane Allograft ("Biovance") and Interfyl® Human Connective Tissue Matrix ("Interfyl"), which are human biologic regenerative technologies. In addition, we maintain our legacy contract manufacturing business, which provides custom hydrogels to the OEM market.

### ***Wound Bed Preparation***

On May 29, 2015, we completed our acquisition of Celleration, Inc. (“Celleration”), a medical device company focused on developing and commercializing the MIST Therapy therapeutic ultrasound platform for the treatment of acute and chronic wounds. MIST Therapy is a painless, noncontact, low-frequency ultrasound delivered through a saline mist medium to the wound bed. The MIST Therapy system and UltraMIST® System (“UltraMIST”) consist of a portable countertop generator and handheld transducer. Attached to the transducer is a single-use disposable applicator, which includes an inlet for sterile saline. As the device is activated, the saline is introduced to the head of the transducer where it is atomized. This saline mist is the medium allowing the ultrasonic energy to be efficiently transmitted to the wounded area without direct contact of the device. The energy delivery via a fluid mist has been described as painless and often pain-relieving for the patient. The disposable applicator is designed for a single use only, to avoid any potential of contamination from patient to patient. Unlike most wound therapies that are limited to treating the wound surface, we have evidence that MIST Therapy sound wave energy promotes healing and reduces bacterial bioburden.

### ***Human Biologics***

In November 2013, we entered into a license, marketing and development agreement with Anthrogenesis Corporation d/b/a Celgene Cellular Therapeutics (“CCT”), an affiliate of Celgene Corporation, pursuant to which CCT granted us an exclusive, royalty-bearing license in its intellectual property related to certain placental based products for wound care and wound management, including those made from extracellular matrix (“ECM”) derived from the human placenta, and Biovance, a decellularized and dehydrated allograft produced from human amniotic membrane for the management of non-infected partial- and full-thickness wounds. On May 5, 2015, the license agreement was amended, pursuant to which we received the additional right to develop and market CCT’s connective tissue matrix product known as Interfyl, our latest regenerative technology. In February 2016, Human Longevity Inc. (“HLI”), a genomics-based, technology-driven company, acquired the assets of CCT related to ECM, Biovance and Interfyl, among other select assets. All of CCT’s rights and obligations under the license agreement were assigned to HLI in connection with this acquisition. In June 2017, Celularity, Inc. (“Celularity”) acquired some of the assets of HLI, including the agreements between HLI and the Company. The initial term of the license agreement ends on November 14, 2023, unless sooner terminated pursuant to the termination rights under the license agreement, and will extend for additional two-year terms unless either party gives written notice within a specified period prior to the end of a term. The license agreement is terminable on a product-by-product basis, and not with respect to the entire license agreement (i) by either Celularity or us, if we fail to meet certain sales thresholds or other conditions, and (ii) by either party upon written notice if outside legal counsel recommends discontinuance of commercialization of a product because of significant safety, legal, or economic risk as a result of a claim, demand or action or as a result of a change in the interpretation of law by a governmental or regulatory authority.

The license agreement permits us to commercialize Biovance and Interfyl in the United States. The development and application of the intellectual property covered under the license agreement is managed by a joint steering committee, composed of members of our company and Celularity. We pay Celularity annual license fees, designated amounts

when certain milestone events occur and royalties on all sales of licensed products, with such amounts being variable and contingent on various factors. On September 30, 2014, the license agreement was amended to give us the exclusive right to market Biovance for podiatric and orthopedic applications.

In connection with the Biovance products, on November 14, 2013, we also entered into a supply agreement with CCT, as subsequently amended on each of April 10, 2014 and September 30, 2014, pursuant to which CCT agreed to supply us with our entire requirement of Biovance for distribution and sale in the United States. On April 10, 2014, we and CCT entered into a supply agreement for ECM, on substantially the same terms as the supply agreement for Biovance. On April 23, 2014, we initiated our sales and marketing efforts for Biovance at the Spring 2014 Symposium on Advanced Wound Care and had our first commercial sale on May 1, 2014. In February 2016, HLI assumed all of CCT's rights and obligations under the supply agreement in connection with the acquisition and the assignment of the license agreement. In June 2017, Celularity acquired this agreement from HLI and assumed all of HLI's rights and obligations thereunder.

In connection with the Interfyl products, on April 15, 2016, we entered into a supply agreement with HLI, pursuant to which HLI agreed to supply us with our entire requirements of Interfyl for distribution and sale in the United States. In September 2016, we announced the commercial introduction of Interfyl in the United States and had our first commercial sale. In June 2017, Celularity acquired this agreement from HLI and assumed all of HLI's rights and obligations thereunder. We offer Interfyl in both particulate and flowable forms. In these forms, Interfyl can be used to fill voids and correct defects in soft tissue, providing mechanical and structural support to facilitate the tissue repair process or replace missing or inadequate soft tissue.

On December 1, 2017, we received notice from Celularity that we are in material breach of our License, Marketing and Development Agreement with Celularity (or its affiliates) dated as of November 14, 2013, as amended from time to time (the "License Agreement") and our Supply Agreements with Celularity (or its affiliates), dated as of April 15, 2016 and November 14, 2013, respectively, as amended from time to time (the "Supply Agreements") for failure to purchase the required amounts of materials under the Supply Agreements and failure to use commercially reasonable best efforts to undertake development activities for the licensed products under the License Agreement (the "Notices"). Celularity estimated that an additional purchase of at least \$842,000 would have to be made by us to remedy the breach under the Supply Agreements. Celularity has agreed to forbear from exercising its right to terminate the Supply Agreements and License Agreements until the closing of the Asset Sale Transaction or termination of the Asset Purchase Agreement for any reason. We believe that Celularity's notice of material breach of the License Agreement is without merit.

Biovance and Interfyl are derived from the placenta of healthy, full-term pregnancies. Both Biovance and Interfyl are regulated by the U.S. Food and Drug Administration (“FDA”) under Section 361 of the Public Health Service Act (“PHS Act”) as a 361 HCT/P, or human tissue product. Human tissues contain collagen, fibronectin, and other proteins and biochemicals that support healing. These important components are maintained in their native architecture throughout Celularity’s processing. However, essentially no cells are contained in the finished products (Biovance and Interfyl are decellularized), which is different from other placenta-based products, and this decellularization together with the gentle minimal manipulation of the tissues contribute to minimization of irritation and inflammation related to immune responses that can interfere with healing. When the scaffold or extracellular matrix of Biovance and Interfyl is placed in a wound or an area with damaged or deficient soft tissue, it can serve as a platform that allows the body’s own cells to migrate into the matrix and attach. Once attached, the cells release growth factors to signal other activities to progress healing.

Biovance is intended for use as a biological membrane covering that provides extracellular matrix while supporting the repair of damaged tissue. As a barrier membrane, Biovance is intended to protect the underlying tissue and preserve tissue plane boundaries with minimized adhesion or fibrotic scarring. Indications include, but are not limited to, surgical covering, wrap or barrier, application to partial- and full-thickness, acute and chronic wounds (such as, traumatic and complex wounds, burns, surgical and Mohs surgery sites; and diabetic, venous, arterial, pressure and other ulcers), including wounds with exposed tendon, muscle, bone or other vital structures.

We believe Interfyl treats deep wounds or soft tissue voids for which a sheet format such as Biovance is not as well suited. Interfyl is indicated for the replacement or supplementation of damaged or inadequate integumental soft tissue. There are podiatric and orthopedic applications, as well as wound management opportunities for homologous use of Interfyl.

Interfyl is intended for use as the replacement or supplementation of damaged or inadequate integumental tissue. Indications include, but are not limited to, treatment of soft tissue voids, correction of soft tissue defects, soft tissue augmentation during repair of dehiscent or complicated surgical closures and repair of small surgical defects resulting from either medical or surgical conditions including those with exposed vital structures (bone, tendon, ligament, or nerve). Interfyl is also intended for use as the replacement or supplementation of damaged or inadequate integumental tissue. Indications include, but are not limited to: augmentation of deficient/inadequate soft tissue and treatment of deep dermal wounds; surgical wounds; soft tissue voids as a result of tunneling wounds, fistula tracts, or dermal undermining—including those with exposed vital structures (bone, tendon, ligament, or nerve).

Any further development and commercialization of ECM is not planned by us at this time.

#### ***Contract Manufacturing***

In connection with our legacy contract manufacturing business; we develop, manufacture and market high water content, electron beam cross-linked, aqueous polymer hydrogels, or gels, used for wound care, medical diagnostics, transdermal drug delivery and cosmetics. We specialize in custom gels by capitalizing on proprietary manufacturing technologies. Our products are manufactured using proprietary and non-proprietary mixing, coating and cross-linking technologies. Together, these technologies enable us to produce gels that can satisfy rigid tolerance specifications with respect to a wide range of physical characteristics (e.g., thickness, water content, adherence, absorption, moisture vapor transmission rate (a measure of the passage of water vapor through a substance) and release rate) while maintaining product integrity. Additionally, we have the manufacturing ability to offer broad choices in the selection of liners onto which the gels are coated. Consequently, our customers are able to determine tolerances in moisture vapor transmission rate and active ingredient release rates while personalizing color and texture.

### ***Planned Future Operations***

If we consummate the Asset Sale Transaction, we, and not our stockholders, will receive the proceeds from the Asset Sale Transaction. We do not intend to liquidate following the Asset Sale Transaction. Our Board will evaluate alternatives for the use of the cash proceeds to be received at closing, which alternatives are expected to include using a portion of the proceeds to repay our outstanding indebtedness (including prepayment fees) to Perceptive Credit Opportunities Fund, L.P. (“Perceptive”) of approximately \$12.6 million in full and to pay transaction and other expenses of approximately \$3 million. In addition, we intend to continue to maximize stockholder interests with a goal of returning value to our stockholders. Although our Board has not made any determination, such alternatives may include paying a special dividend, a share repurchase or other return of capital to our stockholders. We intend to use the remainder of the proceeds, together with any other sources of liquidity available to us at that time, to support operations at our contract manufacturing plant and to pursue strategic opportunities including, without limitation, a reverse merger transaction or a strategic acquisition. The amounts and timing of our actual expenditures, however, will depend upon numerous factors, and we may find it necessary or advisable to use portions of the proceeds from the Asset Sale Transaction for different or presently non-contemplated purposes.

If we do not receive stockholder approval, the Asset Sale Transaction will not occur. Instead, we will retain the assets and liabilities proposed to be sold in the Asset Sale Transaction and will not receive the \$29 million cash consideration from Celularity. We are currently in default of a covenant pertaining to trailing twelve-month revenue under the Credit Agreement as a result of our failure to achieve \$24,600,000, \$27,200,000, \$30,300,000, \$33,800,000 and \$37,800,000 of gross revenue for the twelve-month periods ended December 31, 2016, March 31, 2017, June 30, 2017, September 30, 2017 and December 31, 2017, respectively. The Company is also currently in default of a minimum cash balance requirement under the Credit Agreement due to the Company having a cash balance of less than \$2,000,000. As of the date hereof, the lender has agreed to forbear from exercising any rights and remedies related to each such event of default. In addition, on December 1, 2017, we received the Notices from Celularity.

Without receipt of the cash consideration from Celularity, we will not be able to repay our indebtedness under the Credit Agreement and will be unable to purchase materials under the Supply Agreements. The lender under the Credit Agreement may pursue the rights and remedies available to it under the Credit Agreement including, but not limited to, declaring all or any portion of the outstanding principal amount to be immediately due and payable, imposing a default rate of interest as specified in the Credit Agreement, or pursuing the lender's rights and remedies as a secured party under the UCC as a secured lender. In addition, the lender has a lien on substantially all of our assets and, as a result of the default, may seek to foreclose on some or substantially all of our assets. If we do not consummate the Asset Sale Transaction with Celularity and transfer the License Agreement and Supply Agreements to Celularity as part of the Purchased Assets, we may face termination or litigation with respect to the Supply Agreements and the License Agreement. If we were to lose our rights to license Biovance, Interfyl or other products from Celularity under the License Agreement, it will have a material adverse effect on our business, financial condition and results of operations which could force the Company to file for bankruptcy.

Subject to the risks mentioned above, if the Asset Sale Transaction does not close we will explore other strategic options including sale of some or all of the assets proposed to be sold in the Asset Sale Transaction. In addition, we may seek merger or licensing opportunities to bring additional assets into our product portfolio.

### ***Industry and Markets***

According to medical market research firm BioMedGPS, LLC SmartTRAK™ data, the U.S. market for wound care management products, which had revenues of approximately \$5.9 billion in 2015, is expected to grow to \$7.4 billion by 2019, which is a compound annual growth rate of 5% for 2015 to 2019. Growth in the U.S. wound care market will likely come from new therapies that result in decreasing healing times and subsequent cost savings and a growing focus on special populations such as diabetics and the obese.

We have targeted four specific market segments within the wound care industry:

**Lower Extremity.** According to SmartTRAK there will be an estimated 14 million orthopedic procedures in the U.S. in 2018, a number which is growing at 5% per year, representing a \$146 million market growing at 21% per year (estimates for 2018 from SmartTRAK). We have focused the sales and marketing of our biologics products on lower extremity and primarily foot and ankle procedures, which are a sub-segment of the orthopedic procedures market, and we estimate that there are currently approximately 2.5 million estimated foot and ankle procedures on an annual basis.. However, while we have chosen to focus on a specific segment of the wound care industry, we believe our biologics products are suitable for all types of wounds because of their HCTP-361 designation, and, as such, have applications across all wound types.

**Diabetic Ulcers.** According to the National Diabetes Clearinghouse (“National Diabetes Fact Sheet, 2014” available at [www.cdc.gov](http://www.cdc.gov)), there are over 29 million diabetics in the U.S., or more than 9.3% of the U.S. population. Almost 11.2 million people over the age of 65 are diabetic, which equates to almost 26% of all people in this age group. Furthermore, more than 60% of nontraumatic lower-limb amputations occur in people with diabetes. A study published by Wild, et. al. (*Diabetes Care*, May 2004) estimates that the worldwide number of diabetics is projected to be 366 million people by the year 2030. Boulton, et. al. (“Neuropathic Diabetic Foot Ulcers,” *New England Journal of Medicine*, July 2004) reported that diabetic foot ulcers (DFUs) develop in approximately 15% of patients with diabetes and precede 84% of all diabetes-related lower leg amputations. We believe that our wound care products can aid in the healing of these diabetic foot ulcers, thereby lessening the need for amputation.

**Pressure Ulcers.** Dorner, et. al. (“The Role of Nutrition in Pressure Ulcer Prevention and Treatment,” *The National Pressure Ulcer Advisory Panel*, 2009) stated that according to The Joint Commission, more than 2.5 million patients in U.S. acute-care facilities suffer from pressure ulcers. Dorner, et. al. also stated that the prevalence of pressure ulcers in the U.S. is widespread in all settings, with estimates of 10% to 18% in acute care and 2.3% to 28% in long-term care. The study further noted that these pressure ulcers can reduce overall quality of life and may also contribute to premature mortality in some patients, therefore any intervention that may help to prevent or treat them once they occur is important to reduce the cost of pressure ulcer care and improve the quality of life for affected individuals. Park-Lee, et. al. (“Pressure Ulcers Among Nursing Home Residents: United States, 2004,” *The National Center for Health Statistics Data Brief*, No. 14, February 2009) reported that 35% of nursing home residents with stage 2 or higher pressure ulcers received special wound care by specially trained professionals. We believe that our wound care products can aid in the treatment of pressure sores and ulcers, thereby increasing quality of life and decreasing the amount of time spent in wound care facilities.

**Venous Stasis Ulcers.** These wounds are believed to occur due to improper functioning of venous valves, usually of the legs. According to the University of Washington Medical Center (available at [www.uwmedicine.org/health-library/Pages/venous-stasis-ulcers.aspx](http://www.uwmedicine.org/health-library/Pages/venous-stasis-ulcers.aspx)), the main risk of venous stasis ulcers is the spread of infection from a persistent wound. Failure to address the condition appropriately could ultimately result in limb loss. As these ulcers are typically small, they are often undertreated, which leads to larger ulcers which require more complex treatments. Brem, et. al. ("Protocol for the Successful Treatment of Venous Ulcers," *American Journal of Surgery*, July 2004) reported in one study that up to 48% of venous ulcers had recurred by the fifth year after healing. These often chronic ulcers affect up to 2.5 million U.S. citizens annually. We believe that our wound care products can aid in the treatment of venous stasis ulcers and increase the quality of life for those affected.

### ***Sales and Marketing***

We continue to focus on sales and marketing efforts in the United States. As of December 31, 2017, we had 34 employees dedicated to sales, all of whom have experience in the wound care industry. Additionally, we have developed an independent network of agents to sell our wound care products through our extensive channel reach through a network of distributors. In addition, we have assembled a Medical/Surgical Advisory Board to help us target improvements and new applications for our products and assist in our marketing efforts. We also market our advanced wound care products at conferences, trade shows and other educational events.

### ***Customers***

During the year ended December 31, 2017, one customer accounted for 67% of our contract manufacturing revenue and 6% of our total net revenue from continuing operations. We are uncertain as to this customer's intentions to use our services during the fiscal year ending December 31, 2018.

### ***Competition***

Leading competitors in the tissue-based wound care area that will compete with our biologic products, Biovance and Interfyl include companies such as MiMedx Group, Inc., Osiris Therapeutics, Inc., Organogenesis Inc., Integra LifeSciences Corporation, as well as a significant number of smaller companies.

We believe that MIST Therapy has no direct competition in the advanced wound care market. As a result, we believe that MIST Therapy may compete favorably on the basis of broad application. Notwithstanding the lack of direct competition, we expect many physicians and allied professionals to continue to employ other treatment approaches



and technologies to treat chronic and hard-to-heal wounds.

Our ability to establish sales in a market with many larger manufacturers may be difficult. We continue to recruit veterans of the medical device industry to leverage our product offerings into the most beneficial distribution channels. Our competitors may still have greater resources to support their products and may not allow us to take any market share from them.

***Sources and Availability of Raw Materials; Principal Suppliers***

In general, raw materials essential to our businesses are readily available from multiple sources. For reasons of quality assurance, availability, or cost effectiveness, certain components and raw materials are available only from a sole supplier. Our policy is to maintain sufficient inventory of components so that our production will not be significantly disrupted even if a particular component or material is not available for a period of time.

We purchase MIST Therapy applicators and the saline bottles included with each applicator from single sources. We purchase the MIST systems from one supplier. We and our suppliers purchase many of the components and raw materials in manufacturing the MIST products from numerous suppliers in various countries. We have been able to obtain adequate supplies of such raw materials and components and work closely with suppliers to try to ensure continuity of supply while maintaining high quality and reliability.

Under our Supply Agreements we receive the finished goods of Biovance and Interfyl from Celularity.

On December 1, 2017, we received notice from Celularity that we are in material breach of our supply agreements with Celularity, for failure to purchase the required amounts of materials under the Supply Agreement. Celularity estimated that an additional purchase of at least \$842,000 would have to be made by us to remedy this breach. Celularity has agreed to forbear from exercising its right to terminate the supply agreement until the closing of the Asset Sale Transaction or termination of the Asset Purchase Agreement for any reason.

See “Item 1A. Risk Factors - “We cannot be sure if or when the Asset Sale Transaction will be completed.”

Because we have no direct control over these suppliers, interruptions or delays in the products and services provided by these parties may be difficult to remedy in a timely fashion. In addition, if such suppliers are unable or unwilling to deliver the necessary products or raw materials, we may be unable to redesign or adapt our technology to work without such raw materials or products or find alternative suppliers or manufacturers. In such events, we could experience interruptions, delays, increased costs or quality control problems, or be unable to sell the applicable

products, all of which could have a significant adverse impact on our revenue.

Other than as discussed above, we believe that, due to the size and scale of production of our suppliers, there should be adequate supply of raw materials from our manufacturers.

### ***Patents, Proprietary Rights and Trademarks***

We own or license trademarks covering our company and our products. Our policy is to file patent applications to protect technology, inventions and improvements that are important to the development of our business. We also rely upon trade secrets and continuing technological innovations to develop and maintain our competitive position.

As of December 31, 2017, we have beneficial ownership of 15 issued U.S. utility patents, 2 issued U.S. design patents, 17 foreign patents, and several pending U.S. and foreign patent applications covering aspects of our MIST Therapy platform. Specifically, the MIST Therapy patent rights cover both medical and device aspects of wound care using non-contact ultrasound, as well as other clinical ultrasound applications.

In November 2013, we entered into a license, marketing and development agreement with CCT, as subsequently amended on each of September 30, 2014 and May 6, 2015, pursuant to which we hold an exclusive, royalty-bearing license in CCT's intellectual property related to certain placental based products, including DRS(ECM), Interfyl and Biovance, to develop and commercialize these products in the United States. In January 2016, HLI assumed all of CCT's rights and obligations under the license agreement in connection with HLI's acquisition of the assets of CCT related to DRS and Biovance, among other select assets. In June 2017, Celularity, Inc. ("Celularity") acquired some of the assets of HLI, including the agreements between HLI and the Company. The development and application of the intellectual property covered under the license agreement is managed by a joint steering committee, composed of members of us and Celularity. Following the commencement of commercial sales of each licensed product, the license agreement requires us to pay Celularity certain annual license fees, royalty payments based on a percentage of net sales, as well as financial and performance milestone payments, subject to the terms and conditions set forth in the license agreement. The initial term of the license agreement expires on November 14, 2023, unless sooner terminated pursuant to the termination rights under the license agreement, and will automatically renew for additional two-year periods unless either party gives written notice within a specified period prior to the end of a term. The license agreement may be terminated (i) by Celularity if we or any of our affiliates challenges the validity, enforceability or scope of certain enumerated Celularity patents anywhere in the world; (ii) by either party if there is a final decree that a licensed product infringed on the intellectual property of a third party and the parties cannot cure such third party infringement; (iii) by either party for breach and failure to cure such breach of the license agreement; or (iv) by either party if the other party is the subject of insolvency proceedings, either voluntary or involuntary. In addition, the license agreement is terminable on a product-by-product basis, and not with respect to the entire license agreement: (i) by Celularity, if we fail to meet certain minimum sales thresholds for the second year of commercial sales, and by either Celularity or us if we fail to meet certain minimum sales thresholds for the third or any subsequent year of commercial sales and (ii) by either party upon written notice if outside legal counsel recommends discontinuance of commercialization of a product because of an actual, threatened, or perceived significant safety, legal, or economic risk as a result of a claim, demand or action or as a result of a change in the interpretation of law by a governmental or

regulatory authority. Each year of commercial sales are referred to in the license agreement as “launch years” and the calendar period constituting each launch year for each licensed product is determined in accordance with the terms of the license agreement. See “Item 1A. Risk Factors - If we fail to meet certain minimum sales thresholds for products licensed pursuant to our agreement with Celularity, we could lose our right to license such products.”

On December 1, 2017, we received notice from Celularity that we are in material breach of the License Agreement for failure to use commercially reasonable best efforts to undertake development activities for the licensed products under the License Agreement. Celularity has agreed to forbear from exercising its right to terminate the License Agreement until the closing of the Asset Sale Transaction or termination of the Asset Purchase Agreement for any reason. We believe that Celularity’s notice of material breach of the License Agreement is without merit.

See “Item 1A. Risk Factors - “We cannot be sure if or when the Asset Sale Transaction will be completed.”

### ***Government Regulation***

*Product Regulation.* Under the Federal Food, Drug and Cosmetic Act, medical devices are classified by the FDA into one of three classes—Class I, Class II or Class III—depending on the degree of risk associated with each medical device and the extent of control needed to ensure safety and effectiveness. While some applications of hydrogels fall under the jurisdiction of the FDA, hydrogels are generally classified as Class I exempt devices and the majority of the hydrogel products that we manufacture are thereby exempt from the FDA filing of any regulatory submissions and/or pre-market notification requirements. To the extent that any FDA regulatory submissions are required, we will be required to file these submissions and maintain all appropriate documentation. With respect to registering the manufacturing facility with the FDA under the Code of Federal Regulations, 21 CFR 820.1, Scope: Part A, it is stated that the regulation does not apply to manufacturers of component parts of finished devices. Currently, hydrogels are sold as component parts to various medical device/cosmetic manufacturers.

We believe that a number of products that our partners are developing will be classified in the U.S. as either Class I or Class II medical devices or Human Cells, Tissues, and Cellular and Tissue-Based Products (HCT/Ps). Class I medical devices are subject to the FDA's general controls, which include compliance with the applicable portions of the FDA's Quality System Regulation, facility registration and product listing, reporting of adverse medical events, and appropriate, truthful and non-misleading labeling, advertising, and promotional materials. Class II devices are subject to the FDA's general controls and may also be subject to other special controls as deemed necessary by the FDA to ensure the safety and effectiveness of the device. Most Class II devices require pre-market clearance by the FDA through the 510(k) pre-market notification process. When a 510(k) is required, the manufacturer must submit to the FDA a pre-market notification demonstrating that the device is "substantially equivalent" to either a device that was legally marketed prior to May 28, 1976, the date upon which the Medical Device Amendments of 1976 were enacted, or to another commercially available, similar device which was subsequently cleared through the 510(k) process. By regulation, the FDA is required to clear a 510(k) within 90 days of submission of the application. As a practical matter, clearance often takes longer. HCT/Ps that are regulated under 21 Code of Federal Regulations Part 1271 and Section 361 of the Public Health Service Act ("361 HCT/Ps") and do not require FDA approval or clearance prior to marketing. We are required to follow Current Good Tissue Practices (CGTP) including registration as a storage/distribution facility as well as track the tissue products from receipt to final disposition.

Biovance and Interfyl are products derived from human tissue. The FDA has specific regulations governing HCT/Ps. An HCT/P is a product containing or consisting of human cells or tissue intended for transplantation into humans. HCT/Ps that meet the criteria for regulation solely under Section 361 of the Public Health Service Act and 21 CFR 1271 (361 HCT/Ps) are not subject to pre-market clearance or approval requirements, but are subject to post-market regulatory requirements. To be a 361 HCT/P, a product must meet all four of the following criteria:

- It must be minimally manipulated;
- It must be intended for homologous use;
- It must not be combined with another article; and
- It must not have a systemic effect and not be dependent upon the metabolic activity of living cells for its primary function.

We and Celularity believe that, within their intended uses, Biovance and Interfyl qualify as 361 HCT/Ps. The FDA is in the process of clarifying definitions of homologous use and minimal manipulation in their Guidance for Industry publications.

The FDA has broad post-market regulatory and enforcement powers with respect to medical devices, similar to those for pharmaceutical products. Failure to comply with the applicable U.S. medical device regulatory requirements could result in, among other things, warning letters, fines, injunctions, consent decrees, civil penalties, repairs, replacements, refunds, recalls or seizures of products, total or partial suspension of production, the FDA's refusal to grant future pre-market clearances or approvals, withdrawals or suspensions of current product applications, and criminal prosecution. Similarly, the FDA may audit any manufacturer of medical devices or facilities with a registered 361 HCT/P.

If there are any modifications to a cleared medical device such as our UltraMIST Class II device identified in 510(k) K140782, including changes in indication, manufacturing process or labeling or a change in a manufacturing facility, an applicant must notify the FDA, and in many cases, clearance for such changes must be submitted to the FDA. Additionally, the FDA regulates post-approval promotional labeling and advertising activities to assure that such activities are being conducted in conformity with statutory and regulatory requirements. These regulations include standards or restrictions for direct-to-consumer advertising, industry-sponsored scientific and educational activities, promotional activities and off-label promotion. Likewise, labeling and advertising of HCT/Ps may be monitored for indication language to be consistent with homologous use. While physicians may prescribe for off-label uses, manufacturers may only promote for the approved indications and in accordance with the provisions of the approved label (or homologous use). The FDA has very broad enforcement authority under the Federal Food, Drug and Cosmetic Act, and failure to abide by these regulations can result in enforcement action, including the issuance of untitled or warning letters directing entities to correct deviations from FDA regulations and civil and criminal investigations and prosecutions. These activities could have a material adverse effect on our business, results of operations, financial condition and cash flows.

*Quality Assurance Requirements.* The FDA enforces regulations to ensure that the methods used in, and the facilities and controls used for, the manufacture, processing, packing and holding of drugs, medical devices and/or HCT/Ps conform with current good manufacturing (CGMP) and/or CGTP. The CGMP regulations the FDA enforces are comprehensive and cover all aspects of manufacturing operations, from receipt of raw materials to finished product distribution, insofar as they bear upon whether drugs meet all the identity, strength, quality and purity characteristics required of them. The CGMP regulations for devices, called the Quality System Regulation, are also comprehensive and cover all aspects of device manufacture, from pre-production design validation to installation and servicing, insofar as they bear upon the safe and effective use of the device and whether the device otherwise meets the requirements of the Federal Food, Drug and Cosmetic Act. CGTPs are narrower in scope than CGMPs. CGTP requires a quality program to prevent, detect, and correct deficiencies that could increase communicable disease risk. To assure compliance requires a continuous commitment of time, money and effort in all operational areas.

The FDA also conducts periodic inspections of drug, device and registered HCT/P facilities to assess their current CGMP/CGTP status. If the FDA were to find serious non-compliant manufacturing or processing practices during such an inspection, it could take regulatory actions that could adversely affect our business, results of operations, financial condition and cash flows. With respect to domestic establishments, the FDA could initiate product seizures or in some instances require product recalls and seek to enjoin a product's manufacture and distribution. In certain circumstances, violations could support civil penalties and criminal prosecutions. In addition, if the FDA concludes that a company is not in compliance with CGMP requirements, sanctions may be imposed that include preventing that company from receiving the necessary licenses to export its products and classifying that company as an "unacceptable supplier", thereby disqualifying that company from selling products to federal agencies.

We conduct audits of our outside manufacturers and believe that we and our suppliers and outside manufacturers are currently in compliance with CGMP/CGTP requirements. We are currently registered as a device manufacturer and human tissue distributor with the FDA and we intend to register as a drug facility with the FDA when we are required to do so.

### ***Third-Party Reimbursement***

In the United States as well as in foreign countries, sales of our products depend, in significant part, on the availability of reimbursement from third-party payers. In the U.S., third-party payers consist of government programs such as Medicare, private health insurance plans, managed care organizations and other similar programs. For any product, three factors are critical to reimbursement:

- coding, which ensures uniform description of procedures, diagnoses and medical products;
- coverage, which is the payer's policy describing the clinical circumstances under which it will pay for a given treatment; and
- payment process and fee schedules.

We believe the availability, as of January 2014, of a Category I CPT code for MIST Therapy has encouraged and will continue to encourage, broader coverage and subsequent use of its MIST Therapy System in the United States. Previously, MIST Therapy was billed under a temporary Category III CPT code, which some payers generally refuse to cover. Each government and private payer, however, makes its own coverage decision.

Access to MIST Therapy is available to Medicare beneficiaries in all 50 states. Although private payers will often pay for MIST Therapy when medically necessary and pre-approved, we have not focused on securing private payer coverage decisions for MIST Therapy.

For Medicare-covered patients who are commonly treated in a hospital outpatient department, the payment system is called the Outpatient Prospective Payment System. The facility payment for MIST Therapy is billed under the CPT Code and then categorized for payment under a single Ambulatory payment (“APC”). Each hospital has a specific APC payment based on the hospital’s wage index for their geographic location.

If MIST Therapy is delivered by a physician, non-physician practitioner, or physical therapist, a professional payment may be based on the Medicare Physician Fee Schedule (“MPFS”). The MPFS includes both a facility, and, for treatment delivered in a physician’s office a non-facility rate. The actual amount will vary by location per the geographic practice cost index adjustment to the national rate. Therapy services are typically paid under the non-facility MPFS payment rate pursuant to Medicare guidelines.

Biovance is currently marketed in hospitals where Diagnosis Related Group Procedures are performed, in the Veteran’s Affairs health system, and in hospital outpatient departments as well as Physician offices or other outpatient care centers. Providers of outpatient services will be reimbursed for Biovance by Medicare where there is a local coverage determination by the prevailing Medicare Administrative Contractor (“MAC”). On October 31, 2014, Biovance was assigned a new and unique, Level II Healthcare Common Procedure Coding System product reimbursement Q code (Q4154) by Centers for Medicare and Medicaid Services (“CMS”). The new reimbursement code took effect on January 1, 2015. We currently have reimbursement coverage for Biovance from all eight MACs, as well as 61% of BlueCross BlueShield covered lives in the U.S.

We have the Healthcare Common Procedural Coding System, or HCPCS, codes, from the Pricing, Data, Analysis, and Coding contractor for CMS, for use when billing for our wound care dressings. HCPCS was established in 1978 to provide a standardized coding system for describing the specific items and services provided in the delivery of health care. HCPCS codes are used by Medicare and monitored by the CMS. They are based on the Current Procedural Technology codes developed by the American Medical Association. We believe that these codes will facilitate reimbursement for the use of our dressings in Medicare patients with applicable wounds.

*Environmental Regulation.* We are subject to various laws and governmental regulations concerning environmental matters and employee safety and health in the U.S. and other countries. We have made, and continue to make, significant investments to comply with these laws and regulations. We cannot predict the future capital expenditures or operating costs required to comply with environmental laws and regulations. We believe that we are currently compliant with applicable environmental, health and safety requirements in all material respects. However, we cannot assure you that current or future regulatory, governmental, or private action will not have a material adverse effect on our performance, results or financial condition.





In the future, if a loss contingency related to environmental matters, employee safety, health or conditional asset retirement obligations is recognized, we would record a liability for the obligation and it may result in a material impact on net income for the annual or interim period during which the liability is recorded. The investigation and remediation of environmental obligations generally occur over an extended period of time, and therefore we do not know if these events would have a material adverse effect on our financial condition, liquidity, or cash flow, nor can we assure you that such liabilities would not have a material adverse effect on our performance, results or financial condition.

*Federal and State Anti-kickback, Self-referral, False Claims and Similar Laws.* Our relationships with physicians, hospitals and the marketers of our products are subject to scrutiny under various federal anti-kickback, self-referral, false claims and similar laws, often referred to collectively as healthcare fraud and abuse laws. Healthcare fraud and abuse laws are complex, and even minor, inadvertent violations can give rise to claims that the relevant law has been violated. Certain states have similar fraud and abuse laws, imposing substantial penalties for violations. Any government investigation or a finding of a violation of these laws would likely result in a material adverse effect on the market price of our common stock, as well as our business, financial condition and results of operations. We believe that we are currently compliant with applicable anti-kickback, self-referral, false claims in all material respects.

### ***Research and Development Costs***

For the years ended December 31, 2017 and 2016, we incurred research and development costs of approximately \$121,000 and \$859,000, respectively, related to a randomized controlled trial for our Biovance product in chronic diabetic foot ulcers. We experienced slower than expected patient enrollment and projected costs to complete the trial were significantly higher than we had previously expected. In addition, we believed there was no longer a business need for this trial due to the amount of patient data currently available, our success in getting government and commercial insurance coverage for Biovance, and our recent increase in Biovance sales. Due to these factors, we decided to terminate patient enrollment for the Biovance trial. We completed our study during the first half of 2017.

We bear our own research and development costs and do not directly pass along our research and development costs to our customers.

We intend to commit capital resources to research and development only as our cash resources allow. We have incurred all costs associated with the launch of our proprietary products and will only require research and development expenses for product enhancements and modifications and to obtain additional reimbursement coverage, which we do not expect to be significant.

***Employees***

As of December 31, 2017, we had 60 full-time employees. Of these employees, 46 are involved with finance, sales, marketing, and administration and 14 are involved with manufacturing, clinical and regulatory matters. Our employees are not represented by a labor union or other collective bargaining groups, and we consider relations with our employees to be good. We currently plan to retain and utilize the services of outside consultants for additional research, testing, regulatory, legal compliance and other services on an as needed basis.

**ITEM 1A. RISK FACTORS**

*There are numerous and varied risks, known and unknown, that may prevent us from achieving our goals. You should carefully consider the risks described below and the other information included in this Annual Report on Form 10-K, including the consolidated financial statements and related notes. If any of the following risks, or any other risks not described below, actually occur, it is likely that our business, financial condition, and/or operating results could be materially adversely affected. The risks and uncertainties described below include forward-looking statements and our actual results may differ from those discussed in these forward-looking statements.*

**Risks Related to the Asset Sale Transaction with Celularity.**

*The announcement and pendency of the Asset Sale Transaction, whether or not consummated, may adversely affect our business.*

The announcement and pendency of the Asset Sale Transaction, whether or not consummated, may adversely affect the trading price of our common stock, our business or our relationships with customers, suppliers and employees. In addition, pending the completion of the Asset Sale Transaction, we may be unable to attract and retain key personnel and the focus and attention of our management and employee resources may be diverted from operational matters during the pendency of the Asset Sale Transaction.

***We cannot be sure if or when the Asset Sale Transaction will be completed.***

The closing of the Asset Sale Transaction is subject to the satisfaction or waiver of various conditions, including the Stockholder Approval. We cannot guarantee that the closing conditions set forth in the Asset Purchase Agreement will be satisfied. If we are unable to satisfy the closing conditions in Celularity's favor or if other mutual closing conditions are not satisfied, Celularity will not be obligated to complete the Asset Sale Transaction. In the event that the Asset Sale Transaction is not completed, the announcement of the termination of the Asset Purchase Agreement may adversely affect the trading price of our common stock, our business and operations or our relationships with customers, suppliers and employees. In addition, (i) we will not be able to repay our debt to the lender under the Credit Agreement, and the lender may choose to pursue any rights and remedies available to it, including, but not limited to, declaring all or any portion of the outstanding principal amount to be immediately due and payable, imposing a default rate of interest as specified in the Credit Agreement, pursuing the lender's rights and remedies as a secured party under the UCC as a secured lender, or seeking to foreclose on some or substantially all of our assets pursuant to the lender's lien held on such assets and (ii) we may face termination of, or litigation with respect to, the License Agreement and the Supply Agreements as the Celularity has alleged that we are in default under each of these agreements and will only forbear from seeking to terminate such agreements to the extent that the Asset Sale Transaction closes.

In addition, if the Asset Sale Transaction is not completed, our Board, in discharging its fiduciary obligations to our stockholders, may evaluate other strategic alternatives that may be available, which alternatives may not be as favorable to us as the Asset Sale Transaction.

***The Asset Purchase Agreement limits our ability to pursue alternatives to the Asset Sale Transaction.***

The Asset Purchase Agreement contains provisions that make it more difficult for us to sell our assets or engage in another type of acquisition transaction with a party other than Celularity. These provisions include a non-solicitation provision and a provision obligating us to pay Celularity a termination fee of \$1.45 million under certain circumstances. These provisions could discourage a third party that might have an interest in acquiring all of, or substantially all of, our assets or our common stock from considering or proposing such an acquisition, even if that party were prepared to pay consideration with a higher value than the consideration to be paid by Celularity.

***Our stockholders may not receive any of the proceeds of the Asset Sale Transaction.***

The proceeds from the Asset Sale Transaction will be paid directly to us. Our Board will evaluate different alternatives for the use of the proceeds from the Asset Sale Transaction. Although the alternatives are expected to

include using a portion of the proceeds to repay our outstanding indebtedness (including prepayment fees) to Perceptive of approximately \$12.6 million in full, to pay transaction and other expenses of approximately \$3 million, return capital to our stockholders and to use the remainder of the proceeds, together with any other sources of liquidity available to us at that time, to support operations at our hydrogel plant and to pursue strategic opportunities including, without limitation, a reverse merger transaction or a strategic acquisition, the Board may decide to utilize all of the proceeds for other purposes.

***We will incur significant expenses in connection with the Asset Sale Transaction, regardless of whether the Asset Sale Transaction is completed and, in certain circumstances, may be required to pay a termination fee to Celularity.***

We expect to incur significant expenses related to the Asset Sale Transaction. These expenses include, but are not limited to, financial advisory and opinion fees and expenses, legal fees, accounting fees and expenses, certain employee expenses, filing fees, printing expenses and other related fees and expenses. Many of these expenses will be payable by us regardless of whether the Asset Sale Transaction is completed. In addition, if the Asset Purchase Agreement is terminated in certain circumstances, we will be required to pay Celularity a \$1.45 million termination fee. However, if the Asset Purchase Agreement is terminated in certain other circumstances, we may be entitled to a \$3 million reverse termination fee from Celularity.

#### **Risks Related to Our Future Operations if We Consummate the Asset Sale Transaction.**

***Our operations will be curtailed and we will have limited sources of revenue following the Asset Sale Transaction, which may negatively impact the value and liquidity of our common stock.***

Upon the closing of the Asset Sale Transaction, our operations will be curtailed as our sources of revenue will be limited to our hydrogel manufacturing business. Although the alternatives under evaluation by our Board for the use of the proceeds from the Asset Sale Transaction includes supporting our operations at our hydrogel plant and pursuing strategic opportunities, there can be no assurance that we will be successful at carrying out such alternatives or that they will be successful at generating revenue. A failure by us to secure additional sources of revenue following the closing of the Asset Sale Transaction could negatively impact the value and liquidity of our common stock.

***The uncertainty regarding the use of proceeds from the Asset Sale Transaction and our future operations may negatively impact the value and liquidity of our common stock.***

Although our Board will evaluate various alternatives regarding the use of the proceeds from the Asset Sale Transaction, it has made no decision with respect to the use of proceeds and has not committed to making any such decision by a particular date. This uncertainty may negatively impact the value and liquidity of our common stock.



***We will continue to incur the expense of complying with public company reporting requirements following the closing of the Asset Sale Transaction.***

After the Asset Sale Transaction, we will continue to be required to comply with the applicable reporting requirements of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), even though compliance with such reporting requirements is economically burdensome.

## **Risks Related to Our Company**

***The report of our independent registered public accounting firm contains an explanatory paragraph as to our ability to continue as a going concern, which could prevent us from obtaining new financing on reasonable terms or at all.***

Because we have had recurring losses, negative cash flows from operating activities, limited cash on hand in light of expected expenditures and are in default of certain financial covenants under our Credit Agreement with Perceptive, the report of Marcum LLP, our independent registered public accounting firm, with respect to our financial statements at December 31, 2017, and for the year ended December 31, 2017, contains an explanatory paragraph as to our potential inability to continue as a going concern. This opinion indicates that substantial doubt exists regarding our ability to remain in business. Such an opinion may adversely affect our ability to obtain new financing on reasonable terms or at all.

***We have experienced significant losses and expect losses to continue for the foreseeable future.***

We have incurred annual net losses of \$25.7 million and \$28.2 million, during the years ended December 31, 2017 and 2016, respectively. As of December 31, 2017, we had an accumulated deficit of \$150.0 million. We expect to incur additional operating losses for the foreseeable future.

***We will require additional capital if we do not consummate the Asset Sale Transaction.***

As of December 31, 2017, we had \$2.2 million of cash on hand. Given our current cost structure, we will require additional equity and/or debt financing if we do not consummate the Asset Sale Transaction. If we are unable to raise

additional capital or if we encounter circumstances that place unforeseen constraints on capital resources, we will be required to take measures to conserve liquidity, which may include, but are not limited to, eliminating all non-essential positions, ceasing all marketing efforts, curtailing business development activities and/or suspending all operations. There can be no assurance that we will be successful in improving revenues, reducing expenses and/or securing additional capital in sufficient amounts and on favorable terms to successfully continue our business.

***We have a substantial amount of indebtedness under our \$12.1 million principal term loan and are in default of certain financial covenants under the Credit Agreement, which may adversely affect our cash flow and our ability to operate our business.***

In order to finance our acquisition of Celleration, on May 29, 2015, we and each of our subsidiaries entered into the Credit Agreement with Perceptive, which provided for a senior, secured term loan with a current principal amount of approximately \$12.1 million. The full unpaid principal amount of the term loan will mature on May 29, 2019. Prior to maturity, on the last business day of each calendar month commencing on the earlier of April 30, 2018 or the date the Asset Purchase Agreement with Celularity is terminated, we will be required to make monthly principal payments of \$225,000, with any remaining unpaid balance of the term loan being payable in cash on the maturity date. The repayment of the term loan and our obligations under the Credit Agreement are secured by a first priority lien on all of our existing and after acquired tangible and intangible assets, including intellectual property. The Credit Agreement also contains certain restrictions that prohibit us and our subsidiaries from engaging in certain transactions and activities, including but not limited to the following:

- entering into, creating, incurring or assuming any indebtedness of any kind, subject to limited exceptions;
- creating or incurring new liens, subject to certain exceptions;
- entering into new acquisitions or investments in other entities, subject to certain exceptions;
- winding up, liquidating or dissolving;
- merging or consolidating with another person or disposing of assets, subject to certain exceptions;
- entering into inbound or outbound licenses, subject to certain exceptions;
- changing the nature of our core business;



- paying cash dividends; and
- repaying, repurchasing or otherwise acquiring shares of our common stock or other equity securities.

Our ability to meet our expenses, debt obligations and other financial covenants under the Credit Agreement will depend on our future performance, which will be affected by financial, business, economic, regulatory and other factors. We will be unable to control many of these factors. We cannot be certain that our earnings will be sufficient to allow us to pay the principal and interest on our debt and meet any other obligations. If we do not have enough money to service our debt, we will be required, but may be unable to refinance or restructure all or part of our existing debt, sell assets, borrow money or raise equity on terms acceptable to us, if at all, and the lender could foreclose on its security interest and liquidate some or all of our assets, which would harm our business, financial condition and results of operations.

The Credit Agreement also requires us to meet certain financial covenants. Our ability to meet these financial covenants may be affected by events beyond our control. If, as or when required, we are unable to repay, refinance or restructure our indebtedness under, or amend the covenants contained in, the Credit Agreement, the lender could institute foreclosure proceedings against our assets, which would harm our business, financial condition and results of operations. We are currently in default of certain financial covenants under the Credit Agreement.

In addition, as a result of our increased level of indebtedness, demands on our cash resources will continue to increase in the future and could, among other things:

- require us to dedicate a large portion of our cash flow from operations to the servicing and repayment of our debt, thereby reducing funds available for working capital, capital expenditures, research and development expenditures and other general corporate requirements;
- limit our ability to obtain additional financing to fund future working capital, capital expenditures, research and development expenditures and other general corporate requirements;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- restrict our ability to make strategic acquisitions or dispositions or to exploit business opportunities;
- place us at a competitive disadvantage compared to our competitors that have less debt;

adversely affect our credit rating, with the result that the cost of servicing our indebtedness might increase and our ability to obtain surety bonds could be impaired;

adversely affect the market price of our common stock; and

limit our ability to apply proceeds from an offering or asset sale to purposes other than the servicing and repayment of debt.

***We are currently in default of certain financial covenants under the Credit Agreement, which allows the lender to exercise certain rights and remedies, including, without limitation, declaring the entire outstanding indebtedness under the Credit Agreement of approximately \$12.1 million immediately due and payable, imposing a default rate of interest and/or foreclosing on some or substantially all of our assets.***

Under the Forbearance and Amendment Agreement dated as of February 5, 2018, the lender agreed to defer the commencement of our remaining principal payments and agreed to extend the forbearance period and to forbear from exercising any rights and remedies related to our default of a covenant pertaining to (i) trailing twelve-month revenue under the Credit Agreement as of (A) September 30, 2016, (B) December 31, 2016, (C) March 31, 2017, (D) June 30, 2017, (E) September 30, 2017, and (F) December 31, 2017 and (ii) failure to maintain on a consolidated basis, a monthly minimum cash balance of at least \$2,000,000, until the earlier of April 30, 2018, the termination of the Asset Purchase Agreement, or the date when the lender becomes aware of any other default.

The remedies available for the lender include, among others, the ability to accelerate and immediately demand payment of the outstanding debt of approximately \$12.1 million under the Credit Agreement, to impose a default rate of interest, to foreclose on some or all of our assets, and/or to take possession of or sell some or all of our assets. Were the lender to demand payment of the outstanding debt after expiration of the forbearance period, we would currently have insufficient funds to satisfy that obligation, and the lender's exercise of its other remedies would have a material adverse effect on our operations and financial condition.

***Occurrence of an event of default under the Credit Agreement could result in a material adverse effect on our business, operating results and financial condition, or the loss of our assets as the lender holds a first priority security interest in all of our assets and the assets of our subsidiaries.***

Events of default under the Credit Agreement include, but are not limited to, the following:

- failure to pay principal, interest or other amounts, if any, when due;
- any form of bankruptcy or insolvency proceeding instituted by or against us or any of our subsidiaries that is not dismissed in 60 days;
- a default occurring under any debenture, mortgage, credit agreement, indenture or other instrument representing or securing indebtedness in an amount exceeding \$250,000;
- we or any of our subsidiaries is party to a change of control;
- the FDA or other governmental authority (i) issues a letter or other communication asserting any of our products lacks a required product authorization, including in respect of CE marks or 510(k)s or 361 HCT/P qualification, or (ii) initiates enforcement action or warning against us, any of our products or manufacturing facilities resulting in the discontinuance of marketing, withdrawal of any material products, or delay in the manufacture of any material products, each lasting for more than 90 days;
- a recall of any product that has generated or is expected to generate at least \$1.0 million in revenue in the aggregate over any consecutive twelve (12) month period;
- we or any of our subsidiaries enters into a settlement agreement with the FDA or any other governmental authority that results in aggregate liability as to any single or related series of transactions, incidents or conditions, in excess of \$500,000;
- we are in default under our license agreement with Celularity or the license agreement is terminated, amended, waived or otherwise modified in a manner materially adverse to the lender's interests; and
- failure to observe or perform any other covenant contained in the Credit Agreement.

Upon occurrence of an event of default under the Credit Agreement, payment of the entire principal amount could be accelerated and become immediately due and payable. The cash that we may be required to pay would most likely come out of our working capital, which may be insufficient to repay the obligation or leave us with insufficient cash to finance our operations. In such event, we may lose some or all of our assets as the lender could foreclose on its security interests and liquidate some or all of these assets, which would harm our business, financial condition and results of operations. We may also be required to file for bankruptcy, sell assets, or cease operations, any of which would put our company, our investors and the value of our common stock, at significant risk.

The pledge of these assets and other restrictions may limit our flexibility in raising capital for other purposes. Because substantially all of our assets are pledged under the Credit Agreement, our ability to incur additional secured indebtedness or to sell or dispose of assets to raise capital may be impaired, which could have an adverse effect on our financial flexibility.

***Our goodwill and long-lived assets are subject to potential further impairment, and if those become further impaired, it could materially further the reduction in the value of our assets and increase our net loss for the year in which the write-off occurs.***

Our intangible and fixed assets have finite useful lives and are amortized or depreciated over their useful lives on either a straight-line basis or over the expected period of benefit or as revenues are earned from the sales of the related products. The underlying assumptions regarding the estimated useful lives of these intangible assets are reviewed annually and more often if an event or circumstance occurs making it likely that the carrying value of the assets may not be recoverable and are adjusted through accelerated amortization if necessary. Whenever events or changes in circumstances indicate that the carrying value of the assets is not recoverable we test intangible assets for impairment based on estimates of future cash flows. If an intangible asset is considered to be impaired, the amount of the impairment will equal the excess of the carrying value over the fair value of the asset.

As of December 31, 2017, we had \$1.7 million in goodwill related to acquisitions, which represents the purchase price we paid in excess of the fair value of the net tangible assets and identifiable intangible assets we acquired. We assess the recoverability of goodwill annually, at the beginning of the fourth quarter of each fiscal year, and between annual tests if an event occurs or circumstances change that would indicate the carrying amount may be impaired. Under Financial Accounting Standards Board guidance for goodwill and other intangible assets, a reporting unit is defined as an operating segment or one level below the operating segment, called a component. However, two or more components of an operating segment will be aggregated and deemed a single reporting unit if the components have similar economic characteristics. We adopted authoritative accounting guidance that allows us to first assess qualitative factors to determine whether it is necessary to perform the more detailed two-step quantitative goodwill impairment test. We perform the quantitative test if the qualitative assessment determined it is more likely than not that a reporting unit's fair value is less than its carrying amount. We may elect to bypass the qualitative assessment and proceed directly to the quantitative test for any reporting unit. When performing the quantitative test, an impairment loss is recognized if the carrying amount of the reporting unit's net assets exceeds the estimated fair value of the reporting unit and the carrying amount of reporting unit goodwill is determined to exceed the implied fair value of that goodwill. As of December 31, 2017 and 2016, we elected to bypass the qualitative assessment and proceed directly to the quantitative test for our reporting unit. As of December 31, 2017, the estimated fair value of our reporting unit was calculated using the sale price of the Asset Sales Transaction. As of December 31, 2016, the estimated fair value of

our reporting unit was calculated using a discounted cash flow model. During the year ended December 31, 2017, we recorded an impairment charge of approximately \$10.3 million related to our goodwill. During the year ended December 31, 2016, we recorded an impairment charge of approximately \$1.7 million related to our MIST tradename and approximately \$9.2 million related to our goodwill.

If actual results differ from the assumptions and estimates used in the goodwill and intangible asset calculations, we could incur further impairment or amortization charges. Any finding that the value of our goodwill and long-lived assets has been further impaired would require us to write off the impaired portion, which could materially reduce the value of our assets and reduce our net income or increase our net loss for the year in which the write off occurs and increase our accumulated deficit, which could contribute to difficulty in raising additional funds.

***If we fail to meet certain minimum sales thresholds for products licensed pursuant to our agreement with Celularity, we could lose our right to license such products.***

Our license agreement with Celularity is terminable on a product-by-product basis if we fail to meet certain minimum sales thresholds in the second year or any subsequent year of commercial sales of the licensed products. Each year of commercial sales is referred to in the license agreement as “launch years” and the calendar period constituting each launch year for the licensed product is determined in accordance with the terms of the license agreement, and for the purpose of determining whether the license can be terminated for failure to meet the minimum sales threshold, Biovance and Interfyl are treated on an aggregate basis as if a single licensed product. To maintain our license for Biovance and Interfyl, we must meet a minimum gross sales amount for Biovance and Interfyl in the second year and third year of commercial sales. If we fail to meet the minimum threshold in the second year of commercial sales of a licensed product, we would be able to cure such failure by making a cure payment specified in the license agreement to Celularity; provided, however, we do not have the option to make a cure payment, should we fail to meet the minimum threshold for such product in the third year of commercial sales, and Celularity may terminate the license agreement with respect to such product. If we do not meet the minimum sales threshold, Celularity may terminate the license with respect to Biovance and Interfyl. Even though we are implementing sales and marketing strategies to meet this minimum gross sales amount, no assurance can be given that we will be able to meet the minimum sales thresholds for Biovance and Interfyl. If we were to lose or otherwise become unable to maintain our right to license Biovance, Interfyl or other products from Celularity, it could have a material adverse effect on our business, financial condition and results of operations. In addition, any termination of our right to license Biovance, Interfyl or other products under the license agreement with Celularity could trigger an event of default under our Credit Agreement.

***Decisions in reimbursement levels by governmental or other third-party payers for our products and procedures using our products may have an adverse impact on acceptance and use of our products.***

We believe that our products will be purchased principally by hospitals, physicians and other healthcare providers, which typically bill various third-party payers, such as state and federal healthcare programs (e.g., Medicare and Medicaid), private insurance plans and managed care plans, for the products and services provided to their patients. The ability of our customers to obtain appropriate reimbursement for products and services from third-party payers is critical to the success of our business because reimbursement status affects which products customers purchase and the prices they are willing to pay. In addition, our ability to obtain reimbursement approval in foreign jurisdictions will affect our ability to expand our product offerings internationally.

Third-party payers have adopted, and are continuing to adopt, a number of policies intended to curb rising healthcare costs. These policies include:

- imposition of conditions of payment by foreign, state and federal healthcare programs as well as private insurance plans;

- rules related to how products and services may be marketed; and

- reduction in reimbursement amounts applicable to specific products and services.

Adverse decisions relating to coverage or reimbursement of our products would have an adverse impact on the acceptance of our products and the prices that our customers are willing to pay for them.

We are unable to predict whether foreign, federal, state or local healthcare reform legislation or regulation affecting our business may be proposed or enacted in the future, or what effect any such legislation or regulation would have on our business. Changes in healthcare systems in the United States or internationally in a manner that significantly reduces reimbursement for procedures using our products or denies coverage for these procedures would also have an adverse impact on the acceptance of our products and the prices which our customers are willing to pay for them.

***Our future success depends on our ability to retain key executives and to attract, retain and motivate qualified personnel.***

We believe that our success will depend, in part, upon our ability to retain David Johnson, our Chief Executive Officer. There can be no assurance that we will be able to find and attract additional qualified employees or retain our Chief Executive Officer and other key personnel. Our inability to hire qualified personnel, or the loss of services of our Chief Executive Officer or key personnel who may be hired in the future may have a material and adverse effect on our business.

***Our strategic business plan may not produce the intended growth in revenue and operating income.***

Our strategies include making significant investments in sales and marketing programs to achieve revenue growth and margin improvement targets. If we do not achieve the expected benefit from these investments or otherwise fail to execute on our strategic initiatives, we may not achieve the growth improvement we are targeting and our results of operations may be adversely affected.

***Our acquisition strategy may not produce the intended growth in revenue and operating income.***

As part of our strategy for growth, we may make acquisitions and enter into strategic alliances such as joint ventures and joint development agreements. However, we may not be able to identify suitable acquisition candidates, complete acquisitions or integrate acquisitions successfully, and our strategic alliances may not prove to be successful. Such acquisitions could reduce shareholders' ownership, require us to incur debt, expose us to liabilities and result in amortization expenses related to intangible assets with definite lives. In addition, acquisitions involve other risks, including diversion of management resources otherwise available for ongoing development of our business and risks associated with entering new markets with which we have limited experience or where distribution alliances with experienced distributors are not available. Our future profitability may depend in part upon our ability to further develop our resources to adapt to these new products or business areas and to identify and enter into satisfactory distribution networks. Moreover, we may fail to realize the anticipated benefit of any acquisition as rapidly as expected or at all, or the acquired business may not perform in accordance with our expectations. We may also incur significant expenditures in anticipation of an acquisition that is never realized. There can be no assurance that difficulties encountered in connection with acquisitions will not have a material adverse effect on our business, financial condition and results of operations.

***Our future success depends upon market acceptance of our existing and future products.***



We believe that our success will depend in part upon the acceptance of our existing and future products by the medical community, hospitals and physicians and other health care providers, third-party payers, and end-users. Such acceptance may depend upon the extent to which the medical community and end-users perceive our products as safer, more effective or cost-competitive than other similar products. Ultimately, for our new products to gain general market acceptance, it may also be necessary for us to develop marketing partners for the distribution of our products. There can be no assurance that our new products will achieve significant market acceptance on a timely basis, or at all. Failure of some or all of our future products to achieve significant market acceptance could have a material adverse effect on our business, financial condition, and results of operations.

***We operate in a highly competitive industry and face competition from large, well-established medical device manufacturers as well as new market entrants.***

Competition from other medical device companies and from research and academic institutions is intense, expected to increase, subject to rapid change and significantly affected by new product introductions and other market activities of industry participants. In addition to competing with universities and other research institutions in the development of products, technologies and processes, we compete with other companies in acquiring rights to products or technologies from those institutions. A number of factors may limit the market acceptance of our products, including the timing of regulatory approvals and market entry relative to competitive products, the availability of alternative products, and the price of our products relative to alternative products, the availability of third party reimbursement and the extent of marketing efforts by third party distributors or agents that we retain. There can be no assurance that our products will receive market acceptance in a commercially viable period of time, if at all. Furthermore, there can be no assurance that we can develop products that are more effective or achieve greater market acceptance than competitive products, or that our competitors will not succeed in developing or acquiring products and technologies that are more effective than those being developed by us, that would render our products and technologies less competitive or obsolete.

Our competitors enjoy several competitive advantages over us, including some or all of the following:

- large and established distribution networks in the United States and/or in international markets;
- greater financial, managerial and other resources for products research and development, sales and marketing efforts and protecting and enforcing intellectual property rights;
- significantly greater name recognition;
- more expansive portfolios of intellectual property rights;



- established relations with physicians, hospitals, other healthcare providers and third party payers;
- products which have been approved by regulatory authorities for use in the United States and/or Europe and which are supported by long-term clinical data; and
- greater experience in obtaining and maintaining regulatory approvals and/or clearances from the FDA and other regulatory agencies.

Our competitors' products will compete directly with our products. In addition, our competitors as well as new market entrants may develop or acquire new treatments, products or procedures that will compete directly or indirectly with our products. The presence of this competition in our market may lead to pricing pressure which would make it more difficult to sell our products at a price that will make us profitable or prevent us from selling our products at all. Our failure to compete effectively would have a material and adverse effect on our business, results of operations and financial condition.

***Changes to the FDA approval process or ongoing regulatory requirements could make it more difficult for us to obtain FDA approval of our products or comply with ongoing requirements.***

Our products are subject to rigorous pre- and post-approval regulation by the FDA as well as other federal and state authorities. Based on scientific developments, post-market experience, or other legislative or regulatory changes, the current FDA standards of review for approving new medical device and other FDA regulated products are sometimes more stringent than those that were applied in the past. For example, with passage of the Food and Drug Administration Safety and Innovation Act in 2012 (the "FDASIA"), the FDA was required to revisit some of its policies regarding 510(k) devices which resulted in the FDA drafting new guidance for the 510(k) process. The FDA continues to revisit and clarify its guidance regarding 510(k) devices, and such revisions could impact the process for clearing medical devices, determining which devices are eligible for 510(k) clearance, the ability to rescind previously granted 510(k) clearances and additional requirements that may significantly impact the process.

Additionally, we believe that some of our products are regulated under Section 361 of the PHS Act and that as a result no premarket review or approval is required. If the FDA does not agree that one or more of our HCT/P products meet its regulatory criteria for regulation solely as 361 HCT/Ps, our HCT/Ps will be regulated as drugs, devices, and/or biological products, and we could be required to withdraw those products from the market until the applicable approvals are obtained.

We cannot determine what effect changes in regulations or legal interpretations by the FDA or the courts, when and if promulgated or issued, may have on our business in the future. Changes could, among other things, require additional

product approvals, different labeling, monitoring of patients, interaction with physicians, education programs for patients or physicians, curtailment of necessary supplies, or limitations on product distribution. These changes, or others required by the FDA could have an adverse effect on the sales of these products, up to and including our inability to sell such products until we may be able to address such requirements. The evolving and complex nature of regulatory science and regulatory requirements, the broad authority and discretion of the FDA and the generally high level of regulatory oversight results in a continuing possibility that from time to time, we will be adversely affected by regulatory actions despite ongoing efforts and commitment to achieve and maintain full compliance with all regulatory requirements.

***Should the FDA determine that Biovance and/or Interfyl do not meet regulatory requirements that permit qualifying HCT/Ps to be processed, stored, labeled and distributed without pre-marketing approval, our supplier may be required by the FDA to stop processing and we may be required to stop distributing Biovance and/or Interfyl, or to narrow the indications for which Biovance and/or Interfyl is marketed, which, in turn, could also result in a default under our Credit Agreement.***

Each of Biovance and Interfyl is a product derived from human tissue. The FDA has specific regulations governing HCT/Ps. An HCT/P is a product containing or consisting of human cells and/or tissue intended for transplantation into humans. HCT/Ps that meet the criteria for regulation solely under Section 361 of the PHS Act and 21 CFR 1271 are not subject to pre-market clearance or approval requirements, but are subject to post-market regulatory requirements. To be a 361 HCT/P, a product must meet all four of the following criteria:

- it must be minimally manipulated;
- it must be intended for homologous use only;
- it must not be combined with another article; and
- it must not have a systemic effect and not be dependent upon the metabolic activity of living cells for its primary function.

We and Celularity believe that each of Biovance and Interfyl qualifies as a 361 HCT/P. The FDA has published several draft guidance documents relating to the regulation of HCT/Ps, including the determination of what constitutes minimal manipulation, and held a public hearing on the subject in September 2016. We cannot predict whether or when the FDA will publish any final guidance documents. Moreover, guidance documents, even in final form, are not binding and are merely a reflection of the FDA's thinking on a particular issue at the time that the final guidance document is published. Should the FDA finalize these drafts and include a significant change in its policy with respect to 361 HCT/P qualifications, or determine that our marketing claims exceed what would be permitted for a 361 HCT/P product, and either Biovance and/or Interfyl is determined to not qualify as a 361 HCT/P product, we may have to obtain approval or clearance from the FDA before we can continue to market Biovance or Interfyl in the United States. Furthermore, a communication from the FDA asserting that either Biovance or Interfyl does not qualify as a 361 HCT/P product could also trigger an event of default under our Credit Agreement.



***Modifications to our current products may require new marketing clearances or approvals or require us to cease marketing or recall the modified products until such clearances or approvals are obtained.***

Any modification to an FDA-cleared or approved product that could significantly affect safety or effectiveness, or that would constitute a major change or modification in the product's intended use, requires a new FDA 510(k) clearance or, possibly, a premarket approval. The FDA requires every manufacturer to make its own determination as to whether a modification requires a new 510(k) clearance or premarket approval, but the FDA may review and disagree with any decision reached by the manufacturer. In the future, we may make additional modifications to our products after they have received FDA clearance or approval and, in appropriate circumstances, determine that new clearance or approval is unnecessary. Regulatory authorities may disagree with our past or future decisions not to seek new clearance or approval and may require us to obtain clearance or approval for modifications to our products. If that were to occur for a previously cleared or approved product, we may be required to cease marketing or recall the modified device until we obtain the necessary clearance or approval. Under these circumstances, we may also be subject to significant regulatory fines or other penalties. If any of the foregoing were to occur, our financial condition and results of operations could be negatively impacted.

***We and our manufacturers are required to comply with current good manufacturing practices ("cGMPs") and current good tissue practices ("cGTPs") and could be subject to suspensions or product withdrawals if found non-compliant.***

We rely on collaborative relationships with third-party contractors to manufacture various aspects of our products. Reliance on third-party contractors subjects us to a number of risks, including regulatory compliance issues. We may be responsible for the failures of our third-party contractors. The FDA regulates the facilities, processes and procedures used to manufacture and market medical products in the United States. Manufacturing facilities must be registered with the FDA and all products made in such facilities must be manufactured in accordance with cGMP, regulations enforced by the FDA. Compliance with cGMP regulations require the dedication of substantial resources and requires significant expenditures. The FDA periodically inspects our manufacturing facilities and those of our contractors. The inspections are generally random, however, and we cannot predict with certainty when the FDA will inspect our facilities or those of our contractors. Any failure of regulatory standards of compliance by us or on the part of our third-party contractors may compel the FDA to take actions to recall products or to suspend, or withdraw one or more of our product approvals. We or our third-party contractors may also be subject to additional FDA actions as identified in the subsequent section. Further, in the event that we need to use an additional contractor or transfer our processes or methods to manufacture our products to an alternative contractor; or if the FDA decides to curtail or cease our operations or cease or curtail our contractor due to manufacturing problems, the FDA's actions could result in product delays which could adversely affect our business, results of operations, and financial condition and cash flow.

***We will be subject to ongoing federal and state regulations, and if we fail to comply, our business could be seriously harmed.***

Following regulatory marketing clearance or approval of any products that we may develop, we will be subject to continued regulatory review, including review of adverse (drug or device) events or reactions and clinical results that are reported after our products become commercially available. This would include results from any post-marketing tests or continued actions required by a condition of approval. The manufacturing facilities we may use to make any of our products may become subject to periodic review and inspection by the FDA. If a previously unknown problem or problems with a product or a manufacturing and laboratory facility used by us is discovered, the FDA may impose restrictions on that product or on the manufacturing facility, including requiring us to withdraw the product from the market. Any changes to an approved product, including the way it is manufactured or promoted, often requires FDA approval before the product, as modified, can be marketed. In addition, for products we develop in the future, we and our contract manufacturers may be subject to ongoing FDA requirements for submission of safety and other post-market information. If we or any of our contract manufacturers fail to comply with applicable regulatory requirements, a regulatory agency may:

- issue warning letters;
- impose civil or criminal penalties;
- suspend or withdraw our regulatory approval;
- suspend or terminate any of our ongoing clinical trials;
- refuse to approve pending applications or supplements to approved applications filed by us;
- impose restrictions on our operations;

- close the facilities of our contract manufacturers; and/or

- seize or detain products or require a product recall.

Additionally, regulatory review covers our activities in the promotion of our medical products, with significant potential penalties and restrictions for promotion of drugs, devices or tissues for an unapproved use. Sales and marketing programs, such as illegal promotions to health care professionals, are under scrutiny for compliance with various mandated requirements. We are also required to submit information on open and completed clinical trials to public registries and databases. Failure to comply with these requirements could expose us to negative publicity, fines and penalties that could harm our business.

If we violate regulatory requirements at any stage, whether before or after marketing approval is obtained, we may be fined, be forced to remove a product from the market or experience other adverse consequences, including delay, which would materially harm our financial results. Additionally, we may not be able to obtain the labeling claims necessary or desirable for product promotion.

***We and our sales personnel, whether employed by us or by others, must comply with various federal and state anti-kickback, self-referral, false claims and reporting and similar laws, any breach of which could cause a material adverse effect on our business, financial condition and results of operations.***

Our relationships with physicians, hospitals, other healthcare providers and the marketers of our products are subject to scrutiny under various U.S. federal anti-kickback, self-referral, false claims, physician sunshine and other reporting laws and regulations and similar laws, often referred to collectively as healthcare fraud and abuse laws. Healthcare fraud and abuse laws are complex, and even minor, inadvertent violations can give rise to liability, or claims of alleged violations. Possible sanctions for violation of these fraud and abuse laws include monetary fines; civil and criminal penalties; exclusion from federal and state healthcare programs, including Medicare, Medicaid, Veterans Administration health programs, workers' compensation programs and TRICARE, the healthcare system administered by or on behalf of the U.S. Department of Defense for uniformed services beneficiaries, including active duty and their dependents, retirees and their dependents; and forfeiture of amounts collected in violation of such prohibitions. Many states have similar, or sometimes broader, fraud and abuse laws that also authorize substantial civil and criminal penalties for violations. Any government investigation or a finding of a violation of these laws would likely result in a material adverse effect on the market price of our common stock, as well as our business, financial condition and results of operations.

The federal Anti-Kickback Statute prohibits any knowing and willful offer, payment, solicitation or receipt of any form of remuneration in return for the referral of an individual or the ordering or recommending of the use of a product or service for which payment may be made by any federal healthcare program, including Medicare. The



definition of “remuneration” has been broadly interpreted to include anything of value, including gifts, discounts, the furnishing of supplies or equipment, payments of cash and waivers of payments. States also often have anti-kickback laws which may be broader in scope and apply to referrals and items or services reimbursed by both governmental and non-governmental third-party payers, including private insurers.

The federal Physician Payments Sunshine Act requires certain manufacturers of drugs, devices, biologics and medical supplies that are reimbursable under Medicare, Medicaid or Children’s Health Insurance Program to report annually to Centers for Medicare and Medicaid Services information related to payments and other transfers of value to physicians and teaching hospitals, and ownership and investment interests held by physicians and their immediate family members. States also often have analogous laws and regulations, such as state anti-kickback and false claims laws, which may be broader in scope and apply to referrals and items or services reimbursed by both governmental and non-governmental third-party payers, including private insurers; and state transparency and reporting laws, which may require drug, device, and biologics manufacturers to report information to the state related to payments and other transfers of value to physicians and other healthcare providers, price disclosures, or marketing expenditures.

The scope and enforcement of the healthcare fraud and abuse laws is uncertain and subject to rapid change. There can be no assurance that federal or state regulatory or enforcement agencies will not investigate our current or future activities under these laws. Any investigation or challenge could have a material adverse effect on our business, financial condition and results of operations. Any state or federal investigation, regardless of the outcome, could be costly and time-consuming. Additionally, we cannot predict the impact of any changes in these laws, whether these changes are retroactive or will have effect on a going-forward basis only.

Because our business involves arrangements with physicians, hospitals, and healthcare providers, including physicians who consult with us on the design of our products, we could be materially impacted if regulatory or enforcement agencies or courts interpret our financial relationships with healthcare providers who refer, order, or use our products to be in violation of health care fraud and abuse laws. Such governmental action could harm our reputation and the reputations of the healthcare providers that we do business with. In addition, the cost of noncompliance with these laws could be substantial because we could be subject to monetary fines and civil or criminal penalties, and we could also be excluded from state and federal healthcare programs, including Medicare and Medicaid, for non-compliance.

***If we are unable to protect our intellectual property rights adequately, we may not be able to compete effectively.***

Our success depends in part on our ability to protect the proprietary rights to the technologies used in our products. We rely on patent protection, as well as a combination of trademark laws and confidentiality, noncompetition and other contractual arrangements to protect our proprietary technology. However, these legal means afford only limited protection and may not adequately protect our rights or permit us to gain or keep a competitive advantage. Our patents and patent applications, if issued, may not be broad enough to prevent competitors from introducing similar products into the market. Our patents, if challenged or if it attempts to enforce them, may not necessarily be upheld by the courts. In addition, patent protection in foreign countries may be different from patent protection under U.S. laws and may not be favorable to us. Efforts to enforce any of our proprietary rights could be time-consuming and expensive, which could adversely affect our business and prospects and divert management's attention.

***We are dependent on proprietary know-how, and a failure to protect our proprietary know-how would harm our business and operation.***

We rely on trade secret protection to protect our interests in proprietary know-how and for processes for which patents are difficult to obtain or enforce. We may not be able to protect our trade secrets adequately. In addition, we rely on non-disclosure and confidentiality agreements with employees, consultants and other parties to protect, in part, trade secrets and other proprietary technology. These agreements may be breached and we may not have adequate remedies for any breach. Moreover, others may independently develop equivalent proprietary information, and third parties may otherwise gain access to our trade secrets and proprietary knowledge. Any disclosure of confidential data into the public domain or to third parties could allow competitors to learn our trade secrets and use the information in competition against us.

Despite our efforts to protect our proprietary rights, there is no assurance that such protections will preclude our competitors from developing and/or marketing similar products. While we are not aware of any third party intellectual property that would materially affect our business, our failure or inability to obtain patents and protect our proprietary information could result in our business being adversely affected.

***If we are not able to establish and maintain successful arrangements with third parties or successfully build our own sales and marketing infrastructure, we may not be able to commercialize our products, which would adversely affect our business and financial condition.***

To commercialize our products, we must continue to develop our own sales, marketing and distribution capabilities, which will be expensive and time consuming, or make arrangements with third parties to perform these services for

us. The third parties may not be capable of successfully selling any of our products. We will have to commit significant resources to developing a marketing and sales force and supporting distribution capabilities. If we decide to enter into arrangements with third parties for performance of these services, we may find that they are not available on terms acceptable to us, or at all.

***We may face intellectual property infringement claims that could be time-consuming, costly to defend and could result in our loss of significant rights and, in the case of patent infringement claims, the assessment of treble damages.***

On occasion, we may receive notices of claims of our infringement, misappropriation or misuse of other parties' proprietary rights. We may have disputes regarding intellectual property rights with the parties that have licensed those rights to us. We may also initiate claims to defend our intellectual property. Intellectual property litigation, regardless of its outcome, is expensive and time-consuming, could divert management's attention from our business and have a material negative effect on our business, operating results or financial condition. In addition, the outcome of such litigation may be unpredictable. If there is a successful claim of infringement against us, we may be required to pay substantial damages—including treble damages if we were to be found to have willfully infringed a third party's patent—to the party claiming infringement, and to develop non-infringing technology, stop selling our products or using technology that contains the allegedly infringing intellectual property or enter into royalty or license agreements that may not be available on acceptable or commercially practical terms, if at all. Our failure to develop non-infringing technologies or license the proprietary rights on a timely basis could harm our business. In addition, modifying our products to exclude infringing technologies could require us to seek re-approval or clearance from various regulatory bodies for our products, which would be costly and time consuming. Also, we may be unaware of pending patent applications that relate to our technology. Parties making infringement claims on future issued patents may be able to obtain an injunction that would prevent us from selling our products or using technology that contains the allegedly infringing intellectual property, which could harm our business.

***We may face product liability claims that could result in costly litigation and significant liabilities, and we may not be able to maintain adequate product liability insurance.***

Our business exposes us to the risk of product liability claims that are inherent in the testing, manufacturing and marketing of medical devices. This risk exists even if a device is cleared or approved for commercial sale by the FDA and manufactured in facilities licensed and regulated by the FDA or an applicable foreign regulatory authority. Manufacturing and marketing of our commercial devices may expose us to product liability and other tort claims. Additionally, regardless of the merit or eventual outcome, product liability claims may result in:

- litigation costs;
- distraction of management's attention from our primary business;



- impairment of our business reputation;
- the inability to commercialize our devices;
- device recall or withdrawal from the market;
- withdrawal of clinical trial participants;
- substantial monetary awards to patients or other claimants; or
- loss of revenue.

Although we have, and intend to maintain, liability insurance, the coverage limits of our insurance policies may not be adequate, and one or more successful claims brought against us may have a material adverse effect on our business and results of operations. If we are unable to obtain insurance in the future at an acceptable cost or on acceptable terms with adequate coverage, we will be exposed to significant liabilities.

***Healthcare policy changes, including reforms to the U.S. healthcare system, may have a material adverse effect on us.***

Healthcare costs in the United States have risen significantly over the past decade. There have been, and continue to be, proposals by legislators, regulators, and third-party payers to keep these costs down. The efforts of governments and third-party payers to contain or reduce the cost of healthcare and legislative and regulatory proposals to broaden the availability of healthcare will likely affect the business and financial condition of biomedical companies. A number of legislative and regulatory changes in the healthcare system in the United States and other major healthcare markets have occurred in recent years, and interpretation and application of such changes continue to evolve. These developments have included healthcare reform legislation enacted by certain states and implementation of the Patient Protection and Affordable Care Act (the “Affordable Care Act”) enacted in 2010 which resulted in significant changes to the health care industry. These developments could, directly or indirectly, impose limitations on the prices we will be able to charge for our products, or the amounts of reimbursement available for our products from governmental agencies or third-party payers. These limitations could have a material adverse effect on our financial position and results of operations.

The Affordable Care Act includes significant provisions that encourage state and federal law enforcement agencies to increase activities related to preventing, detecting and prosecuting those who commit health care fraud and abuse. The

Affordable Care Act continues to be implemented through regulation and government activity but is subject to possible amendment, additional implementing regulations and interpretive guidelines. The manner in which the Affordable Care Act continues to evolve could materially affect the extent to which and the amount at which medical devices and products are reimbursed by government programs such as Medicare, Medicaid and TRICARE. We cannot predict all impacts the Affordable Care Act may have on our products, but it may result in our products being chosen less frequently or the pricing being substantially lowered. Further, the Affordable Care Act has been subject to judicial and Congressional challenges, and legislative initiatives to modify, limit, or repeal the Affordable Care Act continue. For example, members of the current Congress have proposed additional legislative changes, including complete repeal and replacement of certain provisions of the Affordable Care Act. It remains to be seen, however, precisely what new healthcare reform legislation will be enacted, and what impact it will have on the availability of healthcare and containing or lowering the cost of healthcare. Such reforms could have an adverse effect on anticipated revenue from our products and may affect our overall financial condition and ability to develop future products.

Other healthcare reform proposals have emerged at the federal and state levels. We cannot predict the exact effect newly enacted laws or any future legislation or regulation will have on us. However, the implementation of new legislation and regulation may lower reimbursements for our products, reduce medical procedure volumes and adversely affect our business, possibly materially.

***If we cannot maintain relationships with certain of our suppliers, it may be difficult to replace those suppliers and our business may suffer.***

In general, raw materials essential to our business are readily available from multiple sources. However, for reasons of quality assurance, availability, or cost effectiveness, certain components and raw materials are available only from a sole supplier.

We believe that, due to the size and scale of production of our suppliers, there should be adequate supply of these raw materials from these manufacturers. In addition, our policy is to maintain sufficient inventory of components so that our production will not be significantly disrupted even if a particular component or material is not available for a period of time. However, there is no guarantee that our inventory will be sufficient to carry us through any disruption in supply. Because we have no direct control over our third-party suppliers, interruptions or delays in the products and services provided by these third parties may be difficult to remedy in a timely fashion. In addition, if such suppliers are unable or unwilling to deliver the necessary raw materials or products, we may be unable to redesign or adapt our technology to work without such raw materials or products or find alternative suppliers or manufacturers. In such events, we could experience interruptions, delays, increased costs or quality control problems.

Under our Supply Agreements, we receive finished goods from Celularity. Because we have no direct control over Celularity's suppliers, interruptions or delays in the products and services provided by these parties may be difficult to remedy in a timely fashion. In addition, if such suppliers are unable or unwilling to deliver the necessary products, we would be unable to sell any products that we expect from Celularity, and, therefore, could experience a significant adverse impact on our revenue.

In addition, on December 1, 2017, we received notice from Celularity that we are in material breach of the Supply Agreements for failure to purchase the required amounts of materials under the Supply Agreements. Celularity estimated that an additional purchase of at least \$842,000 would have to be made by us to remedy this breach. Celularity has agreed to forbear from exercising its right to terminate the supply agreement until the closing of the Asset Purchase Agreement or termination of the Asset Purchase Agreement for any reason. If we do not consummate the Asset Sale Transaction and we were to lose our rights to purchase finished goods from Celularity under the Supply Agreements, it will have a significant adverse effect on our business, financial condition and results of operations.

We purchase the MIST Therapy system from a single source and UltraMIST from a single source. Reliance on outside suppliers makes us vulnerable to a number of risks that could impact our ability to manufacture the MIST Therapy system and UltraMIST and/or disposable applicators, resulting in harm to our business, including:

- inability to obtain an adequate supply in a timely manner or on commercially reasonable terms;
- uncorrected defects that impact the performance, efficacy and safety of our products;
- difficulty identifying and qualifying alternative suppliers for components in a timely manner;
- production delays related to the evaluation and testing of products from alternative suppliers and corresponding regulatory qualifications;
- delays in delivery by our suppliers due to changes in demand from us or other customers; and
- delays in delivery or production stoppage by our supplier due to a shortage of one or more of the components comprising our product.

If the supply of the MIST Therapy system or UltraMIST or the disposable applicators or saline bottles is interrupted or significantly delayed and we are unable to acquire product from alternate sources in a timely manner and at a commercially reasonable price, our ability to meet our customers' demand would be impaired and our business could

be harmed. Identifying and qualifying additional or replacement suppliers for the MIST Therapy system and/or UltraMIST or disposable applicators may not be accomplished quickly or at all and could involve significant additional costs. Interruption of supply from our suppliers or failure to obtain additional suppliers would limit our ability to distribute our products and could therefore have an adverse effect on our business.

***Contractual and other disagreements with or involving our licensors, distribution partners and other commercial partners could harm our business, make us liable to them or result in litigation costs or other expenses, particularly if we do not consummate the Asset Sale Transaction.***

Our agreements with licensors, distribution partners and other commercial partners require us to comply with performance conditions that are subject to interpretation and could result in disagreements. At any given time, we may be in disputes with one or more licensors, distribution partners or other commercial partners. Any such dispute could be very expensive for us, even if the outcome is ultimately in our favor. On December 1, 2017, we received the Notices from Celularity. Celularity has agreed to forbear from exercising its right to terminate the license agreement until the closing of the Asset Sale Transaction or termination of the Asset Purchase Agreement for any reason. If we do not consummate the Asset Sale Transaction and transfer the License Agreement and Supply Agreements to Celularity as a part of the Purchased Assets we may face termination or litigation with respect to the Supply Agreements and the License Agreement. We cannot predict the outcome of any arbitration or litigation, the effect of any negative judgment against us or the amount of any settlement that we may enter into with such licensors, distribution partners or any other third-party. A contractual dispute may result in a licensor or other commercial partners seeking to terminate our agreements, which could harm our business, even if such termination would be wrongful.

***We are dependent upon third-party local distributors to market and distribute our products in key markets.***

We rely on third-party distributors for marketing and distribution of our products in certain markets, both domestically and internationally. Our success in generating sales in markets where we have engaged local distributors depends in part on the efforts of others whom we do not employ. Many of these distributors have only limited personnel, which could impair their ability to successfully market, sell and service our products. Because of limited resources or for other reasons, they may not comply with applicable local regulations or respond promptly to adverse event reporting requirements under FDA regulations. As a result of such failures to comply with regulatory requirements, we may experience significant loss of revenue, increased costs and damage to our reputation, and our business, financial condition and results of operations could be materially adversely affected. In addition, if a distributor is terminated by us or goes out of business, it may take us a period of time to locate an alternative distributor, to transfer or obtain appropriate regulatory approvals and to train our personnel to market our products, and our ability to sell and service our products in the region formerly serviced by such terminated distributor could be materially adversely affected. Any of these factors could materially adversely affect our revenue in markets served by distributors, increase our costs in those markets or damage our reputation.



***Security breaches and other disruptions could compromise our information and expose it to liability, which would cause our business and reputation to suffer.***

In the ordinary course of our business, we use networks to collect and store sensitive data, including intellectual property, proprietary business information and that of our customers, suppliers and business partners, personally identifiable information of our customers and employees, and data relating to patients who use our products. The secure processing, maintenance and transmission of this information is critical to our operations. Despite our security measures, our information technology and infrastructure may be vulnerable to attacks by hackers or breached due to employee error, malfeasance or other disruptions. Any such breach could compromise our networks and the information stored there could be accessed, publicly disclosed, lost or stolen. Any such access, disclosure or other loss of information could result in legal claims or proceedings, liability under laws that protect the privacy of personal information, and regulatory penalties, disrupt our operations and the services we provide to customers, damage our reputation, and cause a loss of confidence in our products and services, which could adversely affect our operating margins, revenues and competitive position.

#### **Risks Related to Ownership of Our Common Stock and Warrants**

***The issuance of additional equity securities may negatively impact the trading price of our common stock.***

We have issued equity securities in the past and may continue to issue equity securities to finance our activities in the future. We may not be able to sell shares or other securities in any offering at a price per share that is equal to or greater than the price per share previously paid by investors. In addition, outstanding options and warrants to purchase our common stock may be exercised and additional options and warrants may be issued, resulting in the issuance of additional shares of common stock. The issuance by us of additional equity securities or securities convertible into or exchangeable or exercisable for common stock, may result in additional dilution to our stockholders, and even the perception that such an issuance may occur could have a negative impact on the trading price of our common stock.

***Our stock price has been and may continue to be volatile, which could result in substantial losses for investors.***

The market price of our common stock has been and is likely to continue to be highly volatile and could fluctuate widely in response to various factors, many of which are beyond our control, including the following:

- technological innovations or new products and services by or our competitors;

- additions or departures of key personnel;
- sales of our common stock, particularly under any registration statement for the purposes of selling any other securities, including management shares;
- our ability to execute our business plan;
- operating results that fall below expectations;
- loss of any strategic relationship;
- industry developments;
- economic, political and other external factors; and
- period-to-period fluctuations in our financial results.

In addition, the securities markets have from time to time experienced significant price and volume fluctuations that are unrelated to the operating performance of particular companies. These market fluctuations may also significantly affect the market price of our common stock.

***Our stock price, and the stock price of many other life science companies, have suffered significant declines over the past 12 months.***

Market prices for securities of life sciences companies, particularly companies like ours with limited product revenues, have been highly volatile and have suffered sharp losses over the past 12 months. As a result of these declines, it has become much harder for life sciences companies, like us, to raise money, as needed, in the capital markets. As such, should we desire to sell equity in the future to raise capital, such capital may not be available on favorable terms, or at all. In addition, any such capital raises could be highly dilutive to current stockholders. Depressed valuations of our stock will also make it harder for us to consummate strategic transactions or acquisitions, which have historically been a significant part of our growth strategy, absent significant dilution to our current investors.

***We do not expect to pay dividends in the future if we do not consummate the Asset Sale Transaction. As a result, any return on investment may be limited to the value of our common stock.***

We do not anticipate paying any dividends in the foreseeable future if we do not consummate the Asset Sale. Our Credit Agreement prohibits us from paying cash dividends or distributions on our capital stock. Even if we are permitted to pay cash dividends in the future, we currently intend to retain any future earnings for funding growth if we do not consummate the Asset Sale Transaction. As a result, an investor should not rely on an investment in our securities if such investor requires dividend income. Capital appreciation, if any, of our shares may be the only source of gain on our securities for the foreseeable future. Moreover, an investor may not be able to re-sell such investor's shares at or above the price paid for them.

***There are inherent limitations in all control systems, and misstatements due to error or fraud may occur and not be detected.***

The ongoing internal control provisions of Section 404 of the Sarbanes-Oxley Act of 2002 require us to identify material weaknesses in internal control over financial reporting, which is a process to provide reasonable assurance regarding the reliability of financial reporting for external purposes in accordance with accounting principles generally accepted in the United States. Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our internal controls and disclosure controls will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. In addition, the design of a control system must reflect the fact that there are resource constraints and the benefit of controls must be relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, in our company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple errors or mistakes. Further, controls

can be circumvented by individual acts of some persons, by collusion of two or more persons, or by management override of the controls. The design of any system of controls is also 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 our stated goals under all potential future conditions. Over time, a control may be inadequate because of changes in conditions, such as growth of the company or increased transaction volume, or the degree of compliance with the policies or procedures may deteriorate. Because of inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

In addition, discovery and disclosure of a material weakness, by definition, could have a material adverse impact on our financial statements. Such an occurrence could discourage certain customers or suppliers from doing business with us, cause downgrades in our future debt ratings leading to higher borrowing costs and affect how our stock trades. This could, in turn, negatively affect our ability to access public debt or equity markets for capital.

***Our board of directors can authorize the issuance of preferred stock, which could diminish the rights of holders of our common stock and make a change of control of it more difficult even if it might benefit our stockholders.***

Our board of directors is authorized to issue shares of preferred stock in one or more series and to fix the voting powers, preferences and other rights and limitations of the preferred stock. Accordingly, we may issue shares of preferred stock with a preference over our common stock with respect to dividends or distributions on liquidation or dissolution, or that may otherwise adversely affect the voting or other rights of the holders of common stock. Issuances of preferred stock, depending upon the rights, preferences and designations of the preferred stock, may have the effect of delaying, deterring or preventing a change of control, even if that change of control might benefit our stockholders.

***Offers or availability for sale of a substantial number of shares of our common stock may cause the price of our common stock to decline.***

Sales of a significant number of shares of our common stock in the public market could harm the market price of our common stock and make it more difficult for us to raise funds through future offerings of common stock. As additional shares of our common stock become available for resale in the public market, the supply of our common stock will increase, which could decrease the price of our common stock.

In addition, if our stockholders sell substantial amounts of our common stock in the public market, upon the expiration of any statutory holding period under Rule 144, upon the expiration of lock-up periods applicable to outstanding shares, or upon the exercise of outstanding options or warrants, it could create a circumstance commonly referred to as an “overhang,” in anticipation of which the market price of our common stock could fall. The existence of an overhang, whether or not sales have occurred or are occurring, could also make it more difficult for us to raise additional financing through the sale of equity or equity-related securities in the future at a time and price that we deem reasonable or appropriate.



*If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.*

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about it or our business. Although we currently have research coverage by securities and industry analysts, you should not invest in our common stock in anticipation that we will increase such coverage. If one or more of the analysts who covers us at any given time downgrades our stock or publishes inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analyst's ceases coverage of us or fails to publish reports on us regularly, demand for our stock could decrease, which could cause our stock price and trading volume to decline.

#### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

**Not applicable**

#### **ITEM 2. PROPERTIES**

As of December 31, 2017, we operated three offices, with our corporate headquarters located in Yardley, Pennsylvania, where we lease approximately 9,000 square feet of office space. We maintain a combined corporate office and warehouse facility in Eden Prairie, Minnesota, where we lease approximately 9,000 square feet of space, as well as a manufacturing facility in Langhorne, Pennsylvania, where we lease approximately 16,500 square feet of office and manufacturing space. We believe that all our facilities are well maintained and are suitable and adequate for our current needs.

#### **ITEM 3. LEGAL PROCEEDINGS**

From time to time, we may become involved in lawsuits, investigations and claims that arise in the ordinary course of business. We believe we have meritorious defenses against all pending claims and intend to vigorously pursue them. While it is not possible to predict or determine the outcomes of any pending actions, we believe the amount of liability, if any, with respect to such actions, would not materially affect our financial position, results of operations or cash flows.

On February 22, 2018, a putative stockholder class action complaint was filed in the United States District Court for the District of Delaware against us and each member of the Board, captioned Ronald Cresta, Individually and on Behalf of All Others Similarly Situated v. Alliqua BioMedical Inc., David Johnson, Joseph M. Leone, Gary Restani, Jeffrey Sklar and Mark Wagner. The complaint alleges, among other things, that we and the Board violated federal securities laws and regulations by soliciting stockholder votes in connection with the Asset Sale Transaction through a proxy statement that omits material facts necessary to make the statements therein not false or misleading. The complaint seeks, among other things, to enjoin us and the Board from conducting the stockholder vote on the Asset Sale Transaction unless and until the allegedly omitted material information is disclosed to the Company's stockholders, damages allegedly suffered by the plaintiffs as a result of the asserted omissions, as well as related attorneys' fees and expenses.

We are reviewing the complaint and have not yet formally responded to it, but we believe that the plaintiffs' allegations are without merit and intend to defend against them vigorously. However, litigation is inherently uncertain and there can be no assurance regarding the likelihood that our defense of the actions will be successful. Additional complaints containing substantially similar allegations may be filed in the future.

#### **ITEM 4. MINE SAFETY DISCLOSURES**

Not applicable.

## **PART II**

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

##### *Market for Common Stock*

Our common stock has been listed on The NASDAQ Capital Market under the symbol "ALQA" since January 28, 2014. The following table sets forth for the periods indicated the high and low sales price per share of our common stock as reported on The NASDAQ Capital Market for the period indicated. The sales prices for our common stock are adjusted for the 1-for-10 reverse stock split of our common stock that occurred on October 5, 2017:

2017		2016	
High	Low	High	Low

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Fourth Quarter	\$3.85	\$1.81	\$9.50	\$5.70
Third Quarter	\$4.60	\$2.30	\$13.00	\$7.30
Second Quarter	\$5.30	\$3.20	\$14.80	\$7.00
First Quarter	\$8.50	\$4.10	\$23.00	\$7.60



### ***Holders of Record***

As of February 28, 2018, there were approximately 263 holders of record of our common stock.

### ***Dividends***

We have never paid cash dividends on our common stock and, if we do not consummate the Asset Sale Transaction, do not anticipate paying any cash dividends in the foreseeable future, but intend to retain our capital resources for reinvestment in our business. In addition, our Credit Agreement prohibits us from paying cash dividends or distributions on our capital stock.

### ***Issuer Purchases of Equity Securities***

We did not repurchase any of our equity securities during the fourth quarter of the fiscal year ended December 31, 2017.

## **ITEM 6. SELECTED FINANCIAL DATA**

Not applicable.

## **ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

*The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes included in this report. This discussion and analysis contains forward-looking statements based on our current expectations, assumptions, estimates and projections. These forward-looking statements involve risks and uncertainties. Our actual results could differ materially from those indicated in these forward-looking statements as a result of certain factors, as more fully discussed in Item 1 of this report, entitled "Business," under "Forward-Looking Statements" and Item 1A of this*

*report, entitled “Risk Factors.”*

## **Overview**

We are a regenerative technologies company that commercializes differentiated regenerative medical products which assist the body in the repair or replacement of soft tissue. Through our sales and distribution network, together with our proprietary products, we believe we offer solutions that allow clinicians to utilize the latest advances in regenerative technologies to bring improved patient outcomes to their practices. Our contract manufacturing business provides custom hydrogels to the OEM market.

On January 5, 2018, we entered into the Asset Purchase Agreement pursuant to which we will sell the Purchased Assets to Celularity. As consideration for the Purchased Assets, Celularity has agreed to pay us \$29 million in cash. No debt or significant liabilities will be assumed by the Celularity in the Asset Sale Transaction.

Under the terms of the Asset Purchase Agreement, we will retain certain specified assets, including, among other things, cash, accounts receivable, and its hydrogel contract manufacturing business, including our SilverSeal and Hydress product lines.

The transactions contemplated by the Asset Purchase Agreement must be approved by the affirmative vote of a majority of the voting power of issued and outstanding shares of our common stock. In addition to the receipt of our approval of our stockholders, each party’s obligation to consummate the Asset Sale Transaction is conditioned upon certain other customary closing conditions. We expect the Asset Sale Transaction to be consummated no later than May 31, 2018.

## **Recent Events**

### ***Reverse Stock Split***

The Company effected a 1-for-10 reverse stock split of its outstanding common stock on October 5, 2017. The accompanying consolidated financial statements and accompanying notes to the consolidated financial statements give retroactive effect to the reverse stock split for all periods presented. The shares of common stock retained a par value of \$0.001 per share. Accordingly, stockholders’ equity reflects the reverse stock split by reclassifying from common stock to additional paid-in capital an amount equal to the par value of the decreased shares resulting from the reverse stock split.



### ***Senior Secured Term Loan Facility***

We are currently in default of certain financial covenants under the Credit Agreement, as a result of our failure (A) to achieve \$22.25 million, \$24.6 million, \$27.0 million, \$30.3 million \$33.8 million and \$37.8 million of gross revenue for the twelve-month periods ended September 30, 2016, December 31, 2016, March 31, 2017, June 30, 2017 September 30, 2017 and December 31, 2017, respectively, and (B) to maintain on a consolidated basis, a monthly minimum cash balance of at least \$2 million. Under the Forbearance and Amendment Agreement dated as of February 5, 2018, the lender agreed to defer the commencement of our remaining principal payments and agreed to extend the forbearance period and to forbear from exercising any rights and remedies related to our default of a covenant pertaining to (i) trailing twelve-month revenue under the Credit Agreement as of (A) September 30, 2016, (B) December 31, 2016, (C) March 31, 2017, (D) June 30, 2017, (E) September 30, 2017, and (F) December 31, 2017 and (ii) failure to maintain on a consolidated basis, a monthly minimum cash balance of at least \$2,000,000, until the earlier of April 30, 2018, the termination of the Asset Purchase Agreement with Celularity, or the date when the lender becomes aware of any other default.

The remedies available for the lender include, among others, the ability to accelerate and immediately demand payment of the outstanding debt of approximately \$12.1 million under the Credit Agreement, to impose a default rate of interest, to foreclose on some or all of our assets, and/or to take possession of or sell some or all of our assets. Were the lender to demand payment of the outstanding debt after expiration of the forbearance period, we would currently have insufficient funds to satisfy that obligation, and the lender's exercise of its other remedies would have a material adverse effect on our operations and financial condition.

The lender has the rights to pursue any rights and remedies available to it, including, but not limited to, declaring all or any portion of the outstanding principal amount to be immediately due and payable, imposing a default rate of interest as specified in the credit agreement, or pursuing the lender's rights and remedies as a secured party under the UCC as a secured lender. In addition, the lender has a lien on substantially all of our assets and, as a result of the default, may seek to foreclose on some or substantially all of our assets after the expiration of the forbearance.

If we consummate the Asset Sale Transactions, we plan to fully repay this debt from the proceeds of the Asset Purchase Transaction.

### ***Contract Manufacturing Business***

During the year ended December 31, 2017, one customer accounted for 67% of our contract manufacturing revenue and 6% of our total net revenue from continuing operations. We are uncertain as to this customer's intentions to use

our services during the fiscal year ending December 31, 2018.

### ***Asset Sales***

In order to add capital and to focus on future investments on commercializing our own regenerative technologies, on August 31, 2017, we entered into the Argentum Purchase Agreement whereby we agreed to sell to Argentum all of the our rights, including (i) all distribution rights, exclusivity rights, intellectual property rights and marketing rights to the TheraBond product line and (ii) the unsold inventory of TheraBond products and work in process previously purchased by us in existence as of the closing, which occurred upon execution and delivery of the Argentum Purchase Agreement. In consideration for the sale of the TheraBond product line and the unsold TheraBond inventory to Argentum by us, Argentum agreed to pay (i) \$3.6 million for the TheraBond product line and certain other agreements between the parties and (ii) up to \$112,000 for the unsold TheraBond inventory upon our completion of our obligations to deliver all remaining and qualifying unsold TheraBond inventory, as specified in the Argentum Purchase Agreement. Of the \$3.6 million of consideration, \$300,000 is deposited in an indemnity escrow account under standard terms and conditions. This amount is classified under current assets of discontinued operations on our balance sheet as of December 31, 2017. As a result of the foregoing, we no longer distribute Therabond and past sales of Therabond are accounted for as a discontinued operation.

On June 30, 2016, we entered into a purchase agreement with BSN, pursuant to which we sold to BSN all of our rights under our former distribution agreement with Sorbion, dated as of September 20, 2013, as subsequently amended and assigned to BSN, including but not limited to all distribution rights, exclusivity rights, intellectual property rights and marketing rights to the sorbion product line and our remaining unsold inventory of sorbion products purchased under the distribution agreement. Subject to the terms and conditions of the purchase agreement, in exchange for the sale of such rights to the sorbion products and unsold products, BSN paid us an aggregate consideration of \$4.1 million. Effective upon the closing of the sale, the distribution agreement was terminated. In addition, we received \$100,000 in connection with a transaction services agreement with BSN. As a result of the foregoing, we no longer distribute sorbion wound dressings and exudate management products and past sales of sorbion products are accounted for as a discontinued operation.

### ***Termination of Merger Agreement***

On October 5, 2016, we entered into a merger agreement to acquire the business of Soluble Systems, LLC (“Soluble”) through a series of transactions. On February 27, 2017, we terminated this agreement.

We advanced Soluble \$1.4 million, \$1.0 million during the year ended December 31, 2016 and \$0.4 million on January 30, 2017.



On October 27, 2017, we received \$1 million under an agreement with Soluble in connection with amounts advanced to Soluble by us. With the receipt of this \$1 million, we acknowledged that all amounts due to us from Soluble were paid in full.

#### ***Private Placement***

On February 27, 2017, we issued and sold an aggregate of 554,000 shares of our common stock at a purchase price of \$5.00 per share to certain accredited investors in a private placement (the “Private Placement”), pursuant to a Securities Purchase Agreement (the “Securities Purchase Agreement”). Proceeds from the Private Placement, net of underwriting and administrative fees, were approximately \$2.5 million.

#### ***Underwritten Public Offering***

On April 3, 2017, we closed an underwritten public offering of 947,325 shares of our common stock at a price to the public of \$4.00 per share. Proceeds from this offering, net of underwriting and administrative fees were approximately \$3.3 million. The shares of common stock were issued pursuant to our shelf registration statement on Form S-3 previously filed with the Securities and Exchange Commission and declared effective on September 25, 2014.

On April 3, 2017, we issued warrants to purchase an aggregate of 23,684 shares of our common stock to the underwriter of this offering. These warrants were immediately exercisable, have an exercise price of \$4.40, and expire on March 29, 2022.

Pursuant to an anti-dilution provision provided in the warrants dated November 8, 2012 to purchase common stock at an initial exercise price of \$21.90, the exercise price of these November 2012 warrants was adjusted to the public offering price of \$4.00. As of April 3, 2017, November 2012 warrants to purchase 36,230 shares of the Company’s common stock were outstanding. These warrants expired in November 2017.

#### ***Amendment and Adjustments of the Perceptive Warrant***

On April 6, 2017, we and Perceptive entered into an amendment and restatement of a warrant to reduce the exercise price from \$5.00 to \$4.70, reflecting the impact of the public offering price of \$4.00 per share at which we sold our

common stock in the underwritten public offering that closed on April 3, 2017 as described above. The warrant was exercisable for 200,000 shares of our common stock. Perceptive will not have the right to exercise the warrant to the extent that after giving effect to such exercise, Perceptive would beneficially own in excess of 9.99% of the common stock outstanding immediately after giving effect to such exercise. On June 1, 2017, we and Perceptive entered into an amendment to increase the warrant from 200,000 to 210,000 shares of our common stock as well as delay the principal payments due under the Credit Agreement beginning June 30, 2017 until August 31, 2017.

## Results of Operations

### *Year Ended December 31, 2017 Compared to the Year Ended December 31, 2016*

#### Overview.

Our operations intended to be sold under the Asset Purchase Agreement have not been reclassified to discontinued operations since they are classified as Held for Use. These operations will be presented in continuing operations until the Asset Purchase Agreement is approved by our stockholders. Upon approval of the Asset Purchase Agreement, these operations will be reclassified to discontinued operations.

For the years ended December 31, 2017 and 2016, we had a net loss of \$25.7 million and \$28.2 million, respectively. Included in the operating loss for the years ended December 31, 2017 and 2016 was non-cash stock-based compensation of \$2.0 million and \$4.9 million, and an increase in the fair value adjustments to contingent consideration of \$35,000 and a decrease in the fair value adjustments to contingent consideration of \$10.1 million, respectively. Impairment charges of \$10.3 million and \$10.9 million were also included in our operating loss for the year ended December 31, 2017 and 2016, respectively.

**Revenues, net.** For the year ended December 31, 2017 revenues increased by \$3.3 million, or 20%, to \$19.6 million from \$16.3 million for the year ended December 31, 2016. The increase in our overall revenue was primarily due to increase in sales of our biologics products.



The components of revenue were as follows for the years ended December 31, 2017 and 2016 (in thousands):

	Year Ended December 31,	
	2017	2016
Revenues		
Product	\$ 17,573	\$ 14,142
Contract manufacturing	1,992	2,152
Total revenues, net	\$ 19,565	\$ 16,294

**Gross profit.** Our gross profit was \$12.8 million for the year ended December 31, 2017 compared to gross profit of \$10.2 million for the year ended December 31, 2016. The improved results for the year ended December 31, 2017, as compared to 2016 was primarily due to the greater volume of product sales as product revenue typically commands higher gross profit margins. Gross margin on our product sales was approximately 75%, while our overall gross margin was approximately 65% for year ended December 31, 2017. Gross margin on our product sales was approximately 77%, while our overall gross margin was approximately 63% for year ended December 31, 2016.

The components of cost of revenues are as follows for the years ended December 31, 2017 and 2016 (in thousands):

	Year Ended December 31,	
	2017	2016
Cost of revenues		
Materials and finished products	\$ 4,315	\$ 3,301
Stock-based compensation	45	184
Compensation and benefits	663	916
Depreciation and amortization	841	779
Equipment, production and other expenses	899	871
Total cost of revenues	\$ 6,763	\$ 6,051

**Selling, general and administrative expenses.** The following table highlights selling, general and administrative expenses by type for the years ended December 31, 2017 and 2016 (in thousands):

	Year Ended December 31,	
	2017	2016
Selling, general and administrative expenses		
Compensation and benefits	\$ 12,798	\$ 15,504
Stock-based compensation	1,975	4,691
Professional fees	2,866	4,420

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Marketing	1,435	2,302
Depreciation and amortization	4,404	3,054
Other expenses	4,612	5,354
Total selling, general and administrative expenses	\$ 28,090	\$ 35,325

Selling, general and administrative expenses decreased by \$7.2 million, to \$28.1 million for the year ended December 31, 2017, as compared to \$35.3 million for the year ended December 31, 2016.

Compensation and benefits decreased by \$2.7 million, to \$12.8 million for the year ended December 31, 2017, as compared to \$15.5 million for the year ended December 31, 2016. The decrease in compensation and benefits was primarily due to the decrease in the average number of full-time employees in 2017 compared to 2016. Stock-based compensation decreased by \$2.7 million, to \$2.0 million for the year ended December 31, 2017, as compared to \$4.7 million for the year ended December 31, 2016. The decrease in stock-based compensation is primarily due to the lower weighted average estimated fair value of options granted during the year ended December 31, 2017, as compared to the year ended December 31, 2016.

Marketing expenses decreased by \$0.9 million to \$1.4 million for the year ended December 31, 2017, as compared to \$2.3 million for the year ended December 31, 2016. This decrease was primarily due to a reduction in the number of industry conferences attended.

The decrease in professional fees and other expenses is due to a reduction in expenditures for recruiting, travel, information technology, and legal fees. This decrease is consistent with our strategy to reduce operating costs.

**Royalties.** Royalties expense decreased by \$0.3 million, to \$0.8 million for the year ended December 31, 2017, as compared to \$1.1 million for the year ended December 31, 2016. During the year ended December 31, 2016, a minimum royalty of \$600,000 was due Noble Fiber Technologies (“Noble”). During the year ended December 31, 2017, there was no minimum royalty due Noble. The decrease in royalties payable to Noble was offset by increased royalties paid to Celularity, due to increased sales of our licensed biologics products.

**Research and product development expenses.** During the years ended December 31, 2017 and 2016, we incurred research and development costs of approximately \$121,000 and \$859,000, respectively, related to a randomized controlled trial for our Biovance product in chronic diabetic foot ulcers. We experienced slower than expected patient enrollment and projected costs to complete the trial were significantly higher than we had previously expected. In addition, we believed there was no longer a business need for this trial due to the amount of patient data currently available, our success in getting government and commercial insurance coverage for Biovance, and our recent increase in Biovance sales. Due to these factors, we decided to terminate patient enrollment for the Biovance trial. We completed our study during the first half of 2017.

**Milestone expense to licensor.** During the year ended December 31, 2016, we incurred \$1.0 million of milestone expense for achieving two of the three milestones under the license agreement with HLI related to the launch of the Interfyl product. We incurred expense of \$500,000 related to the first commercial sale of Interfyl in the flowable matrix configuration and \$500,000 related to the first commercial sale of Interfyl in the particulate form. We initiated sales and marketing efforts of Interfyl in September 2016 and commercial sales of both configurations occurred in September 2016. This milestone payment is included in other current liabilities as of December 31, 2017. This milestone payment will be forgiven by Celularity if the Asset Sale Transaction is consummated.

**Acquisition-related expenses.** On October 5, 2016, we entered into a merger agreement to acquire the business of Soluble through a series of transactions. On February 27, 2017, we terminated this agreement.

In connection with the merger agreement to acquire the business of Soluble, we provided Soluble with bridge loans in the form of subordinated promissory notes totaling approximately \$1.4 million. We advanced Soluble \$1.0 million during the year ended December 31, 2016 and \$0.4 million on January 30, 2017. Pursuant to the terms of the merger agreement, the amount was to be repaid in full upon termination of the agreement.

On October 27, 2017, we received \$1 million under an agreement with Soluble in connection with amounts advanced to Soluble by us. With the receipt of this \$1 million, we acknowledged that all amounts due to us from Soluble were paid in full.

During the year ended December 31, 2017 we recorded a reduction of \$365,000 in acquisition expenses which consisted of a recovery of bad debt expense for \$650,000, offset by approximately \$285,000 of other acquisition related expenses related to the terminated Soluble transaction.

During the year ended December 31, 2016, we incurred \$3.0 million of acquisition-related costs related to Soluble, including bad debt expense of \$1.0 million related to amounts advanced to Soluble as of that date.

**Change in fair value of contingent consideration liability.** During the year ended December 31, 2017, we recorded an increase in the fair value of the contingent consideration liability of approximately \$35,000 compared to a decrease of \$10.1 million in the year ended December 31, 2016.

The decrease in the fair value of the contingent consideration liability in the year ended December 31, 2016 was due to lower MIST sales than originally projected.

**Impairment charges.** During the year ended December 31, 2017, we recorded an impairment charge of approximately \$10.3 million related to our goodwill. We proceeded directly to the quantitative analysis considering the consideration to be received and the assets to be sold under the Asset Purchase Agreement. During the year ended December 31, 2016, we recorded an impairment charge of approximately \$1.7 million related to our MIST Therapy tradename and \$9.2 million related to our goodwill. The impairment charge was triggered by the significant and sustained decline in our stock price and resulting market capitalization. The revenue from our portfolio of advanced wound care technologies was less than anticipated. Based on our revised forecasts our fair value was calculated to be less than the amounts assigned to our assets and liabilities resulting in an impairment of goodwill as of December 31, 2016. The impairment charge related to the tradename was calculated based on the fair value of MIST Therapy tradename as compared to the carrying value as of December 31, 2016

**Warrant modification expense.** During the year ended December 31, 2017, we recognized \$803,000 of warrant modification expense in connection with the amendment of the warrant issued to Perceptive. In connection with entry into the January 2017 forbearance agreement, as amended March and June 2017, we also amended and restated the warrant issued to Perceptive in connection with the closing of the Credit Agreement in May 2015. The amended and restated warrant is exercisable for 210,000 shares of our common stock. The expense recorded during the year ended December 31, 2017 represents the incremental value of the modified warrant as compared to the original warrant, both valued as of the respective modification dates.

**Other income.** During the year ended December 31, 2017, we were required to perform certain services related to the transition of the TheraBond business to Argentum. As compensation, Argentum paid us \$200,000 for the services completed during the year ended December 31, 2017. This compensation was recognized over the 90-day service period and is included in other income for the year ended December 31, 2017. During the year ended December 31, 2016, we were required to perform certain services related to the transition of the sorbion business to BSN. As compensation, BSN paid us \$100,000 for the services completed during the year ended December 31, 2016. This compensation was recognized over the 90-day service period and is included in other income for the year ended December 31, 2016.

**Income tax benefit.** During the year ended December 31, 2017, we recorded an income tax benefit of approximately \$743,000. The income tax benefit is primarily attributable to the change in the useful life of the MIST Therapy tradename from indefinite to definite, which necessitates a write-down of the deferred tax liability associated with the asset. During the year ended December 31, 2016, we recorded an income tax benefit of approximately \$715,000.

On December 22, 2017, the U.S. government enacted significant changes to federal tax law following the passage of the Tax Cuts and Jobs Act (“the Act”). The Act significantly changes the U.S. corporate tax system. We have reasonably estimated the accounting for the effects of the Act during the year ended December 31, 2017. Our financial statements for the year ended December 31, 2017 reflect certain effects of the Act including a reduction in the corporate tax rate from 34% to 21% and changes to limitations on deductibility of executive compensation. As we have recorded a full valuation allowance against our net deferred tax assets as of December 31, 2017, these changes have no impact on the income tax benefit for year ending December 31, 2017. Given the significant changes resulting from and complexities associated with the Act, the financial impacts for the fourth quarter and full year 2017 are provisional and subject to further analysis, interpretation and clarification of the Act, which could result in changes to these estimates during 2018. We will reflect any adjustments to the provisional amounts within one year from the enactment date of the Act, if applicable. For additional discussion of the impact on the income tax provision, other income tax balances and related disclosures, see “Note 15 – Income Taxes” in the Notes accompanying the audited Consolidated Financial Statements.

**Income from Discontinued Operations.** During the year ended December 31, 2017, we sold our rights to the TheraBond product line, as well as our remaining TheraBond inventory. This sale resulted in income from discontinued operations of approximately \$2.15 million for the year ended December 31, 2017, which consists of \$454,000 of income from discontinued operations as well as \$1.7 million recognized as a gain on the sale of the assets. During the year ended December 31, 2016, we had \$4.2 million of income from discontinued operations in connection with our discontinued sorbion product line and \$0.6 million from our discontinued Therabond product line.

## **Liquidity and Capital Resources**

***Year Ended December 31, 2017 Compared to Year Ended December 31, 2016***

As of December 31, 2017, we had cash and cash equivalents totaling \$2.2 million compared to \$5.6 million at December 31, 2016. The decrease was largely attributable to cash used in operating activities of approximately \$10.7 million, \$1.6 million paid to Perceptive for the early extinguishment of debt, \$675,000 to pay a portion of the contingent consideration related to the Celleration acquisition, and \$350,000 issued as a bridge loan to Soluble in connection with the terminated acquisition. This decrease was offset by \$5.9 million received from net proceeds from the issuance of common stock, the proceeds of \$3.4 million from the sale of TheraBond and \$1 million repaid by Soluble in connection with the bridge loan.

Net cash used in operating activities was \$10.7 million and \$18.3 million for the years ended December 31, 2017 and 2016, respectively. The decrease in net cash used in operating activities was due to an increase in our gross profit and a decrease in our selling, general and administrative expenses.

Net cash provided by investing activities was \$3.9 million for the year ended December 31, 2017, compared to net cash used in investing activities of \$2.2 million in the year ended December 31, 2016. Cash provided by investing activities during the year ended December 31, 2017 included \$3.4 million from the sale of TheraBond and net receipts of \$650,000 from Soluble. Cash provided by investing activities during the year ended December 31, 2016 included \$4.1 million received from the sale of the rights to the sorbion product, offset by purchases of improvements and equipment of \$893,000 and \$1.0 million provided to Soluble as a bridge loan.

Net cash provided by financing activities for the year ended December 31, 2017 consisted of \$5.9 million received from issuance of common stock offset by payments of \$1.6 million to repay a portion of our long-term debt and \$675,000 to pay the cash portion of the contingent consideration related to the Celleration acquisition. During the year ended December 31, 2016, net cash flow used in financing activities consisted of \$2.6 million utilized to pay the cash portion of the contingent consideration related to the Celleration acquisition and \$1.7 million utilized to repay a portion of our long-term debt.

At December 31, 2017, current assets totaled \$7.5 million and current liabilities totaled \$17.0 million, as compared to current assets totaling \$11.8 million and current liabilities totaling \$20.1 million at December 31, 2016. As a result, we had negative working capital of \$9.5 million at December 31, 2017 compared to working capital of \$8.4 million at December 31, 2016.

Our cash requirements have historically been for mergers and acquisitions, post-market clinical trials, marketing and sales activities, finance and administrative costs, capital expenditures and overall working capital. We have experienced negative operating cash flows since inception and have funded our operations primarily from sales of common stock and other securities.

## **Liquidity Outlook**

Because we have had recurring losses, negative cash flows from operating activities, limited cash on hand in light of our expected expenditures and are in default of our Credit Agreement, the report of our independent auditors with respect to our financial statements as of December 31, 2017 and for the year ended December 31, 2017 contains an explanatory paragraph as to the potential inability to continue as a going concern. This opinion indicates that substantial doubt exists regarding our ability to remain in business.

Our financial statements have been prepared assuming we will continue as a going concern. We have experienced recurring losses since our inception. We incurred a net loss of \$25.7 million and used \$10.7 million in cash from operations for the year ended December 31, 2017, and had an accumulated deficit of \$150.0 million as of December 31, 2017. At December 31, 2017, we had approximately \$2.2 million of cash and cash equivalents.

On December 1, 2017, we received the Notices from Celularity. Celularity estimated that an additional purchase of at least \$842,000 would have to be made by us to remedy the breach under the Supply Agreements. Celularity has agreed to forbear from exercising its right to terminate the Supply Agreements and License Agreements until the closing of the Asset Sale Transaction or termination of the Asset Purchase Agreement for any reason. We believe that Celularity's notice of material breach of the License Agreement is without merit.

If we do not receive stockholder approval, the Asset Sale Transaction will not occur. Instead, we will retain the assets and liabilities proposed to be sold in the Asset Sale Transaction and will not receive the \$29 million cash consideration from Celularity. We are currently in default of a covenant pertaining to trailing twelve-month revenue under the Credit Agreement as a result of our failure to achieve \$24,600,000, \$27,200,000, \$30,300,000, \$33,800,000 and \$37,800,000 of gross revenue for the twelve-month periods ended December 31, 2016, March 31, 2017, June 30, 2017, September 30, 2017 and December 31, 2017, respectively. The Company is also currently in default of a

minimum cash balance requirement under the Credit Agreement due to the Company having a cash balance of less than \$2,000,000. As of the date hereof, the lender has agreed to forbear from exercising any rights and remedies related to each such event of default until the earlier of April 30, 2018 or the termination of the Asset Purchase Agreement with Celularity. In addition, on December 1, 2017, we received the Notices from Celularity.

Without receipt of the cash consideration from Celularity, we will not be able to repay our indebtedness under the Credit Agreement and will be unable to purchase materials under the Supply Agreements. The lender under the Credit Agreement may pursue the rights and remedies available to it under the Credit Agreement including, but not limited to, declaring all or any portion of the outstanding principal amount to be immediately due and payable, imposing a default rate of interest as specified in the Credit Agreement, or pursuing the lender's rights and remedies as a secured party under the UCC as a secured lender. In addition, the lender has a lien on substantially all of our assets and, as a result of the default, may seek to foreclose on some or substantially all of our assets. If we do not consummate the Asset Sale Transaction with Celularity and transfer the License Agreement and Supply Agreements to Celularity as part of the Purchased Assets, we may face termination or litigation with respect to the Supply Agreements and the License Agreement. If we were to lose our rights to license Biovance, Interfyl or other products from Celularity under the License Agreement, it will have a material adverse effect on our business, financial condition and results of operations which could force the Company to file for bankruptcy if we are not successful in obtaining the level of financing needed for our operations.

Therefore, if we do not consummate the Asset Sale Transaction, due to our history of recurring losses and our negative working capital, there is substantial doubt about our ability to continue operating as a going concern within one year from the date of this filing.

If we consummate the Asset Sale Transaction, we, and not our stockholders, will receive the proceeds from the Asset Sale Transaction. We do not intend to liquidate following the Asset Sale Transaction. Our Board will evaluate alternatives for the use of the cash proceeds to be received at closing, which alternatives are expected to include using a portion of the proceeds to repay our outstanding indebtedness (including prepayment fees) to Perceptive of approximately \$12.6 million in full and to pay transaction and other expenses of approximately \$3 million. In addition, we intend to continue to maximize stockholder interests with a goal of returning value to our stockholders. Although our Board has not made any determination, such alternatives may include paying a special dividend, a share repurchase or other return of capital to our stockholders. We intend to use the remainder of the proceeds, together with any other sources of liquidity available to us at that time, to support operations at our hydrogel plant and to pursue strategic opportunities including, without limitation, a reverse merger transaction or a strategic acquisition. The amounts and timing of our actual expenditures, however, will depend upon numerous factors, and we may find it necessary or advisable to use portions of the proceeds from the Asset Sale Transaction for different or presently non-contemplated purposes.



### **Off Balance Sheet Arrangements**

As of December 31, 2017, we had no off-balance sheet arrangements in the nature of guarantee contracts, retained or contingent interests in assets transferred to unconsolidated entities (or similar arrangements serving as credit, liquidity or market risk support to unconsolidated entities for any such assets), or obligations (including contingent obligations) arising out of variable interests in unconsolidated entities providing financing, liquidity, market risk or credit risk support to us, or that engage in leasing, hedging or research and development services with us.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements in accordance with generally accepted accounting principles requires that we make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of our financial statements and the reported amounts of revenues and expenses during the reporting period. The accounting policies that we believe require more significant estimates and assumptions include valuing equity securities and derivative financial instruments issued in financing transactions, allowance for doubtful accounts, inventory reserves, deferred taxes and related valuation allowances, and the fair values of long lived assets, intangibles, goodwill and contingent consideration. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable. We evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ significantly from these estimates under different assumptions or conditions. There have been no material changes to these estimates for the periods presented in this Annual Report.

We believe that of our significant accounting policies, which are described below and in Note 2 to our audited consolidated financial statements included in this Item 7 of this Annual Report, the following accounting policies involve a greater degree of judgment and complexity. Accordingly, these are the policies we believe are the most critical to aid in fully understanding and evaluating our financial condition and results of operations.

### ***Acquisitions***

Results of operations of acquired companies are included in our results of operations as of the respective acquisition dates. The purchase price of each acquisition is allocated to the net assets acquired based on estimates of their fair values at the date of the acquisition. Any purchase price in excess of these net assets is recorded as goodwill. The allocation of purchase price in certain cases may be subject to revision based on the final determination of fair values during the measurement period, which may be up to one year from the acquisition date.

Contingent consideration is recognized at the estimated fair value on the acquisition date. Subsequent changes to the fair value of contingent payments are recognized in earnings. Contingent payments related to acquisitions consist of revenue based payments, and are valued using discounted cash flow techniques. The fair value of revenue based payments is based upon probability-weighted future revenue estimates and increases or decreases as revenue estimates or expectation of timing of payments changes.

### ***Goodwill and Other Indefinite-Lived Intangible Assets***

Goodwill and other indefinite-lived intangible assets are tested for impairment annually, at the end of the four quarter of each fiscal year, and between annual tests if an event occurs or circumstances change that would indicate it is more likely than not that the carrying amount may be impaired. Impairment testing for goodwill is done at a reporting unit level. A reporting unit is defined as an operating segment or one level below an operating segment, called a component. However, two or more components of an operating segment will be aggregated and deemed a single reporting unit if the components have similar economic characteristics. We operate as one reporting unit.

Authoritative accounting guidance allows us to first assess qualitative factors to determine whether it is necessary to perform a more detailed quantitative impairment test for goodwill and other indefinite-lived intangible assets. We may elect to bypass the qualitative assessment and proceed directly to the quantitative test for any reporting unit or indefinite-lived intangible assets. Qualitative factors that we consider as part of our assessment include a comparison of the most recent valuation to reporting unit carrying amounts, change in our market capitalization and its implied impact on reporting unit fair value, industry and market conditions, macroeconomic conditions, trends in product costs and financial performance of our businesses. If we perform the quantitative test for any reporting units or indefinite-lived intangible assets, we generally use a discounted cash flow method to estimate fair value. The discounted cash flow method is based on the present value of projected cash flows. Assumptions used in these cash flow projections are generally consistent with our internal forecasts. The estimated cash flows are discounted using a rate that represents the weighted average cost of capital. The weighted average cost of capital is based on a number of variables, including the equity-risk premium and risk-free interest rate. Management believes the assumptions used for the impairment tests are consistent with those that would be utilized by a market participant performing similar analyses and valuations. Adverse changes in future market conditions or weaker operating results compared to our expectations may impact our projected cash flows and estimates of weighted average cost of capital, which could result in a potential impairment charge if we are unable to recover the carrying value of our goodwill and other intangible assets.

On January 5, 2018, we entered into the Asset Purchase Agreement pursuant to which we agreed to sell the Purchased Assets to Celularity. As consideration for the Purchased Assets, Celularity has agreed to pay us \$29 million in cash. No debt or significant liabilities will be assumed by the Celularity in the Asset Sale.

Under the terms of the Asset Purchase Agreement, we will retain certain specified assets, including, among other things, cash, accounts receivable, and its hydrogel contract manufacturing business, including our SilverSeal and Hydress product lines.

The transactions contemplated by the Asset Purchase Agreement must be approved by the affirmative vote of a majority of the voting power of issued and outstanding shares of our common stock. In addition, to the receipt of our approval of our stockholders, each party's obligation to consummate the Asset Sale is conditioned upon certain other customary closing conditions.

We proceeded directly to the quantitative analysis considering the consideration to be received and the assets to be sold under the Asset Purchase Agreement. As a result of this test, our goodwill was determined to be impaired and an impairment charge of \$10.3 million was recorded for the year ended December 31, 2017.

For the 2016 annual goodwill impairment test and certain indefinite-lived intangible assets impairment tests, we elected to bypass the qualitative assessment and proceeded directly to the quantitative analysis using a discounted cash flow method to estimate fair value. As a result of this test, our goodwill was determined to be impaired and an impairment charge of \$9.2 million was recorded for the year ended December 31, 2016. Additionally, our indefinite-lived intangible asset related to the MIST Therapy tradename was also impaired and an impairment charge of \$1.7 million was recorded for the year ended December 31, 2016. Total non-cash impairment charges related to goodwill and indefinite-lived intangible assets of \$10.9 million is included in impairment charges the consolidated statement of operations for the year ended December 31, 2016. The impairment charge was triggered by the significant and sustained decline in our stock price and resulting market capitalization. The revenue from our portfolio of advanced wound care technologies was less than anticipated. Based on our revised forecasts, our fair value was calculated to be less than the amounts assigned to our assets and liabilities, resulting in an impairment in goodwill as of December 31, 2016. The impairment charge related to the tradename was calculated based on the fair value of the MIST Therapy tradename as compared to the carrying value of the MIST Therapy tradename as of December 31, 2016.

If different assumptions for our goodwill and other indefinite-lived intangible assets impairment tests had been applied, significantly different outcomes could have resulted. There can be no assurance that the estimates and assumptions used in our goodwill and indefinite-lived intangible assets impairment testing performed as of the end of the fourth quarter of 2017 will prove to be accurate predictions of the future. For example, if general macroeconomic conditions deteriorate or otherwise vary from current assumptions (including changes in the weighted average cost of

capital), industry or market conditions deteriorate, business conditions or strategies for a specific reporting unit change from current assumptions, including cost increases or loss of major customers, our businesses do not perform as projected, or there is an extended period of a significant decline in our stock price, this could be an indicator that the excess fair value of our reporting units could be lessened and the chance of an impairment of goodwill could be raised.

### ***Impairment of Long-Lived Assets Subject to Amortization***

We amortize intangible assets with finite lives over their estimated useful lives and review them for impairment at least annually or whenever an impairment indicator exists. We continually monitor events and changes in circumstances that could indicate carrying amounts of our long-lived assets, including our intangible assets, may not be recoverable. When such events or changes in circumstances occur, we assess recoverability by determining whether the carrying value of such assets will be recovered through the undiscounted expected future cash flows. If the future undiscounted cash flows are less than the carrying amount of these assets, we recognize an impairment loss based on the excess of the carrying amount over the fair value of the assets.

Due to the Asset Purchase Agreement, we expect that it is more likely than not that our long-lived asset group related to the Purchased Assets will be sold or otherwise disposed of significantly before the end of its previously estimated useful life. We, therefore, tested our long-lived assets for recoverability as of December 31, 2017. These long-lived assets consist of property, plant and equipment and intangible assets subject to amortization.

The expected consideration under the Asset Purchase Agreement for the sale of the long-lived asset group related to the Purchased Assets approximate the net book value of these assets at December 31, 2017. Therefore, no impairment charge was recorded for long-lived assets during the year ended December 31, 2017

### **Recent Accounting Standards**

Recently issued accounting pronouncements are addressed in Note 2 in the Notes to Consolidated Financial Statements.

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

Not required.

## **ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Our Consolidated Financial Statements and the relevant notes to those statements are attached to this report beginning on page F-1.

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

None.

## **ITEM 9A. CONTROLS AND PROCEDURES**

### ***Disclosure Controls and Procedures.***

We conducted an evaluation of the effectiveness of our “disclosure controls and procedures” (“Disclosure Controls”), as defined by Rules 13a-15(e) and 15d-15(e) of the Exchange Act, as of December 31, 2017, the end of the period covered by this Annual Report on Form 10-K. The Disclosure Controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our Disclosure Controls were effective at the reasonable assurance level as of December 31, 2017.

### ***Management’s Report on Internal Control over Financial Reporting***

Management is responsible for establishing and maintaining adequate internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the consolidated financial statements for external reporting purposes in accordance with generally accepted accounting principles.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness of internal control over financial reporting to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate over time.

Management, including our Chief Executive Officer and Chief Financial Officer, assessed the effectiveness of our internal control over financial reporting as of December 31, 2017. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) in *Internal Control—Integrated Framework (2013)*. Based on its assessment and those criteria, management has concluded that we maintained effective internal control over financial reporting as of December 31, 2017.

#### ***Changes in Internal Control over Financial Reporting***

We regularly review our system of internal control over financial reporting to ensure we maintain an effective internal control environment. As we expand, we make changes to our processes and systems to improve controls and we continue to create and enhance the design and documentation of our internal control processes to ensure effective controls over financial reporting.

There have been no changes in our internal control over financial reporting during the quarter ended December 31, 2017 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### **ITEM 9B. OTHER INFORMATION**

None.

#### **PART III**

**ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

Information with respect to this item will be set forth in our definitive proxy statement for the 2018 Annual Meeting of Stockholders, which shall be filed with the Securities and Exchange Commission within 120 days after the end of the fiscal year covered by this report, (our “Proxy Statement”), and is incorporated herein by reference.

## **ITEM 11. EXECUTIVE COMPENSATION**

Information with respect to this item will be set forth in our Proxy Statement, and is incorporated herein by reference.

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

Information with respect to this item will be set forth in our Proxy Statement, and is incorporated herein by reference.

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

Information with respect to this item will be set forth in our Proxy Statement, and is incorporated herein by reference.

## **ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

Information with respect to this item will be set forth in our Proxy Statement, and is incorporated herein by reference.

## **ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES**

The following documents are filed as part of this report:

(1) Financial Statement Schedules:

Report of Independent Registered Public Accounting Firm  
Consolidated Balance Sheets as of December 31, 2017 and 2016

F-2  
F-3



<u>Consolidated Statements of Operations for the years ended December 31, 2017 and 2016</u>	<u>F-4</u>
<u>Consolidated Statements of Stockholders' Equity for the years ended December 31, 2017 and 2016</u>	<u>F-5</u>
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2017 and 2016</u>	<u>F-6</u>
<u>Notes to Consolidated Financial Statements</u>	<u>F-7</u>

(2) Financial Statement Schedules:

None

(3) Exhibits:

See "Index to Exhibits" for a description of our exhibits.

## SIGNATURES

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

ALLIQUA  
BIOMEDICAL, INC.

By: /s/ DAVID JOHNSON  
David Johnson  
President and Chief  
Executive Officer

Date: March 2, 2018

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

Signature	Title	Date
/s/ DAVID JOHNSON David Johnson	President, Chief Executive Officer and Director (principal executive officer)	March 2, 2018
/s/ BRIAN M. POSNER Brian M. Posner	Chief Financial Officer, Treasurer and Secretary (principal financial and accounting officer)	March 2, 2018
/s/ JOSEPH LEONE Joseph Leone	Director	March 2, 2018
/s/ GARY RESTANI Gary Restani	Director	March 2, 2018
/s/ JEFFREY SKLAR Jeffrey Sklar	Director	March 2, 2018
/s/ MARK WAGNER Mark Wagner	Director	March 2, 2018



## Index to Exhibits

### Exhibit No. Description

<u>2.1</u>	<u>Agreement and Plan of Merger, dated May 5, 2014, by and between Alliqua, Inc., ALOA Merger Sub, Inc., Choice Therapeutics, Inc. and E. James Hutchens, as the Stockholder Representative, incorporated by reference to Exhibit 2.1 to the Form 8-K filed May 6, 2014.</u>
<u>2.2</u>	<u>Agreement and Plan of Merger, dated June 5, 2014, by and between Alliqua, Inc. and Alliqua BioMedical, Inc., incorporated by reference to Exhibit 2.1 to the Form 8-K filed June 11, 2014.</u>
<u>2.3**</u>	<u>Agreement and Plan of Merger, dated February 2, 2015, by and among Alliqua BioMedical, Inc., ALOA Cedar, Inc., Celleration, Inc. and certain representatives of the stockholders of Celleration, Inc., as identified therein, incorporated by reference to Exhibit 2.1 to the Form 8-K filed February 2, 2015.</u>
<u>2.4**</u>	<u>Contribution Agreement and Plan of Merger, dated October 5, 2016, by and among Alliqua BioMedical, Inc., Alliqua Holdings, Inc., Chesapeake Merger Corp., and Soluble Systems, LLC, incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K filed on October 6, 2016.</u>
<u>2.5**</u>	<u>Asset Purchase Agreement, dated January 5, 2018, by and between Alliqua BioMedical, Inc. and Celularity Inc., incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K filed on January 5, 2018.</u>
<u>2.6**</u>	<u>Asset Purchase Agreement, dated August 31, 2017, by and between Alliqua BioMedical, Inc. and Argentum Medical, LLC, incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K filed on September 5, 2017.</u>
<u>3.1</u>	<u>Certificate of Incorporation of Alliqua BioMedical, Inc., incorporated by reference to Exhibit 3.1 to the Form 8-K filed June 11, 2014.</u>
<u>3.2</u>	<u>Certificate of Amendment to Certificate of Incorporation of Alliqua BioMedical, Inc., incorporated by reference to Exhibit 3.3 to the Form 8-K filed June 11, 2014.</u>
<u>3.3</u>	<u>Certificate of Amendment to Certificate of Incorporation of Alliqua BioMedical, Inc., incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on May 6, 2016.</u>
<u>3.4</u>	<u>Certificate of Amendment to Certificate of Incorporation of Alliqua BioMedical, Inc., incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on October 5, 2017.</u>
<u>3.5</u>	<u>Bylaws of Alliqua BioMedical, Inc., incorporated by reference to Exhibit 3.2 to the Form 8-K filed June 11, 2014.</u>
<u>4.1</u>	<u>Form of Warrant used in connection with February 16, 2012 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed February 21, 2012.</u>
<u>4.2</u>	<u>Form of Warrant used in connection with August 14, 2012 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed August 16, 2012.</u>
<u>4.3</u>	<u>Form of Warrant used in connection with November 8, 2012 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed November 14, 2012.</u>
<u>4.4</u>	<u>Form of Warrant used in connection with February 22, 2013 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed February 25, 2013.</u>
<u>4.5</u>	<u>Form of Warrant used in connection with April and May 2013 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed April 26, 2013.</u>
<u>4.6</u>	<u>Form of Warrant used in connection with June 28, 2013 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed July 5, 2013.</u>
<u>4.7</u>	<u>Form of \$0.10 Warrant used in connection with October 22, 2013 private placement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed October 28, 2013.</u>
<u>4.8</u>	

- Warrant issued to Celgene Corporation on November 18, 2013, incorporated by reference to Exhibit 4.12 to the Form 10-K filed December 31, 2013.
- 4.9 Form of Warrant used in connection with November 18, 2013 private placement, incorporated by reference to Exhibit 4.13 to the Form 10-K filed December 31, 2013.
- 4.10 Form of Warrant, dated April 14, 2014, by and between Alliqua, Inc. and certain accredited investors, incorporated by reference to Exhibit 10.2 to the Form 8-K filed April 15, 2014.
- 4.11 Form of Warrant, dated April 3, 2017, by and between Alliqua BioMedical, Inc. and H.C. Wainwright & Co. LLC and its designees, incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed April 4, 2017.
- 10.1+ 2001 Incentive Stock Purchase Plan, incorporated by reference to Exhibit 10.2 to the Form S-8 filed on May 8, 2003.
- 10.2+ Form of Nonstatutory Stock Option Agreement under the 2001 Incentive Stock Purchase Plan, incorporated by reference to Exhibit 10.2 to the Form 10-K/A filed May 16, 2013.
- 10.3+ Form of Incentive Stock Option Agreement under the 2001 Incentive Stock Purchase Plan, incorporated by reference to Exhibit 10.3 to the Form 10-K/A filed May 16, 2013.
- 10.4+ Form of Indemnification Agreement, incorporated by reference to Exhibit 10.2 to the Form 8-K filed January 5, 2011.
- 10.5 Exclusive License Agreement, dated as of July 15, 2011, by and between Noble Fiber Technologies, LLC and Alliqua Biomedical, Inc., incorporated by reference to Exhibit 10.1 to the Form 8-K filed July 20, 2011.
- 10.6 Collateral Assignment of 510(k) Rights, dated as of July 15, 2011, by and between Noble Fiber Technologies, LLC and Alliqua Biomedical, Inc., incorporated by reference to Exhibit 10.1 to the Form 8-K filed July 20, 2011.

- 10.7+ 2011 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.1 to the Form 8-K filed December 20, 2011.
- 10.8 Form of Securities Purchase Agreement, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.1 to the Form 8-K filed February 21, 2012.
- 10.9 Securities Purchase Agreement, dated as of August 14, 2012, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.1 to the Form 8-K filed August 16, 2012.
- 10.10 Securities Purchase Agreement, dated as of November 8, 2012, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.1 to the Form 8-K filed November 14, 2012.
- 10.11+ First Amendment to the 2011 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.1 to the Form 8-K filed December 20, 2012.
- 10.12+ Form of Nonstatutory Stock Option Agreement under the 2011 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.32 to the Form 10-K/A filed May 16, 2013.
- 10.13+ Form of Incentive Stock Option Agreement under the 2011 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.33 to the Form 10-K/A filed May 16, 2013.
- 10.14+ Executive Employment Agreement, dated as of February 4, 2013, between Alliqua, Inc. and David Johnson, incorporated by reference to Exhibit 10.1 to the Form 8-K filed February 7, 2013.
- 10.15+ Indemnification Agreement, dated as of February 4, 2013, in favor of David Johnson, incorporated by reference to Exhibit 10.3 to the Form 8-K filed February 7, 2013.
- 10.16 Securities Purchase Agreement, dated as of February 22, 2013, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.1 to the Form 8-K filed February 25, 2013.
- 10.17 Securities Purchase Agreement, dated as of April 11, 2013, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.1 to the Form 8-K filed April 26, 2013.
- 10.18 Securities Purchase Agreement, dated as of June 28, 2013, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.3 to the Form 8-K filed July 5, 2013.
- 10.19+ Nonqualified Stock Option Agreement, dated September 3, 2013, between Brian Posner and Alliqua, Inc., incorporated by reference to Exhibit 10.2 to the Form 8-K filed September 9, 2013.
- 10.20^ Distributor Agreement, dated September 23, 2013, by and between Sorbion GmbH & Co KG and Alliqua Biomedical, Inc., incorporated by reference to Exhibit 10.5 to the Form 10-Q filed November 12, 2013.
- 10.21^ License, Marketing and Development Agreement, dated as of November 14, 2013, by and between Anthrogenesis Corporation, d/b/a CCT, and Alliqua, Inc., incorporated by reference to Exhibit 10.48 to the Form 10-K filed December 31, 2013.
- 10.22^ Supply Agreement, dated as of November 14, 2013, by and between Anthrogenesis Corporation and Alliqua, Inc., incorporated by reference to Exhibit 10.49 to the Form 10-K filed December 31, 2013.
- 10.23 Stock Purchase Agreement, dated as of November 14, 2013, by and between Celgene Corporation and Alliqua, Inc., incorporated by reference to Exhibit 10.50 to the Form 10-K filed December 31, 2013.
- 10.24 Securities Purchase Agreement, dated as of November 18, 2013, by and among Alliqua, Inc. and certain purchasers set forth therein, incorporated by reference to Exhibit 10.51 to the Form 10-K filed December 31, 2013.
- 10.25 First Amendment to Executive Employment Agreement dated December 20, 2013, by and between Alliqua, Inc. and David Johnson, incorporated by reference to Exhibit 10.1 to the Form 8-K filed December 27, 2013.
- 10.26 Nonqualified Stock Option Agreement dated December 20, 2013, by and between Alliqua, Inc. and David Johnson, incorporated by reference to Exhibit 10.2 to the Form 8-K filed December 27, 2013.
- 10.27+ Form of Restricted Stock Award Agreement under the 2011 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.62 to the Form 10-K filed December 31, 2013.
- 10.28+ Form of Restricted Stock Award Agreement for 2013 Executive Bonuses under the 2011 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.63 to the Form 10-K filed December 31, 2013.
- 10.29+

- Form of Nonqualified Stock Option Agreement (outside of any incentive plan), incorporated by reference to Exhibit 99.8 to the Form S-8 filed January 23, 2014.
- 10.30 Form of Securities Purchase Agreement, dated April 14, 2014, by and between Alliqua, Inc. and certain accredited investors, incorporated by reference to Exhibit 10.1 to the Form 8-K filed April 15, 2014.
- 10.31 Form of Letter Agreement, dated April 11, 2014, by and between Alliqua, Inc. and certain holders of warrants to purchase Common Stock of Alliqua, Inc., incorporated by reference to Exhibit 10.3 to the Form 8-K filed April 15, 2014.
- 10.32+ Alliqua BioMedical, Inc. 2014 Long-Term Incentive Plan, incorporated by reference to Exhibit 10.1 to the Form 8-K filed June 11, 2014.
- 10.33^ Supply Agreement, dated April 10, 2014, by and between Alliqua, Inc. and Anthrogenesis Corporation, d/b/a Celgene Cellular Therapeutics, incorporated by reference to Exhibit 10.4 to the Form 10-Q filed August 11, 2014.
- 10.34^ First Amendment to Supply Agreement, dated April 10, 2014 by and between Alliqua, Inc. and Anthrogenesis Corporation, d/b/a Celgene Cellular Therapeutics, incorporated by reference to Exhibit 10.5 to the Form 10-Q filed August 11, 2014.
- 10.35^ First Amendment to License, Marketing and Development Agreement, dated September 30, 2014, by and between Alliqua, Inc. and Anthrogenesis Corporation, d/b/a Celgene Cellular Therapeutics, incorporated by reference to Exhibit 10.1 to the Form 10-Q filed November 5, 2014.
- 10.36^ Second Amendment to Supply Agreement, dated September 30, 2014, by and between Alliqua, Inc. and Anthrogenesis Corporation, d/b/a Celgene Cellular Therapeutics, incorporated by reference to Exhibit 10.2 to the Form 10-Q filed November 5, 2014.

- Voting Agreement, dated February 2, 2015, by and between Alliqua BioMedical, Inc. and each of the  
10.37 stockholders of Celleration, Inc., as identified therein, incorporated by reference to Exhibit 10.1 to  
Amendment No. 1 to Registration Statement on Form S-4 filed on April 2, 2015.
- Commitment Letter, dated February 2, 2015, by and between Perceptive Credit Opportunities Fund, LP and  
10.38 Alliqua BioMedical, Inc., incorporated by reference to Exhibit 10.2 to Amendment No. 1 to Registration  
Statement on Form S-4 filed on April 2, 2015.
- Side Letter Agreement to Commitment Letter, dated March 10, 2015, by and between Perceptive Credit  
10.39 Opportunities Fund, LP and Alliqua BioMedical, Inc., incorporated by reference to Exhibit 10.3 to  
Amendment No. 1 to Registration Statement on Form S-4 filed on April 2, 2015.
- Second Amendment to the License, Marketing and Development Agreement, dated April 30, 2015, by and  
10.40^ between Alliqua BioMedical, Inc. and Anthrogenesis Corporation, d/b/a Celgene Cellular Therapeutics,  
incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q filed with the Securities and  
Exchange Commission on August 6, 2015.
- First Amendment to the Alliqua BioMedical, Inc. 2014 Long-Term Incentive Plan, incorporated by reference  
10.41+ to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on  
May 6, 2015.
- Form of Incentive Stock Option Agreement under the 2014 Long-Term Incentive Plan, incorporated by  
10.42+ reference to Exhibit 99.3 to the Form S-8 filed August 6, 2015.
- Form of Nonqualified Stock Option Agreement under the 2014 Long-Term Incentive Plan, incorporated by  
10.43+ reference to Exhibit 99.4 to the Form S-8 filed August 6, 2015.
- Form of Restricted Stock Award Agreement under the 2014 Long-Term Incentive Plan, incorporated by  
10.44+ reference to Exhibit 99.5 to the Form S-8 filed August 6, 2015.
- Form of Restricted Stock Unit Agreement under the 2014 Long-Term Incentive Plan, incorporated by  
10.45+ reference to Exhibit 99.6 to the Form S-8 filed August 6, 2015.
- Credit Agreement and Guaranty, dated May 29, 2015, by and among Alliqua BioMedical, Inc., Perceptive  
10.46 Credit Opportunities Fund, LP and those certain subsidiary guarantors party thereto, incorporated by reference  
to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on  
June 1, 2015.
- Pledge and Security Agreement, dated May 29, 2015, by and among Alliqua BioMedical, Inc., Perceptive  
10.47 Credit Opportunities Fund, LP and those certain subsidiary guarantor party thereto, incorporated by reference  
to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on  
June 1, 2015.
- Warrant, dated May 29, 2015, by and between Alliqua BioMedical, Inc. and Perceptive Credit Opportunities  
10.48 Fund, LP, incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K filed with the  
Securities and Exchange Commission on June 1, 2015.
- Employment Agreement, dated June 3, 2015, by and between Alliqua BioMedical, Inc. and Nino Pionati,  
10.49+ incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and  
Exchange Commission on June 9, 2015.
- Employment Agreement, dated June 5, 2015, by and between Alliqua BioMedical, Inc. and Brian Posner,  
10.50+ incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and  
Exchange Commission on June 9, 2015
- Employment Agreement, dated June 5, 2015, by and between Alliqua BioMedical, Inc. and Bradford Barton,  
10.51+ incorporated by reference to Exhibit 10.3 to the Current Report on Form 8-K filed with the Securities and  
Exchange Commission on June 9, 2015.
- First Amendment to Distributor Agreement, dated July 31, 2015, by and between Alliqua BioMedical, Inc.  
10.52 and BSN Medical, Inc., an affiliate of Sorbion GmbH & Co KG, incorporated by reference to Exhibit 10.1 to  
the Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 5,  
2015.
- 10.53



Purchase Agreement, dated June 30, 2016, by and between Alliqua BioMedical, Inc. and BSN medical, Inc., incorporated by reference to Exhibit 10.3 to the Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on August 9, 2016.

10.54 Transition Agreement, dated June 30, 2016, by and between Alliqua BioMedical, Inc. and BSN medical, Inc., incorporated by reference to Exhibit 10.4 to the Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on August 9, 2016.

10.55 Consent Agreement, dated August 25, 2016, by and among Alliqua BioMedical, Inc., certain subsidiaries set forth on the signature pages thereto, and Perceptive Credit Holdings, L.P., incorporated by reference to Exhibit 10.1 to the Quarterly Report on Form 10-Q filed with the Securities and Exchange Commission on November 4, 2016.

10.56 Forbearance and Amendment Agreement, dated January 26, 2017, by and among Alliqua BioMedical, Inc., AquaMed Technologies, Inc. and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 30, 2017.

- Amended Warrant, dated January 26, 2017, by and between Alliqua BioMedical, Inc. and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 30, 2017.
- Form of Securities Purchase Agreement, dated February 27, 2017, by and between Alliqua BioMedical, Inc. and certain accredited investors, incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on February 28, 2017.
- Amendment No. 1 to Forbearance and Amendment Agreement, dated March 7, 2017, by and among Alliqua BioMedical, Inc., AquaMed Technologies, Inc. and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on March 13, 2017.
- Amended Warrant, dated March 7, 2017, by and between Alliqua BioMedical, Inc. and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.2 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on March 13, 2017.
- Amended Warrant, dated April 6, 2017, by and between Alliqua BioMedical, Inc. and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on April 12, 2017.
- Amendment No. 2 to Forbearance and Amendment Agreement, dated April 27, 2017, by and among Alliqua BioMedical, Inc., AquaMed Technologies and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on May 1, 2017
- Amendment to Credit Agreement and Guaranty and Warrant, dated June 1, 2017, by and among Alliqua BioMedical, Inc., AquaMed Technologies, Inc. and Perceptive Credit Holdings, L.P., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 5, 2017
- Second Amendment to the Alliqua BioMedical, Inc. 2014 Long-Term Incentive Plan, effective as of June 23, 2017, incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on June 23, 2017
- Second Forbearance Agreement, dated August 9, 2017, by and among Alliqua BioMedical, Inc., AquaMed Technologies, Inc. and Perceptive Credit Holdings, LP., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on August 10, 2017
- Consent, Forbearance and Amendment Agreement, dated August 31, 2017, by and among Alliqua BioMedical, Inc., AquaMed Technologies, Inc. and Perceptive Credit Holdings, L.P., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on September 5, 2017
- Forbearance and Amendment Agreement, dated February 5, 2018, by and among Alliqua BioMedical, Inc., AquaMed Technologies, Inc. and Perceptive Credit Holdings, L.P., incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed with the Securities and Exchange Commission on February 9, 2018
- 21.1\* List of Subsidiaries
- 23.1\* Consent of Independent Registered Public Accounting Firm to the Form 10-K.
- 31.1\* Certification of Chief Executive Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002
- 31.2\* Certification of Chief Financial Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002
- 32.1\* Certification of Chief Executive Officer Pursuant to Section 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2\* Certification of Chief Financial Officer Pursuant to Section 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- The following materials from the Company's Annual Report on Form 10-K for the year ended December 31, 2017, formatted in XBRL (eXtensible Business Reporting Language), (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to the Consolidated Financial Statements

\* Filed herewith.

\*\*Certain exhibits and schedules have been omitted and the Company agrees to furnish supplementary to the Securities and Exchange Commission a copy of any omitted exhibits upon request.

^ Confidential treatment has been granted with respect to certain portions of this exhibit.

+ Management contract or compensatory plan or arrangement.

**ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

Consolidated Financial Statements

<u>Report of Independent Registered Public Accounting Firm</u>	<u>F-2</u>
<u>Consolidated Balance Sheets as of December 31, 2017 and 2016</u>	<u>F-3</u>
<u>Consolidated Statements of Operations for the years ended December 31, 2017 and 2016</u>	<u>F-4</u>
<u>Consolidated Statements of Stockholders' Equity for the years ended December 31, 2017 and 2016</u>	<u>F-5</u>
<u>Consolidated Statements of Cash Flows for the years ended December 31, 2017 and 2016</u>	<u>F-6</u>
<u>Notes to Consolidated Financial Statements</u>	<u>F-7</u>

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Audit Committee of the  
Board of Directors and Shareholders of  
Alliqua BioMedical, Inc. and Subsidiaries

**Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Alliqua BioMedical, Inc. and Subsidiaries (the “Company”) as of December 31, 2017 and 2016, the related consolidated statements of operations, stockholders’ equity and cash flows for each of the two years in the period ended December 31, 2017, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

**Explanatory Paragraph – Going Concern**

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As more fully described in Note 3, the Company has a significant working capital deficiency, has incurred significant losses and needs to raise additional funds to meet its obligations and sustain its operations. The Company is currently in default of a covenant pertaining to trailing twelve-month revenue and a minimum cash balance requirement under its Credit Agreement and Guaranty with Perceptive Credit Opportunities Fund, L.P. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 3. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

**Basis for Opinion**

These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's financial statements based on our audits. We are a public accounting firm registered with

the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Marcum llp

/s/ Marcum LLP

We have served as the Company's auditor since 2010.

New York, NY

March 2, 2018

**ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS***(in thousands, except share and per share data)*

	December 31, 2017	December 31, 2016
<b>ASSETS:</b>		
Current Assets:		
Cash and cash equivalents	\$ 2,181	\$ 5,580
Accounts receivable, net	3,243	2,453
Inventory, net	1,551	2,152
Prepaid expenses and other current assets	185	735
Current assets of discontinued operations	317	857
Total current assets	7,477	11,777
Improvements and equipment, net	1,563	2,092
Intangible assets, net	22,069	26,605
Goodwill, net	1,659	11,959
Other assets	173	173
Assets of discontinued operations - noncurrent	-	1,893
Total assets	\$ 32,941	\$ 54,499

**LIABILITIES AND STOCKHOLDERS' EQUITY**

Current Liabilities:		
Accounts payable	\$ 1,641	\$ 2,614
Accrued expenses and other current liabilities	4,270	5,224
Contingent consideration, current	-	675
Senior secured term loan, net	10,929	11,541
Warrant liability	130	20
Current liabilities of discontinued operations	-	60
Total current liabilities	16,970	20,134
Contingent consideration, long-term	-	1,141
Deferred tax liability	-	749
Other long-term liabilities	304	385
Total liabilities	17,274	22,409

**Commitments and Contingencies****Stockholders' Equity**

Preferred Stock, par value \$0.001 per share, 1,000,000 shares authorized, no shares issued and outstanding	-	-
Common Stock, par value \$0.001 per share, 95,000,000 shares authorized; 4,986,034 and 2,966,904 shares issued and outstanding as of December 31, 2017 and December	5	3

31, 2016, respectively

Additional paid-in capital	165,672	156,390
Accumulated deficit	(150,010 )	(124,303 )
Total stockholders' equity	15,667	32,090
Total liabilities and stockholders' equity	\$ 32,941	\$ 54,499

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

F-3



**ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS***(in thousands, except share and per share data)*

	Year Ended December 31,	
	2017	2016
Revenue, net of returns, allowances and discounts	\$ 19,565	\$ 16,294
Cost of revenues	6,763	6,051
Gross profit	12,802	10,243
Operating expenses		
Selling, general and administrative	28,090	35,325
Royalties	820	1,093
Research and product development	121	859
Milestone expense to licensor	-	1,000
Acquisition-related	(365)	) 2,959
Change in fair value of contingent consideration liability	35	(10,065)
Impairment charges	10,300	10,895
Total operating expenses	39,001	42,066
Loss from operations	(26,199)	) (31,823)
Other (expense) income		
Interest expense	(2,282)	) (2,541)
Change in fair value of warrant liability	692	841
Warrant modification expense	(803)	) -
Loss on early extinguishment of debt, net	(214)	) (373)
Other income	206	142
Total other expense	(2,401)	) (1,931)
Loss from continuing operations before tax	(28,600)	) (33,754)
Income tax benefit	743	715
Loss from continuing operations	(27,857)	) (33,039)
Discontinued operations:		
Income from discontinued operations, net of tax of \$0 for the years ended December 31, 2017 and 2016	454	1,485
Gain on sale of assets, net of tax of \$0 for the years ended December 31, 2017 and 2016	1,696	3,311

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Income from discontinued operations, net of tax	2,150	4,796
Net loss	\$(25,707)	\$(28,243)
Net loss per basic and diluted common share:		
Loss from continuing operations	\$(6.49)	\$(11.81)
Income from discontinued operations	0.11	0.53
Gain on sale of assets	0.40	1.18
Total from discontinued operations	0.51	1.71
Net loss per basic and diluted common share	\$(5.98)	\$(10.10)
Weighted average shares used in computing net loss per basic and diluted common share	4,291,600	2,796,563

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

**ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY***(in thousands, except for share and per share data)*

	Common Stock Shares	Amount	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
Balance, December 31, 2015	2,766,891	\$ 3	\$ 148,484	\$ (96,060 )	\$ 52,427
Stock-based compensation (A)	101,653	-	5,336	-	5,336
Issuance of common stock in connection with the contingent consideration of the Celleration, Inc. acquisition (B)	98,594	-	2,572	-	2,572
Net settlement on vesting of restricted stock awards	(234 )	-	(2 )	-	(2 )
Net loss	-	-	-	(28,243 )	(28,243 )
Balance, December 31, 2016	2,966,904	\$ 3	\$ 156,390	\$ (124,303 )	\$ 32,090
Issuance common stock for cash, net of issuance costs of \$695	1,639,825	2	5,847		5,849
Stock-based compensation (C)	181,936	-	2,393		2,393
Issuance of common stock in connection with the contingent consideration of the Celleration, Inc. acquisition (D)	101,243	-	675		675
Issuance of common stock in connection with the contingent consideration of the Choice Therapeutics acquisition (E)	131,579	-	500		500
Net settlement on vesting of restricted stock awards	(35,453 )	-	(133 )		(133 )
Net loss				(25,707 )	(25,707 )
Balance, December 31, 2017	4,986,034	\$ 5	\$ 165,672	\$ (150,010 )	\$ 15,667

(A) Includes \$474,000 that was part of accrued expenses as of December 31, 2015, which was credited to equity upon the issuance of 32,456 restricted common shares during the year ended December 31, 2016.

(B) Includes \$2.6 million that was part of contingent consideration as of December 31, 2015, which was credited to equity upon the issuance of 98,594 common shares during the year ended December 31, 2016.

(C) Includes \$374,000 that was part of accrued expenses as of December 31, 2016, which was credited to equity upon the issuance of 60,000 restricted common shares during the year ended December 31, 2017.

(D) Includes \$675,000 that was part of contingent consideration as of December 31, 2016, which was credited to equity upon the issuance of 101,243 common shares during the year ended December 31, 2017.

(E) Includes \$500,000 that was part of contingent consideration as of December 31, 2016, which was credited to equity upon the issuance of 131,579 common shares during the year ended December 31, 2017.

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

**ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS***(in thousands)*

	Year Ended December 31,	
	2017	2016
Operating Activities		
Net loss	\$ (25,707 )	\$ (28,243 )
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	5,415	4,162
Amortization of deferred lease incentive	(45 )	(42 )
Lease incentive	-	267
Impairment charges	10,300	10,895
Deferred income tax expense	(743 )	(715 )
Provision for doubtful accounts	122	38
Reserve for note receivable	(650 )	1,020
Provision for excess and slow moving inventory	68	(58 )
Stock-based compensation expense	2,020	4,863
Deferred rent	2	84
Accrued interest receivable	-	(19 )
Amortization of debt issuance and discount costs	824	841
Loss on early extinguishment of debt	182	321
Warrant modification expense	803	-
Change in fair value of warrant liability	(692 )	(841 )
Fair value adjustment of contingent consideration liability	35	(10,065 )
Gain on sale of assets	(1,696 )	(3,311 )
Changes in operating assets and liabilities:		
Accounts receivable	(621 )	(281 )
Inventory	792	(112 )
Prepaid expenses and other assets	550	207
Accounts payable	(1,004 )	(26 )
Accrued expenses and other current liabilities	(627 )	2,680
Net Cash Used in Operating Activities	(10,672 )	(18,335 )
Investing Activities		
Proceeds from sale of assets	3,411	4,103
Purchase of improvements and equipment	(179 )	(893 )
Issuance of bridge loan	(350 )	(1,000 )
Proceeds from bridge loan	1,000	-
Net Cash Provided by Investing Activities	3,882	2,210
Financing Activities		
Contingent purchase price payments	(675 )	(2,573 )

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Repayment of long-term debt	(1,618 )	(1,748 )
Loss on early extinguishment of debt	(32 )	(52 )
Net proceeds from issuance of common stock	5,849	-
Payment of withholding taxes related to stock-based employee compensation	(133 )	(2 )
Net Cash Provided by (Used in) Financing Activities	3,391	(4,375 )
Net Decrease in Cash and Cash Equivalents	(3,399 )	(20,500 )
<b>Cash and Cash Equivalents - Beginning of year</b>	5,580	26,080
<b>Cash and Cash Equivalents - End of year</b>	\$ 2,181	\$ 5,580
Supplemental Disclosure of Cash Flows Information		
Cash paid during the period for:		
Interest	\$ 1,008	\$ 1,599
Non-cash investing and financing activities:		
2016 Accrued bonus awarded in equity	\$ 374	\$ -
2015 Accrued bonus awarded in equity	-	474
Common stock issued for contingent purchase price payments	1,175	2,573

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

## **ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES**

### **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

#### **1. Description of Business and Basis of Presentation**

Alliqua BioMedical, Inc. (the “Company”) is a regenerative technologies company that commercializes differentiated regenerative medical products which assist the body in the repair of human tissue.

On January 5, 2018, the Company entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Celularity, Inc. (“Celularity”) pursuant to which the Company agreed to sell substantially all of its assets to Celularity (the “Asset Sale Transaction”), including certain assets comprising its MIST, Biovance and Interfyl Product lines (the “Purchased Assets”). As consideration for the Purchased Assets, Celularity has agreed to pay the Company \$29 million in cash. No debt or significant liabilities will be assumed by Celularity in the Asset Sale.

Under the terms of the Asset Purchase Agreement, the Company will retain certain specified assets, including, among other things, cash, accounts receivable, and its hydrogel contract manufacturing business, including its SilverSeal and Hydress product lines.

The transactions contemplated by the Asset Purchase Agreement must be approved by the affirmative vote of a majority of the voting power of issued and outstanding shares of the Company’s common stock. In addition, to the receipt of the approval of the Company’s stockholders, each party’s obligation to consummate the Asset Sale Transaction is conditioned upon certain other customary closing conditions.

The Company’s operations intended to be sold under the Asset Purchase Agreement have not been reclassified to discontinued operations since they are classified as Held for Use. These operations will be presented in continuing operations until the Asset Purchase Agreement is approved by the Company’s stockholders. Upon stockholder approval of the Asset Purchase Agreement, these operations will be reclassified to discontinued operations.

#### ***Principles of Consolidation***

The accompanying consolidated financial statements include the financial statements of the Company and its wholly-owned subsidiary, AquaMed Technologies, Inc. All significant inter-company transactions and accounts have been eliminated in consolidation.

### ***Reclassifications***

Certain amounts in prior periods have been reclassified to conform to the current year presentation. Such reclassifications did not have a material effect on the Company's financial condition or results of operations as previously reported.

### ***Reverse Stock Split***

The Company effected a 1-for-10 reverse stock split of its outstanding common stock on October 5, 2017. The accompanying consolidated financial statements and accompanying notes to the consolidated financial statements give retroactive effect to the reverse stock split for all periods presented. The shares of common stock retained a par value of \$0.001 per share. Accordingly, stockholders' equity reflects the reverse stock split by reclassifying from common stock to additional paid-in capital an amount equal to the par value of the decreased shares resulting from the reverse stock split.

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

### ***Use of Estimates in the Financial Statements***

The preparation of the consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. These estimates and assumptions include valuing equity securities and derivative financial instruments issued in financing transactions, allowance for doubtful accounts, inventory reserves, deferred taxes and related valuation allowances, and the fair values of long lived assets, intangibles, goodwill and contingent consideration. Actual results could differ from the estimates.

### ***Cash and Cash Equivalents***

The Company considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents. The Company's balance of cash and cash equivalents at December 31, 2017 and 2016 consisted



principally of bank deposits. From time to time, the Company's cash account balances may be uninsured or in deposit accounts that exceed Federal Deposit Insurance Corporation guarantee limit. The Company reduces its exposure to credit risk by maintaining its cash deposits with major financial institutions and monitoring their credit ratings.

F-7

### ***Trade Accounts Receivable***

Trade accounts receivable are stated at the amount the Company expects to collect and do not bear interest. The Company evaluates the collectability of accounts receivable based on a combination of factors. In circumstances where a specific customer is unable to meet its financial obligations to the Company, a provision to the allowances for doubtful accounts is recorded against amounts due to reduce the net recognized receivable to the amount that is reasonably expected to be collected. For all other customers, a provision to the allowances for doubtful accounts is recorded based on factors including the length of time the receivables are past due, the current business environment and the Company's historical experience. Provisions to the allowances for doubtful accounts are recorded to selling, general and administrative expenses. Account balances are charged off against the allowance when it is probable that the receivable will not be recovered. The allowance for doubtful accounts was approximately \$307,000 and \$213,000 as of December 31, 2017 and 2016, respectively.

### ***Inventory***

Inventory is stated at the lower of cost, the value determined by the first-in, first-out method, or net realizable value. At each balance sheet date, the Company evaluates inventories for excess quantities, obsolescence or shelf life expiration. This evaluation includes analysis of historical sales levels by product, projections of future demand, the risk of technological or competitive obsolescence for products, general market conditions, and a review of the shelf life expiration dates for products. To the extent that management determines there are excess or obsolete inventory or quantities with a shelf life that is too near its expiration for the Company to reasonably expect that it can sell those products prior to their expiration, the Company adjusts the carrying value to estimated net realizable value.

### ***Improvements and Equipment***

Improvements and equipment are recorded at cost. Depreciation of equipment is computed utilizing the straight-line method over the estimated useful lives of the assets. Amortization of leasehold improvements is computed utilizing the straight-line method over the lesser of the lease term or the estimated useful life. Repairs and maintenance costs are expensed as incurred. The cost of major additions and improvements is capitalized, while maintenance and repair costs that do not improve or extend the lives of the respective assets are charged to operations as incurred.

### ***Goodwill and Other Indefinite-Lived Intangible Assets***

The Company records goodwill and other indefinite-lived assets in connection with business combinations. Goodwill, which represents the excess of acquisition cost over the fair value of the net tangible and intangible assets of acquired companies, is not amortized. Indefinite-lived assets are stated at fair value as of the date acquired in a business combination.

The Company assesses the recoverability of goodwill and certain indefinite-lived intangible assets annually in the fourth quarter and between annual tests if an event occurs or circumstances change that would indicate the carrying amount may be impaired. Impairment testing for goodwill is done at a reporting unit level. Under Financial Accounting Standards Board (“FASB”) guidance for goodwill and intangible assets, a reporting unit is defined as an operating segment or one level below the operating segment, called a component. However, two or more components of an operating segment will be aggregated and deemed a single reporting unit if the components have similar economic characteristics. The Company operates as one reporting unit.

Authoritative accounting guidance allows the Company to first assess qualitative factors to determine whether it is necessary to perform the more detailed two-step quantitative goodwill impairment test. The Company performs the quantitative test if its qualitative assessment determined it is more likely than not that a reporting unit’s fair value is less than its carrying amount. The Company may elect to bypass the qualitative assessment and proceed directly to the quantitative test for any reporting unit or asset. The quantitative goodwill impairment test, if necessary, is a two-step process. The first step is to identify the existence of a potential impairment by comparing the fair value of a reporting unit (the estimated fair value of a reporting unit is usually calculated using a discounted cash flow model) with its carrying amount, including goodwill. If the fair value of a reporting unit exceeds its carrying amount, the reporting unit’s goodwill is considered not to be impaired and performance of the second step of the quantitative goodwill impairment test is unnecessary. However, if the carrying amount of a reporting unit exceeds its fair value, the second step of the quantitative goodwill impairment test is performed to measure the amount of impairment loss to be recorded, if any. The second step of the quantitative goodwill impairment test compares the implied fair value of the reporting unit’s goodwill with the carrying amount of that goodwill. If the carrying amount of the reporting unit’s goodwill exceeds its implied fair value, an impairment loss is recognized in an amount equal to that excess. The implied fair value of goodwill is determined using the same approach as employed when determining the amount of goodwill that would be recognized in a business combination. That is, the fair value of the reporting unit is allocated to all of its assets and liabilities as if the reporting unit had been acquired in a business combination and the fair value was the purchase price paid to acquire the reporting unit.

The Company proceeded directly to the quantitative analysis considering the consideration to be received and the assets to be sold under the Asset Purchase Agreement. As a result of this test, the Company's goodwill was determined to be impaired and an impairment charge of \$10.3 million was recorded for the year ended December 31, 2017.

The Company's indefinite lived intangible asset related to the MIST Therapy tradename was impaired and an impairment charge of \$1.7 million was recorded for the year ended December 31, 2016. The impairment charge related to the tradename was calculated based on the fair value of the MIST Therapy tradename as compared to the carrying value of the MIST Therapy tradename as of December 31, 2016. There were no long-lived asset impairment charges recorded during the year ended December 31, 2017. At December 31, 2017 the remaining recorded goodwill was \$1,659,000 compared to \$12.0 million at December 31, 2016. The changes in the carrying amount of goodwill for the years ended December 31, 2017 and 2016, are as follows (in thousands):

	Goodwill
Balance as of December 31, 2015	\$21,166
Impairment loss	(9,207 )
Balance as of December 31, 2016	\$11,959
Impairment loss	(10,300 )
Balance as of December 31, 2017	\$1,659

### ***Long-Lived Assets***

Long-lived assets, such as property and equipment, and intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company's long-lived intangible assets primarily consist of developed technology, customer lists/relationships, non-compete agreements, trade names and trademarks and are amortized ratably over a range of one to ten years which approximates customer attrition rate and technology obsolescence. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized of the amount by which the carrying amount of the asset exceeds the fair value of the asset.

The Company continually evaluates whether events or changes in circumstances might indicate that the remaining estimated useful life of long-lived assets may warrant revision, or that the remaining balance may not be recoverable.

When factors indicate that long-lived assets should be evaluated for possible impairment, the Company uses an estimate of the related undiscounted cash flows in measuring whether the long-lived asset should be written down to fair value. Measurement of the amount of impairment is based on generally accepted valuation methodologies, as deemed appropriate. The factors used to determine fair value are subject to management's judgement and expertise and include, but are not limited to, the present value of future cash flows, net of estimated operating costs, anticipated capital expenditures and various discount rates commensurate with the risk and current market conditions associated with realizing the expected cash flows projected.

Due to the Asset Purchase Agreement, the Company expects that it is more likely than not that its long-lived asset group related to the Purchased Assets will be sold or otherwise disposed of significantly before the end of its previously estimated useful life. The Company, therefore, tested its long-lived assets for recoverability as of December 31, 2017. These long-lived assets consist of property, plant and equipment and intangible assets subject to amortization.

The expected consideration under the Asset Purchase Agreement for the sale of the long-lived assets approximate the net book value of these assets at December 31, 2017, therefore, no impairment charge was recorded for long-lived assets during the year ended December 31, 2017.

There were no long-lived asset impairment charges recorded during the year ended December 31, 2016, other than the impairment of the MIST Therapy tradename, described above and in Note 9 - *Intangible Assets*.

#### ***Fair Value of Financial Instruments***

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable and accounts payable and accrued expenses approximate fair value based on the short-term maturity of these instruments.

Fair value is defined as the price that would be received upon selling an asset or the price paid to transfer a liability on the measurement date. It focuses on the exit price in the principal or most advantageous market for the asset or liability in an orderly transaction between willing market participants. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair values are as follows:

Level 1: Observable prices in active markets for identical assets and liabilities.

Level 2: Observable inputs other than quoted prices in active markets for identical assets and liabilities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities.

### ***Revenue Recognition***

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, title and risk of loss have passed to the customer, there is a fixed or determinable sales price, and collectability of that sales price is reasonably assured. The Company also recognizes revenue under a variety of rental programs of the MIST Therapy system, which is recognized over the term of the rental agreement.

### ***Cost of Goods Sold and Selling, General and Administrative Expenses***

Costs associated with the production and procurement of product are included in cost of goods sold, including shipping and handling costs such as inbound freight costs, purchasing and receiving costs, inspection costs and other product procurement related charges. All other expenses are included in selling, general and administrative expenses, as the predominant expenses associated therewith are general and administrative in nature.

### ***Advertising***

Advertising costs are expensed as incurred and are included in selling, general and administrative expenses. Advertising expenses for the years ended December 31, 2017 and 2016 were approximately \$1.4 million and \$2.4

million, respectively.

### ***Shipping and Handling***

Amounts billed to customers for shipping and handling are included in revenues. The related shipping and freight charges incurred by the Company are included in cost of goods sold and were not material for either the years ended December 31, 2017 or 2016.

### ***Research and Development***

All research and product development costs are expensed as incurred. For the years ended December 31, 2017 and 2016, the Company incurred research and development costs of approximately \$121,000 and \$859,000, respectively, related to a randomized controlled trial for its Biovance product in chronic diabetic foot wounds.

### ***Income Taxes***

The Company accounts for income taxes pursuant to the asset and liability method which requires us to recognize current tax liabilities or receivables for the amount of taxes we estimate are payable or refundable for the current year and deferred tax assets and liabilities for the expected future tax consequences attributable to temporary differences between the financial statement carrying amounts and their respective tax bases of assets and liabilities and the expected benefits of net operating loss and credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in operations in the period enacted. A valuation allowance is provided when it is more likely than not that a portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income and the reversal of deferred tax liabilities during the period in which related temporary differences become deductible.

The Company adopted the provisions of Accounting Standards Codification Topic 740 ("ASC 740") related to the accounting for uncertainty in income taxes recognized in an enterprise's consolidated financial statements. ASC 740 prescribes a comprehensive model for the financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns.

The tax benefit positions taken or expected to be taken in the Company's income tax returns are recognized in the financial statements if such positions are more likely than not of being sustained upon examination by taxing authorities. Differences between tax positions taken or expected to be taken in a tax return and the benefit recognized and measured pursuant to the interpretation are referred to as "unrecognized benefits". A liability is recognized (or amount of net operating loss carryover or amount of tax refundable is reduced) for an unrecognized tax benefit because it represents an enterprise's potential future obligation to the taxing authority for a tax position that was not recognized as a result of applying the provisions of ASC 740. Interest costs and related penalties related to unrecognized tax benefits are required to be calculated, if applicable. The Company's policy is to classify assessments, if any, for tax related interest as interest expense and penalties as selling, general and administrative expenses. No interest or penalties were recorded during the years ended December 31, 2017 and 2016. As of December 31, 2017 and 2016, no liability for unrecognized tax benefits was required to be reported. The Company does not expect any significant changes in its unrecognized tax benefits in the next year.

### ***Common Stock Purchase Warrants***

The Company assesses classification of common stock purchase warrants at each reporting date to determine whether a change in classification between assets and liabilities or equity is required. The Company's free-standing derivatives consist of warrants to purchase common stock that were issued pursuant to a Securities Purchase Agreement on November 8, 2012 and pursuant to a Credit Agreement on May 29, 2015. The November 8, 2012 warrants expired in November 2017. The Company evaluated the common stock purchase warrants to assess their proper classification in the consolidated balance sheet and determined that the common stock purchase warrants contain exercise reset provisions. Accordingly, the outstanding portion of these instruments have been classified as warrant liabilities in the accompanying consolidated balance sheets as of December 31, 2017 and 2016. The Company re-measures warrant liabilities at each reporting and exercise date, with changes in fair value recognized in earnings for each reporting period.

### ***Stock-Based Compensation***

The Company measures the cost of services received in exchange for an award of equity instruments based on the fair value of the award. For employees and directors, the fair value of the award is measured on the grant date and for non-employees, the fair value of the award is generally re-measured on interim financial reporting dates and vesting dates until the service period is complete. The fair value amount is then recognized over the period services are required to be provided in exchange for the award, usually the vesting period. The Company recognizes stock-based compensation expense on a graded-vesting basis over the requisite service period for each separately vesting tranche of each award. Stock-based compensation expense is reflected within cost of revenues and operating expenses in the consolidated statements of operations. The Company recognizes stock-based compensation expense for awards with performance conditions if and when the Company concludes that it is probable that the performance condition will be achieved. The Company reassesses the probability of vesting at each reporting period for awards with performance conditions and adjusts stock-based compensation expense based on its probability assessment.



### ***Recent Accounting Standards***

On December 22, 2017 the U.S. government enacted significant changes to federal tax law following the passage of the Tax Cuts and Jobs Act (“the Act”). Following the enactment of the Act, the SEC staff issued Staff Accounting Bulletin No. 118, *Income Tax Accounting Implications of the Tax Cuts and Jobs Act* (“SAB 118”). The Company follows the guidance in SAB 118, which provides additional clarification regarding the application of US GAAP in situations where the Company does not have the necessary information available, prepared, or analyzed in reasonable detail to complete the accounting for certain income tax effects of the Act for the reporting period in which the Act was enacted. SAB 118 provides for a measurement period beginning in the reporting period that includes the Act’s enactment date and ending when the Company has obtained, prepared, and analyzed the information needed in order to complete the accounting requirements but in no circumstances, should the measurement period extend beyond one year from the enactment date. The Company has evaluated the Act and, based on the information available, recorded provisional amounts as the impacts can be reasonably estimated. These impacts are disclosed in “Note 15 – Income Taxes” in the Notes accompanying the audited Consolidated Financial Statements.

In May 2017, the FASB issued ASU 2017-09, Compensation-Stock Compensation (Topic 718) Scope of Modification Accounting (“ASU 2017-09”). This ASU clarifies which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The standard is effective for the Company on January 1, 2018, with early adoption permitted. The impact of this new standard will depend on the extent and nature of future changes to the terms of Company’s share-based payment awards.

In January 2017, the FASB issued Accounting Standards Update (ASU) 2017-04: “Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment” (“ASU 2017-04”), which removes Step 2 from the goodwill impairment test. It is effective for annual and interim periods beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment test performed with a measurement date after January 1, 2017. The Company adopted ASU 2017-04 during the year ended December 31, 2017.

In January 2017, the FASB issued ASU 2017-01 “Business Combinations (Topic 805): Clarifying the Definition of a Business”, which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions or disposals of assets or businesses. The standard introduces a screen for determining when assets acquired are not a business and clarifies that a business must include, at a minimum, an input and a substantive process that contribute to an output to be considered a business. This standard is effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period. The Company does not expect this new guidance to have a material impact on its financial position, results of operations or financial statement disclosures.

In December 2016, the FASB issued ASU 2016-18 “Statement of Cash Flows (Topic 230): Restricted Cash (a consensus of the FASB Emerging Issues Task Force,” which clarifies the presentation requirements of restricted cash within the statement of cash flows. The changes in restricted cash and restricted cash equivalents during the period should be included in the beginning and ending cash and cash equivalents balance reconciliation on the statement of cash flows. When cash, cash equivalents, restricted cash or restricted cash equivalents are presented in more than one line item within the statement of financial position, an entity shall calculate a total cash amount in a narrative or tabular format that agrees to the amount shown on the statement of cash flows. Details on the nature and amounts of restricted cash should also be disclosed. This standard is effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period. The Company does not expect this new guidance to have a material impact on its financial position or results of operations.

In August 2016, the FASB issued ASU No. 2016-15, “Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments.” ASU No. 2016-15 clarifies and provides specific guidance on eight cash flow classification issues that are not currently addressed by current GAAP and thereby reduce the current diversity in practice. ASU No. 2016-15 is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after December 15, 2017, with early application permitted. This guidance is applicable to the Company’s fiscal year beginning January 1, 2018. The Company does not anticipate that this guidance will have a material impact on its consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting” (“ASU 2016-09”). The standard is intended to simplify several areas of accounting for share-based compensation arrangements, including the income tax impact, classification on the statement of cash flows and forfeitures. ASU 2016-09 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016, which for the Company will commence with the year beginning January 1, 2018, with early adoption permitted commencing January 1, 2017. The Company does not expect that this guidance will have a material impact on its consolidated financials.

In February 2016, the FASB issued Accounting Standards Update 2016-02, “Leases (Topic 842)” (“ASU 2016-02”). The standard requires a lessee to recognize assets and liabilities on the balance sheet for leases with lease terms greater than 12 months. The standard is effective for annual reporting periods beginning after December 15, 2018, which for

the Company will commence with the year beginning January 1, 2019, with early application permitted. The adoption will require a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest period presented. The Company is currently evaluating the standard to determine the impact of the adoption on the consolidated financial statements.

In November 2015, the FASB issued Accounting Standards Update 2015-17, “Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes” (“ASU 2015-07”), an update to accounting guidance to simplify the presentation of deferred income taxes. The guidance requires an entity to classify all deferred tax liabilities and assets, along with any valuation allowance, as noncurrent in the balance sheet. The guidance is effective for public companies with annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is permitted. The Company has elected to early adopt ASU 2015-17 during the year ended December 31, 2015 with retrospective application. The adoption of ASU 2015-17 did not have a material impact on the Company’s consolidated financial statements.

In May 2014 the FASB issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes all existing revenue recognition requirements, including most industry-specific guidance. This new standard requires a company to recognize revenue when it transfers goods or services to customers in an amount that reflects the consideration that the company expects to receive for those goods or services. The FASB subsequently issued amendments to ASU No. 2014-09 that have the same effective date and transition date. These new standards became effective for us on January 1, 2018, and will be adopted using the modified retrospective method through a cumulative-effect adjustment, if any, directly to retained earnings as of that date. The Company has performed a review of these new standards as compared to our current accounting policies for its product and contract manufacturing revenues. As of December 31, 2017, the Company has not identified any accounting changes that would materially impact the amount of reported revenues with respect to our product and contract manufacturing revenues.

### 3. Going Concern

The Company's financial statements are prepared using accounting principles generally accepted in the United States of America applicable to a going concern that contemplates the realization of assets and liquidation of liabilities in the normal course of business.

As of December 31, 2017, the Company had a cash balance of \$2.2 million. The Company has experienced recurring losses since its inception. The Company incurred a net loss of \$25.7 million and used \$10.7 million in cash from operations for the year ended December 31, 2017, and had an accumulated deficit of \$150.0 million as of December 31, 2017.

The Company is currently in default of a covenant pertaining to trailing twelve-month revenue under its Credit Agreement and Guaranty (the "Credit Agreement") with Perceptive Credit Opportunities Fund, L.P. as a result of its failure to achieve \$24,600,000, \$27,200,000, \$30,300,000, \$33,800,000 and \$37,800,000 of gross revenue for the twelve-month periods ended December 31, 2016, March 31, 2017, June 30, 2017, September 30, 2017 and December 31, 2017, respectively. The Company is also currently in default of a minimum cash balance requirement under the Credit Agreement due to the Company having a cash balance of less than \$2,000,000. As of the date hereof, the lender has agreed to forbear from exercising any rights and remedies related to each such event of default until the earlier of April 30, 2018 or the termination of the Asset Purchase Agreement with Celularity. In addition, on December 1, 2017, the Company received notice from Celularity that it is in material breach of its License, Marketing and Development Agreement with Celularity (or its affiliates) dated as of November 14, 2013, as amended from time to time (the "License Agreement") and its Supply Agreements with Celularity (or its affiliates), dated as of April 15, 2016 and November 14, 2013, respectively, as amended from time to time (the "Supply Agreements") for failure to purchase the required amounts of materials under the Supply Agreements and failure to use commercially reasonable best efforts to undertake development activities for the licensed products under the License Agreement.

Without receipt of the cash consideration from Celularity, the Company will not be able to repay its indebtedness under the Credit Agreement and will be unable to purchase materials under the Supply Agreements. The lender under the Credit Agreement may pursue the rights and remedies available to it under the Credit Agreement including, but not limited to, declaring all or any portion of the outstanding principal amount to be immediately due and payable, imposing a default rate of interest as specified in the Credit Agreement, or pursuing the lender's rights and remedies as a secured party under the Uniform Commercial Code as a secured lender. In addition, the lender has a lien on substantially all of the Company's assets and, as a result of the default, may seek to foreclose on some or substantially all of its assets. If the Company does not consummate the Asset Sale Transaction with Celularity and transfer the License Agreement and Supply Agreements to Celularity as part of the Purchased Assets, the Company may face termination or litigation with respect to the Supply Agreements and the License Agreement. If the Company was to lose its rights to license Biovance, Interfyl or other products from Celularity under the License Agreement, it will have a material adverse effect on its business, financial condition and results of operations which could force the Company to file for bankruptcy, if it is not successful in obtaining the level of financing needed for its operations.

Such action could hinder the Company's ability to recover the remaining carrying value of some or all of its intangible assets including goodwill that aggregated approximately \$23.7 million at December 31, 2017.

These factors raise substantial doubt as to the Company's ability to continue as a going concern within one year from the date of this filing. The ability of the Company to continue as a going concern is dependent upon the Company's successful efforts to consummate the Asset Sale Transaction or raise additional capital.

The consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded assets and liabilities that might be necessary should the Company be unable to continue as a going concern.

#### 4. Net Loss Per Common Share

Basic loss per share data for each period presented is computed using the weighted-average number of shares of common stock outstanding during each such period. Diluted loss per share data is computed using the weighted-average number of common and dilutive common-equivalent shares outstanding during each period. Dilutive common-equivalent shares consist of: (a) shares that would be issued upon the exercise of stock options and warrants, computed using the treasury stock method; and (b) shares of non-vested restricted stock.

The following securities are excluded from the calculation of weighted average dilutive common shares because their inclusion would have been anti-dilutive:

	As of December 31,	
	2017	2016
Stock options	809,586	719,929
Warrants	478,330	336,541
Non-vested restricted stock	189,674	147,023
Total	1,477,590	1,203,493

## 5. Discontinued Operations

### *Asset Sales*

In order to add capital and to focus on future investments on commercializing its own regenerative technologies on August 31, 2017, the Company entered into an Asset Purchase Agreement (“the Argentum Purchase Agreement”) with Argentum Medical, LLC. (“Argentum”) whereby the Company agreed to sell to Argentum all of the Company’s rights, including (i) all distribution rights, exclusivity rights, intellectual property rights and marketing rights to the TheraBond product line and (ii) the unsold inventory of TheraBond products and work in process previously purchased by the Company in existence as of the closing, which occurred upon execution and delivery of the Argentum Purchase Agreement. In consideration for the sale of the TheraBond product line and the unsold TheraBond inventory to Argentum by the Company, Argentum agreed to pay (i) \$3.6 million for the TheraBond product line and certain other agreements between the parties and (ii) up to \$112,000 for the unsold TheraBond inventory upon the Company’s completion of its obligations to deliver all remaining and qualifying unsold TheraBond inventory, as specified in the Argentum Purchase Agreement. Of the \$3.6 million of consideration, \$300,000 is deposited in an indemnity escrow account under standard terms and conditions. This amount is classified under current assets of discontinued operations on the Company’s balance sheet as of December 31, 2017.

Additionally, effective June 30, 2016, the Company entered into a purchase agreement with BSN medical, Inc. (“BSN”) whereby the Company agreed to sell to BSN all of the Company’s rights, including all distribution rights, exclusivity rights, intellectual property rights and marketing rights to the sorbion product line pursuant to its distribution agreement with Sorbion GmbH & Co KG.

Summarized operating results of discontinued operations for the years ended December 31, 2017 and 2016 are presented in the following table (in thousands):

	Years Ended December 31,	
	2017	2016
Revenue, net of returns, allowances and discounts	\$ 1,242	\$ 3,655
Cost of revenues	396	1,140
Gross profit	846	2,515
Selling, general and administrative	392	1,030
Income from discontinued operations, net of tax	\$ 454	\$ 1,485

Non-cash amortization expense of \$185,000 and \$334,000 is included in selling, general and administrative expense for the years ended December 31, 2017 and 2016, respectively.

F-14

During the year ended December 31, 2017, the Company recorded a gain of approximately \$1.7 million (net of tax of \$0) on the sale of the assets related to the Argentum Purchase Agreement, pursuant to the following (in thousands):

Proceeds from sale		
Consideration for inventory	\$ 112	
Consideration for intangible assets	3,600	
Total Consideration		3,712
Less: Net book value of assets sold to Argentum		
Inventory, net	(307 )	
Intangibles, net	(1,709)	
Total net book value of assets		(2,016)
Gain on sale of assets		\$1,696

During the year ended December 31, 2016, the Company recorded a gain of approximately \$3.3 million (net of tax of \$0) on the sale of the assets related to the purchase agreement with BSN, pursuant to the following (in thousands):

Proceeds from sale		
Consideration for inventory	\$ 603	
Consideration for intangible assets	3,500	
Total Consideration		4,103
Less: Net book value of assets sold BSN		
Inventory, net	(603 )	
Intangibles, net	(189 )	
Total net book value of assets		(792 )
Gain on sale of assets		\$3,311

Summarized assets and liabilities of discontinued operations are presented in the following table (in thousands):

	December 31 2017	December 31, 2016
Accounts receivable, net	\$ 17	\$ 307
Escrow	300	-
Inventory, net	-	550
Total current assets	317	857
Intangible assets, net	-	1,893
Total assets	317	2,750
Accounts payable	-	19
Accrued expenses and other current liabilities	-	41



Total current liabilities	\$ -	\$ 60
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On June 30, 2016, the Company entered into a ninety-day transition services agreement with BSN (“Transition Agreement”). Under the Transition Agreement, the Company was required to perform certain services related to the communication with distributors, wholesalers and customers in respect of transition of the business to BSN, as specified in the Transition Agreement. As compensation, BSN paid the Company \$100,000 for the services completed during the year ended December 31, 2016. This compensation was recognized over the service period and is included in other income for the year ended December 31, 2016.

On August 31, 2017, the Company entered into a ninety-day transition services agreement with Argentum (“Transition Agreement”). Under the Transition Agreement, the Company is required to perform certain services related to the communication with distributors, wholesalers and customers in respect of transition of the TheraBond product line to Argentum, as specified in the Transition Agreement. As compensation, Argentum paid the Company \$200,000 for the services completed during the period from the closing of the purchase for three months ended November 30, 2017. This compensation was recognized over the service period and is included in other income for the year ended December 31, 2017.

## 6. Termination of Merger Agreement

On October 5, 2016, the Company entered into a merger agreement to acquire the business of Soluble Systems, LLC (“Soluble”) through a series of transactions. On February 27, 2017, the Company terminated this agreement.

In connection with the merger agreement to acquire the business of Soluble, the Company provided Soluble with bridge loans in the form of subordinated promissory notes totaling approximately \$1.4 million. The Company advanced Soluble \$1.0 million during the year ended December 31, 2016 and \$0.4 million on January 30, 2017. Pursuant to the terms of the merger agreement, the amount was to be repaid in full upon termination of the agreement. As of December 31, 2016, the Company had provided for a full reserve for the amount that had been advanced to Soluble as of that date.

On October 27, 2017, the Company received \$1 million under an agreement with Soluble in connection with amounts advanced to Soluble by the Company. With the receipt of this \$1 million, the Company acknowledged that all amounts due to the Company from Soluble are paid in full. During the year ended December 31, 2017, the Company recorded a reduction in acquisition-related expenses of \$365,000 which consisted of the recovery of bad debt expense of \$650,000, offset by approximately \$285,000 of other acquisition-related expenses.

## 7. Inventory

Inventory consists of the following (dollars in thousands):

	December 31, 2017	December 31, 2016
Raw materials	\$ 98	\$ 134
Work in process	-	20
Finished goods	1,521	1,998
Less: Inventory reserve for excess and slow moving inventory	(68)	-
Total	\$ 1,551	\$ 2,152

## 8. Improvements and Equipment, net

Improvements and equipment consist of the following (in thousands):

		December 31,	
	Useful Life	2017	2016
	(Years)		
Machinery and equipment	3-10	\$4,911	\$5,041
Office furniture and equipment	3-10	344	337
Leasehold improvements	(A)	594	595
		5,849	5,973
Less: Accumulated depreciation and amortization		(4,286)	(3,881)
Improvements and equipment, net		\$1,563	\$2,092

(A) Leasehold improvements are amortized over the shorter of the remaining lease term or estimated useful life.

Depreciation and amortization expense was \$706,000 and \$1.8 million for the years ended December 31, 2017 and 2016, respectively.

**9.Intangible Assets**

The gross carrying amount and accumulated amortization of intangible assets are as follows (in thousands):

December 31, 2017					
	Useful Life (Years)	Gross Amount	Accumulated Amortization	Impairment	Net Carrying Amount
Technology	10	\$32,539	\$ (12,083 )		\$ 20,456
Customer relationships	9-12	1,984	(934 )		1,050
Tradename	3	111	(111 )		-
Tradename related to MIST Therapy (1)	3	1,913	(1,350 )		563
Non-compete	1	208	(208 )	-	-
Total intangible assets		36,755	(14,686 )	-	22,069

December 31, 2016					
	Useful Life (Years)	Gross Amount	Accumulated Amortization	Impairment	Net Carrying Amount
Technology	10	\$32,539	\$ (9,069 )	\$ -	\$ 23,470
Customer relationships	9-12	1,984	(762 )	-	1,222
Tradename	3	111	(111 )	-	-
Tradename related to MIST Therapy (1)	3	3,601	-	(1,688 )	1,913
Non-compete	1	208	(208 )	-	-
Total intangible assets		38,443	(10,150 )	(1,688 )	26,605

In December 2016, the Company determined the tradename related to MIST Therapy was no longer an (1)indefinite-lived intangible asset. The Company assigned a remaining useful of approximately 1.5 years, consistent with the Company's other trademarks.

The Company performs its assessment of the recoverability of indefinite-lived intangible assets annually during the fourth quarter, or more frequently as impairment indicators arise, and it is based upon a comparison of the carrying value of such assets to their estimated fair values. The Company performed its most recent annual assessment during the four quarter of 2017, which resulted in no impairment charge. During the year ended December 31, 2016 the Company recorded an impairment charge of approximately \$1.7 million to the MIST Therapy tradename and is included in impairment charges in the consolidated statement of operations.

Amortization expense attributable to intangible assets for the years ended December 31, 2017 and 2016 was approximately \$4.7 million and \$3.5 million, respectively.

Amortization expense in each of the five years and thereafter subsequent to December 31, 2017 related to the Company's intangible assets is expected to be as follows (in thousands):

	Expected Amortization Expense
2018	\$ 3,748
2019	2,910
2020	2,885
2021	2,839
2022	2,835
Thereafter	6,852
Total	\$ 22,069

#### 10. Accrued Expenses

Accrued expenses and other current liabilities consist of the following (in thousands):

	December 31, 2017	December 31, 2016
Salaries, benefits and incentive compensation	\$ 1,981	\$ 3,007
Milestone payment to licensor	1,000	1,000
Professional fees	538	692
Royalty fees	227	197
Deferred revenue	365	181
Other	159	147
Total accrued expenses and other current liabilities	\$ 4,270	\$ 5,224

## 11. Operating Leases

The Company leases two corporate offices and one commercial manufacturing facility through operating lease agreements. The Company has obligations through 2023 for both corporate offices, one located in Eden Prairie, Minnesota, and one located in Yardley, Pennsylvania. The Company also has an obligation for its commercial manufacturing facility located in Langhorne, Pennsylvania, through 2026. During the year ended December 31, 2016, the landlord of the office in Yardley, Pennsylvania, made certain improvements to the facility. The Company recorded a deferred lease incentive liability of \$267,000 for the improvements funded by the landlord in accrued and other long-term liabilities on the consolidated balance sheet and amortizes the deferred liability as a reduction to rent expense on the consolidated statement of operations over the term of the lease. Tenant improvements are also included in leasehold improvements on the balance sheet.

Future minimum lease payments, excluding expense reimbursements, under noncancelable operating leases at December 31, 2017 are as follows (in thousands):

2018	\$506
2019	512
2020	519
2021	525
2022	530
Thereafter	780
Total	\$3,372

Total rent expense was \$570,000 and \$542,000 for the years ended December 31, 2017 and 2016, respectively.

## 12. Debt

### *Senior Secured Term Loan Facility*

On May 29, 2015, the Company entered into a Credit Agreement and Guaranty (the “Credit Agreement”) with Perceptive Credit Opportunities Fund, L.P. (“Perceptive”). The Credit Agreement provided a senior secured term loan in a single borrowing to the Company in the principal amount of \$15.5 million. The Credit Agreement (i) has a four-year term, (ii) accrues interest at an annual rate equal to the greater of (a) one-month LIBOR or 1% plus (b) 9.75%, (iii) is interest only for the first 24 months, followed by monthly amortization payments of \$225,000, with the remaining unpaid balance due on the maturity date and (iv) is secured by a first priority lien on substantially all of the Company’s assets. The Company is required to pay an exit fee when the term loan is paid in full equal to the greater of 2% of the

outstanding principal balance immediately prior to the final payment or \$200,000, which was amended in conjunction with the extinguishment of debt described below from the greater of 1% of the outstanding principal balance immediately prior to the final payment or \$100,000. The interest rate at December 31, 2017 was 11.125%.

In connection with the Credit Agreement, the Company incurred approximately \$1.3 million of debt issuance costs. The debt issuance costs are being amortized over the term of the loan on a straight-line basis, which approximates the effective interest method. During the years ended December 31, 2017 and 2016, the Company recorded amortization of debt issuance costs of \$247,000 and \$273,000 respectively, which is included in interest expense for the periods presented.

In connection with the entry into the Credit Agreement, a five-year warrant (the “Warrant”) to purchase 75,000 shares of common stock, par value of \$0.001 per share at an exercise price of \$55.138 per share (the “Exercise Price”) was issued to Perceptive. The Company granted Perceptive customary demand and piggy-back registration rights with respect to the shares of common stock issuable upon exercise of the Warrant. The warrant contains a weighted average anti-dilution feature whereby the Exercise Price is subject to reduction if the Company issues shares of common stock (or securities convertible into common stock) in the future at a price below the current Exercise Price. As a result, the warrant was determined to be a derivative liability. The warrant had an issuance date fair value of approximately \$2.7 million which was recorded as a debt discount. During the years ended December 31, 2017 and 2016, the Company recorded amortization of debt discount of \$577,000 and \$569,000, respectively, which is included in interest expense for the periods presented. See Note 18 – *Fair Value Measurement* for additional details.

As of December 31, 2017, the Company was in default of a covenant pertaining to trailing twelve-month revenue under the Credit Agreement as a result of its failure to achieve \$24,600,000, \$27,200,000, \$30,300,000, \$33,800,000 and \$37,800,000 of gross revenue for the twelve-month periods ended December 31, 2016, March 31, 2017, June 30, 2017, September 30, 2017 and December 31, 2017, respectively. At times during 2017, the Company was in default of a minimum monthly cash balance requirement under the Credit Agreement of \$2,000,000. The Company has classified the entire principal balance as a current liability in its balance sheet as of December 31, 2017 and 2016.

The Company amended and restated the Warrant on each of October 25, 2016, January 26, 2017, March 7, 2017 and April 6, 2017. In addition, on June 1, 2017, the Company further amended the Warrant. The amended and restated Warrant, as amended, is exercisable for 210,000 shares of the Company's common stock at an exercise price of \$4.70. The amended and restated Warrant, as amended, contains a weighted average anti-dilution feature whereby the exercise price of the amended and restated warrant is subject to reduction if the Company issues shares of common stock (or securities convertible into common stock) in the future at a price below the current exercise price of such warrant. Perceptive will not have the right to exercise the warrant to the extent that after giving effect to such exercise, Perceptive would beneficially own in excess of 9.99% of the common stock outstanding immediately after giving effect to such exercise. See Note 18 – *Fair Value Measurement* for additional details.

### ***Consent and Forbearance Agreement***

Under an agreement dated January 26, 2017, as amended March 7, 2017, April 27, 2017 and August 9, 2017, the lender agreed to forbear from exercising any rights and remedies related to the default until the earlier of September 30, 2017 or the date when the lender becomes aware of any other default.

On August 31, 2017, in connection with the Argentum Purchase Agreement, the Company and Perceptive entered into a Consent, Forbearance and Amendment Agreement (the "Consent and Forbearance Agreement"), pursuant to which the Company agreed to pay \$1,650,000 of the proceeds from the Argentum Purchase Agreement to Perceptive, of which approximately \$1,618,000 was applied towards the outstanding principal amount of the term loan under the credit agreement and approximately \$32,000 was used to pay an early prepayment fee. This payment was made on August 31, 2017. During the year ended December 31, 2017, the Company recorded a loss on early extinguishment of debt of \$214,000 related to the Consent and Forbearance Agreement. This amount consisted of the \$32,000 prepayment penalty, the write-off of \$129,000 of unamortized discount, and the write-off of \$53,000 of unamortized debt issuance costs.

Under the Consent and Forbearance Agreement the lender agreed to: (a) release its liens on assets purchased by Argentum; (b) defer the commencement of the Company's remaining principal payments until January 31, 2018, and agreed to extend the forbearance period and to forbear from exercising any rights and remedies related to the Company's default of a covenant pertaining to (i) trailing twelve-month revenue under the Credit Agreement as of (A) September 30, 2016, (B) December 31, 2016 (C) March 31, 2017 and (D) June 30, 2017 and (ii) failure to maintain on a consolidated basis, a monthly minimum cash balance of at least \$2,000,000, until the earlier of October 13, 2017 or the date when the lender becomes aware of any other default. On November 7, 2017, the lender agreed to extend the forbearance period and to forbear from exercising any rights and remedies to the Company's default of the aforementioned covenants, including the trailing twelve-month revenue as of September 30, 2017, until the earlier of December 31, 2017 or the date when the lender becomes aware of any other default.



Under the Forbearance and Amendment Agreement dated as of February 5, 2018, the lender agreed to defer the commencement of the Company's remaining principal payments and agreed to extend the forbearance period and to forbear from exercising any rights and remedies related to the Company's default of a covenant pertaining to (i) trailing twelve-month revenue under the Credit Agreement as of (A) September 30, 2016, (B) December 31, 2016 (C) March 31, 2017 (D) June 30, 2017 (E) September 30, 2017 and (F) December 31, 2017 and (ii) failure to maintain on a consolidated basis, a monthly minimum cash balance of at least \$2,000,000, until the earlier of April 30, 2018, the termination of the Asset Purchase Agreement, or the date when the lender becomes aware of any other default.

The lender reserved the rights, commencing with the occurrence of any of these events, to pursue any rights and remedies available to it, including, but not limited to, declaring all or any portion of the outstanding principal amount to be immediately due and payable, imposing a default rate of interest as specified in the credit agreement, or pursuing the lender's rights and remedies as a secured party under the UCC as a secured lender. In addition, the lender has a lien on substantially all of the Company's assets and, as a result of the default, the lender may seek to foreclose on some or substantially all of the Company's assets after the expiration of the forbearance.

### ***2016 Extinguishment***

On June 30, 2016, the Company entered into a Consent Under Credit Agreement (the "Consent Agreement") with Perceptive pursuant to which Perceptive consented to the Purchase Agreement with BSN provided that the Company agreed to pay \$1.8 million of the proceeds from the Purchase Agreement to Perceptive, of which \$1.7 million was applied towards the outstanding principal amount of the term loan under the Credit Agreement and \$52,000 was used to pay an early prepayment fee. This payment was made on July 1, 2016. During the year ended December 31, 2016, the Company recorded a loss on early extinguishment of debt of \$373,000 related to the Consent Agreement. This amount consisted of a \$52,000 prepayment penalty, the write-off of \$226,000 of unamortized discount, and the write-off of \$95,000 of unamortized debt issuance costs. See Note 5 – *Discontinued Operations* for additional details.

Debt consists of the following (in thousands):

	December 31, 2017	December 31, 2016
Principle balance	\$ 12,135	\$ 13,752
Unamortized debt issuance and discount costs	(1,206 )	(2,211 )
Total	\$ 10,929	\$ 11,541

### 13. Commitments and Contingencies

#### *Agreements for Human Placental Based Products with Celularity, Inc.*

In November 2013, the Company entered into a License, Marketing and Development Agreement (the “License Agreement”) and Supply Agreement (the “Biovance Supply Agreement”) with Celgene Cellular Therapeutics (“CCT”), an affiliate of Celgene Corporation (“Celgene”). The agreements grant the Company an exclusive, royalty-bearing license in CCT’s intellectual property for certain placental based products, including ECM and Biovance®, as well as provide the Company with the its requirements of Biovance for distribution. In January 2016, HLI Cellular Therapeutics, LLC (“HLI”), a genomics-based, technology-driven company, announced the purchase of LifebankUSA and other select assets from CCT. CCT assigned and HLI assumed the license and supply agreements the Company entered into with CCT, for certain placental based products. In June 2017, Celularity acquired some of the assets of HLI, including the agreements between HLI and the Company. The Company is required to pay Celularity annual license fees, designated amounts when certain milestone events occur and royalties on all sales of licensed products, with such amounts being variable and contingent on various factors. During the years ended December 31, 2017 and 2016, the Company incurred royalties of approximately \$818,000 and \$493,000, respectively, in connection with this agreement. Approximately \$227,000 and \$197,000 is included in accrued expenses as of December 31, 2017 and December 31, 2016, respectively, in connection with this agreement. The initial term of the License Agreement ends on November 14, 2023, unless sooner terminated pursuant to the termination rights under the License Agreement, and will extend for additional two-year terms unless either party gives written notice within a specified period prior to the end of a term.

The License Agreement with Celularity is terminable on a product-by-product basis if the Company fails to meet certain minimum sales thresholds in the second year or any subsequent year of commercial sales of each licensed product. Each year of commercial sales are referred to in the License Agreement as “launch years” and the calendar period constituting each launch year for each licensed product is determined in accordance with the terms of the License Agreement. To maintain its license for Biovance, the Company must meet a minimum gross sales amount for Biovance in the second year and third year of commercial sales. If the Company fails to meet the minimum threshold in the second year of commercial sales of product, it would be able to cure such failure by making a cure payment specified in the License Agreement to Celularity; provided, however, the Company does not have the option to make a

cure payment, should it fail to meet the minimum threshold for such product in the third year of commercial sales and Celularity may terminate the License Agreement with respect to such product.

In September 2014, the Company entered into a First Amendment to the License Agreement (the “Amended License Agreement”), pursuant to which the Company received the right to market Biovance for podiatric and orthopedic applications. The Amended License Agreement also amends certain terms and the related schedule for milestone payments to CCT. In May 2015, the Company amended its exclusive licensing agreement with CCT, which granted the Company the right to develop and market CCT’s connective tissue matrix product, also known as Interfyl.

In April 2016, the Company entered into a Supply Agreement with HLI (now Celularity), pursuant to which Celularity supplies the Company with the Company’s entire requirement of Interfyl™ Human Connective Tissue Matrix. Additionally, the Company agreed to make certain future milestone payments upon the achievement of certain milestones. The Company initiated sales and marketing efforts of Interfyl Human Connective Tissue Matrix in September 2016 and achieved two milestones under the license agreement. The Company is required to pay Celularity \$500,000 related to the first commercial sale of Interfyl in the flowable matrix configuration and \$500,000 related to the first commercial sale of Interfyl in the particulate form. Commercial sales of both configurations occurred in September 2016, and as such, the Company recorded \$1.0 million of milestone expense during the year ended December 31, 2016. The milestone has been included in accrued expenses and other current liabilities as of December 31, 2017 and December 31, 2016. The payment of this milestone will be waived if the Asset Purchase Agreement with Celularity is consummated.

On December 1, 2017, the Company received notice from Celularity that the Company is in material breach of the License Agreement or Supply Agreements with Celularity, for failure to purchase the required amounts of materials under the Supply Agreements and failure to use commercially reasonable best efforts to undertake development activities for the licensed products under the License Agreement. Celularity estimated that an additional purchase of at least \$842,000 would have to be made by the Company to remedy the breach under the Supply Agreements. Celularity has agreed to forbear from exercising its right to terminate the supply and license agreements until the closing of the Asset Purchase Agreement or termination of the Asset Purchase Agreement for any reason.

***License Agreement with Noble Fiber Technologies, LLC***

On July 15, 2011, the Company entered into a license agreement with Noble Fiber Technologies, LLC, whereby the Company has the exclusive right and license to manufacture and distribute “SilverSeal Hydrogel Wound Dressings” and “SilverSeal Hydrocolloid Wound Dressings”. The license is granted for ten years with an option to be extended for consecutive renewal periods of two years after the initial term. Royalties are to be paid equal to 9.75% of net sales of licensed products. The agreement calls for minimum royalties in 2016 in the amount of \$600,000. There are no minimum royalties subsequent to 2016. Total royalties, for the years ended December 31, 2017 and 2016 were \$1,900 and \$600,000, respectively, in connection with this agreement. Approximately \$0 and \$598,000 is included in accounts payable as of December 31, 2017 and 2016, respectively, in connection with this agreement.

***Contingent Consideration***

***Celleration, Inc.***

On May 29, 2015, the Company acquired all outstanding equity interest of Celleration, Inc. (“Celleration”), a medical device company focused on developing and commercializing the MIST Therapy® therapeutic ultrasound platform for the treatment of acute and chronic wounds. The Company agreed to pay contingent consideration of 3.5 times revenue from acquired MIST Therapy products in excess of certain revenue targets for the years ending December 31, 2015 and 2016, payable in equal amounts of cash and the Company’s common stock. This contingent consideration was payable in two installments in March 2016 and March 2017.

The first installment consisted of \$2.6 million of cash and approximately 98,600 shares of the Company’s common stock valued at approximately \$2.6 million and was paid in March 2016. This payment was based on 3.5 times of the excess of 2015 MIST Therapy revenue of approximately \$10.2 million over 2014 MIST Therapy revenue of approximately \$8.7 million.

The second installment consisted of \$675,000 of cash and approximately 101,000 shares of the Company’s common stock valued at approximately \$675,000 and was paid in March 2017. This payment was based on 3.5 times of the excess of 2016 MIST Therapy revenue of approximately \$10.5 million over 2015 MIST Therapy revenue of approximately \$10.2 million. There are no further contingent payments due in connection with the Celleration acquisition.

*Choice Therapeutics, Inc.*

On May 5, 2014, the Company acquired all outstanding equity interest of Choice Therapeutics, Inc., a provider of innovative wound care products using proprietary TheraBond 3D® Antimicrobial Barrier Systems. The Company agreed to pay contingent consideration based upon the Company achieving specific performance metrics over the three twelve-month periods, ended April 30, 2017. The Company issued approximately 132,000 shares of its common stock valued at approximately \$500,000 in June 2017. There are no further contingent payments due in connection with the Choice acquisition.

***Litigation, Claims and Assessments***

From time to time, the Company may become involved in lawsuits, investigations and claims that arise in the ordinary course of business. The Company believes it has meritorious defenses against all pending claims and intends to vigorously pursue them. While it is not possible to predict or determine the outcomes of any pending actions, the Company believes the amount of liability, if any, with respect to such actions, would not materially affect its financial position, results of operations or cash flows.

On February 22, 2018, a putative stockholder class action complaint was filed in the United States District Court for the District of Delaware against the Company and each member of the Board, captioned Ronald Cresta, Individually and on Behalf of All Others Similarly Situated v. Alliqua BioMedical Inc., David Johnson, Joseph M. Leone, Gary Restani, Jeffrey Sklar and Mark Wagner. The complaint alleges, among other things, that the Company and the Board violated federal securities laws and regulations by soliciting stockholder votes in connection with the Asset Sale Transaction through a proxy statement that omits material facts necessary to make the statements therein not false or misleading. The complaint seeks, among other things, to enjoin the Company and the Board from conducting the stockholder vote on the Asset Sale Transaction unless and until the allegedly omitted material information is disclosed to the Company's stockholders, damages allegedly suffered by the plaintiffs as a result of the asserted omissions, as well as related attorneys' fees and expenses.

The Company is reviewing the complaint and has not yet formally responded to it, but the Company denies the allegations and intends to defend against them vigorously.

**14. Stockholders' Equity**

***Preferred Stock***

The Company has authorized 1,000,000 shares of preferred stock, \$0.001 par value per share, which may be divided into series and with preferences, limitations and relative rights determined by the Board of Directors.

***Common Stock***

On May 6, 2016, the Company held its 2016 annual meeting of stockholders. The stockholders approved an amendment to the Company's Certificate of Incorporation to increase the number of authorized shares of common stock from 45,714,286 to 95,000,000 shares.

F-21

### ***2011 Plan***

The Company maintains the 2011 Long-Term Incentive Plan (the “2011 Plan”) that provides for the granting of stock options, restricted stock units (“RSUs”), restricted stock and other awards to employees, directors and others. A total of 182,857 shares of common stock have been authorized for issuance under the 2011 Plan, of which, as of December 31, 2017, 30,903 shares were available for future issuances.

### ***2014 Plan***

The Company maintains the 2014 Long-Term Incentive Plan (the “2014 Plan”) that provides for the granting of stock options, RSUs, restricted stock and other awards to employees, directors and others. On February 26, 2015 and May 6, 2015, the Company’s Board of Directors and the Company’s shareholders, respectively, approved an amendment to the 2014 Plan to increase the total number of shares of common stock authorized for issuance under the 2014 Plan by an additional 350,000 shares. On April 26, 2017 and June 23, 2017, the Company’s Board of Directors and the Company’s shareholders, respectively, approved an amendment to the 2014 Plan to increase the total number of shares of common stock authorized for issuance under the 2014 Plan by an additional 400,000 shares. A total of 950,000 shares of common stock are reserved for award under the 2014 Plan, of which, as of December 31, 2017, 92,459 shares were available for future issuances.

### ***Private Placement***

On February 27, 2017, the Company entered into a securities purchase agreement (the “Securities Purchase Agreement”) with certain accredited investors, pursuant to which the Company agreed to issue and sell to the investors in a private placement (the “Private Placement”) an aggregate of 554,000 shares of the Company’s common stock at a purchase price of \$5.00 per share. The Company closed the Private Placement on the same day as it entered into the Securities Purchase Agreement and received aggregate gross proceeds of approximately \$2.8 million. In connection with the Private Placement, the Company paid an aggregate of \$196,000 of financial advisory fees and \$40,000 of administrative fees, which were recorded as a reduction of additional paid-in capital.

The Securities Purchase Agreement contains a “most-favored nation” provision that provides that if the Company, during 120 days from February 27, 2017, issues or sells any common stock or common stock equivalents reasonably believed to be more favorable in terms or conditions than those in the Private Placement, then the Company must amend the terms of the Securities Purchase Agreement to give the private investors the benefit of such favorable terms or conditions. In connection with the common stock sold in the Public Offering (as defined below) and in accordance with this provision, on April 11, 2017, the Company issued an aggregate of 38,072 shares of its common stock to

these investors. On June 23, 2017, the Company held its 2017 annual meeting of stockholders during which the stockholders approved the issuance of the remaining 100,428 additional shares of common stock to be issued to the investors, and, following the meeting, on June 23, 2017, the Company issued the remaining shares.

### ***Underwritten Public Offering***

On April 3, 2017, the Company closed an underwritten public offering (the “Public Offering”) of 947,325 shares of its common stock at a price to the public of \$4.00 per share. The Company received aggregate gross proceeds of approximately \$3.8 million. In connection with the Public Offering, the Company paid an aggregate of \$365,000 of financial advisory fees and \$92,000 of administrative fees, which were recorded as a reduction of additional paid-in capital. The shares of common stock were issued pursuant to the Company’s shelf registration statement on Form S-3 previously filed with the Securities and Exchange Commission and declared effective on September 25, 2014.

On April 3, 2017, the Company issued warrants to purchase an aggregate of 23,686 of the Company’s common stock to the underwriter of this offering. These warrants are immediately exercisable, have an exercise price of \$4.40, and expire on March 29, 2022. The warrants had an aggregate issuance date fair value of \$78,000 which was recorded as both a debit and credit to additional paid in capital.

Pursuant to an anti-dilution provision provided in the warrants dated November 8, 2012 to purchase common stock at an initial exercise price of \$21.90, the exercise price of these warrants was adjusted to the public offering price of \$4.00. As of April 3, 2017, November 2012 warrants to purchase 36,231 shares of the Company’s common stock were outstanding. These warrants expired in November 2017.

### ***Stock-Based Compensation***

For the year ended December 31, 2017, the Company recognized \$2.0 million of stock-based compensation expense, of which, \$45,000 is included in cost of revenues and \$2.0 million is included in selling, general and administrative expenses in the consolidated statements of operation. For the year ended December 31, 2016, the Company recognized \$4.9 million of stock-based compensation expense, of which, \$0.2 million is included in cost of revenues and \$4.7 million is included in selling, general and administrative expenses in the consolidated statements of operations. As of December 31, 2017, there was \$0.7 million of unrecognized stock-based compensation expense which will be amortized over a weighted average period of 0.8 years.



***Restricted Stock***

During the year ended December 31, 2017, the Company granted an aggregate of 181,936 shares of restricted stock to employees with an aggregate grant date value of \$621,000, which will be recognized proportionate to the vesting period. The shares vest as follows: (i) 66,936 shares vest on September 21, 2017, (ii) 5,000 shares vest on December 31, 2017, (iii) 50,000 shares vest on June 23, 2018, and (iv) 60,000 shares vest pursuant to the satisfaction of certain performance conditions.

During the year ended December 31, 2016, the Company granted an aggregate of 102,500 shares of restricted stock to employees with an aggregate grant date value of \$1,076,000, which will be recognized proportionate to the vesting period. The shares vest as follows : (i) 32,500 vested the earlier of February 9, 2017 or the participants termination of service by the Company without cause and (ii) 70,000 shares vest pursuant to the satisfaction of certain performance conditions.

A summary of restricted stock award activity during the year ended December 31, 2017 and 2016 is presented below (in thousands, except per share data):

	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Total Grant Date Fair Value
Non-vested, December 31, 2015	69	\$ 61.10	\$ 4,226
Granted	103	10.50	1,076
Vested	(24 )	60.00	(1,428 )
Forfeited	(1 )	14.60	(12 )
Non-vested, December 31, 2016	147	\$ 26.26	\$ 3,862
Granted	182	3.41	621
Vested	(137 )	17.35	2,373
Forfeited	(2 )	3.87	-
Non-vested, December 31, 2017	190	\$ 11.07	\$ 6,856

**Warrants**

See Note 12 - *Debt – Senior Secured Term Loan Facility* for details associated with a warrant issued in connection with debt.

There were no compensatory warrants issued during the year ended December 31, 2017.

A summary of the warrant activity during the year ended December 31, 2017 and 2016 is presented below (in thousands, except years and per warrant data):

	Number of Warrants	Weighted Average Exercise Price per Warrant	Weighted Average Remaining Life in Years	Intrinsic Value
Outstanding, December 31, 2015	338	\$ 57.00		
Issued	-	-		
Exercised	-	-		
Cancelled	(1 )	87.50		
Outstanding, December 31, 2016	337	\$ 56.90		\$ -
Issued	159	4.66		
Adjustment for price reset	29			
Exercised	-	-		
Cancelled	(47 )	9.35		
Outstanding, December 31, 2017	478	\$ 32.79	2.4	\$ -
Exercisable, December 31, 2017	478	\$ 32.79	2.4	\$ -

The following table presents information related to warrants at December 31, 2017 (in thousands, except years and per warrant data):

Warrants Outstanding		Warrants Exercisable	
Exercise Price	Outstanding Number of Warrants	Weighted Average Remaining Life in	Exercisable Number of Warrants

		Years	
\$4.0 - \$21.80	233	4.1	233
\$40.00 - \$49.99	98	0.5	98
\$50.00 - \$59.90	104	0.9	104
\$60.00 - \$105.00	43	1.3	43
	478	2.4	478

As of December 31, 2017 and 2016, warrants to purchase an aggregate of 210,000 and 81,628 shares of common stock at a weighted average exercise price of \$4.70 and \$52.40 per share, respectively, were deemed to be a derivative liability. See Note 18— *Fair Value Measurement*.

### ***Stock Options***

During 2016, the Company granted ten-year options to purchase an aggregate of 164,976 shares of common stock at exercise prices ranging from \$8.00 to \$22.00 with an aggregate grant date value of \$1.3 million to employees and directors pursuant to the 2014 Plan. The options vest as follows: (i) 22,500 shares vest one-twelfth monthly over one year, and (ii) 142,400 shares vest ratably over three years on the anniversaries of the grant date. The grant date value is being amortized over the vesting term.

During 2017, the Company granted ten-year options to purchase an aggregate of 258,105 shares of common stock at exercise prices ranging from \$2.09 to \$5.70 per share with an aggregate grant date value of \$642,000 to non-executive employees and directors pursuant to the 2014 Plan. The options vest as follows: (i) 45,045 shares vest one-twelfth monthly over one year, and (ii) 213,060 shares vest in one-fourth increments every six months over a period of two years. The grant date value is being amortized over the vesting term.

In applying the Black-Scholes option pricing model to stock options granted, the Company used the following assumptions:

	Year Ended December 31,	
	2017	2016
Risk free interest rate	1.81% - 2.43%	1.14% - 2.06%
Expected term (years)	5.04 – 6.50	5.04 – 6.50
Expected volatility	81.94% - 87.00%	89.53% - 89.95%
Expected dividends	0.00%	0.00%

The risk-free interest rate is based on rates of treasury securities with the same expected term as the options. The Company uses the “simplified method” to calculate the expected term of employee and director stock-based options. The expected term used for consultants is the contractual life. The Company is utilizing an expected volatility figure based on a review of the Company’s historical volatility, over a period of time, equivalent to the expected life of the instrument being valued. The expected dividend yield is based upon the fact that the Company has not historically paid dividends, and does not expect to pay dividends in the near future.

Option forfeitures are estimated at the time of valuation and reduce expense ratably over the vesting period. This estimate will be adjusted periodically based on the extent to which actual option forfeitures differ, or are expected to differ, from the previous estimate, when it is material. The Company estimated forfeitures related to options at annual rates ranging from 0% to 5% for options outstanding at December 31, 2017 and 2016.

The weighted average estimated grant date fair value of the options granted during the years ended December 31, 2017 and 2016 was \$2.49 and \$7.73 per share, respectively.

A summary of the stock option activity during the years ended December 31, 2017 and 2016 is presented below (in thousands, except years and per option data):

	Number of Options	Weighted Average Exercise Price per Option	Weighted Average Remaining Life in Years	Intrinsic Value
Outstanding, December 31, 2015	623	\$ 62.60		
Granted	165	10.50		
Exercised	-	-		

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Forfeited	(68	)	39.50			
Outstanding, December 31, 2016	720		\$ 52.90			
Granted	258		3.53			
Exercised	-		-			
Forfeited	(168	)	40.60			
Outstanding, December 31, 2017	810		\$ 39.67	6.3	\$	-
Exercisable, December 31, 2017	658		\$ 42.71	5.6	\$	-

F-25

The following table presents information related to stock options at December 31, 2017 (in thousands, except years and per option data):

Range of Exercise Price	Options Outstanding		Options Exercisable		Exercisable Number of Options
	Weighted Average Exercise Price	Outstanding Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Life in Years	
\$2.00 - \$4.00	\$ 3.52	222	3.57	8.9	68
\$4.10 - \$9.90	8.54	32	8.61	6.8	143
\$10.00 - \$19.90	10.58	80	10.59	7.6	28
\$20.00 - \$29.90	23.08	1	22.90	4.1	1
\$30.00 - \$39.90	33.72	47	33.72	5.6	45
\$40.00 - \$49.90	46.61	68	46.01	6.0	66
\$50.00 - \$59.90	52.99	51	53.20	5.5	39
\$60.00 - \$69.90	66.06	205	66.47	4.4	185
\$70.00 - \$79.90	77.54	3	77.54	6.3	3
\$80.00 - \$89.90	87.40	74	87.36	2.0	53
\$90.00 - \$99.90	90.04	21	90.04	3.5	21
\$100.00 - \$266.90	110.13	6	110.13	5.2	6
		810		5.6	658

## 15. Income Taxes

The Company files corporate income tax returns in U.S. federal, state and local jurisdictions, including Pennsylvania, and has tax returns subject to examination by tax authorities generally beginning in the year ended December 31, 2013 and through December 31, 2017. However, to the extent the Company utilizes its net operating loss (“NOL”) carryforwards in the future, the tax years in which the attribute was generated may still be adjusted upon examination by the Internal Revenue Service or state tax authorities of the future period tax return in which the attribute is utilized.

The income tax (benefit) provision consists of the following (in thousands):

	For The Years Ended	
	December 31,	
	2017	2016
Federal:		
Current	\$ -	\$ -
Deferred	(664 )	(627 )

State and local:

Current	6	4
Deferred	(85 )	(92 )

Income tax provision \$ (743 ) \$ (715 )

F-26

For the years ended December 31, 2017 and 2016, the expected tax expense based on the federal statutory rate reconciled with the actual tax expense is as follows:

	For The Years Ended December 31,			
	2017		2016	
U.S. federal statutory rate	34.0	%	34.0	%
State tax rate, net of federal benefit	3.0	%	4.5	%
Permanent differences				
- Change in fair value of warrant liability	(0.1	)%	0.9	%
- Change in fair value of contingent consideration	0.0	%	10.4	%
- Intangible impairment	(12.0	)%	(9.3	)%
- Other	(0.3	)%	(0.4	)%
Adjustments to deferred taxes	(4.6	)%	(8.2	)%
Tax Reform - Federal Rate Change	(50.9	)%	0.0	%
Tax Reform - Change in valuation allowance	50.9	%	0.0	%
Change in valuation allowance	(17.4	)%	(29.7	)%
Income tax provision	2.6	%	2.2	%

On December 22, 2017 the U.S. government enacted significant changes to federal tax law following the passage of the Tax Cuts and Jobs Act (“the Act”). The Act significantly changes the U.S. corporate tax system. The Company has reasonably estimated the accounting for the effects of the Act during the year ended December 31, 2017. The Company’s financial statements for the year ended December 31, 2017 reflect certain effects of the Act including a reduction in the corporate tax rate from 34% to 21% and changes to limitations on the deductibility of executive compensation. As the Company has recorded a full valuation allowance against its net deferred tax assets as of December 31, 2017, these changes have no impact on the income tax benefit for year ended December 31, 2017. The Company has recorded changes to its deferred tax assets and liabilities due to enactment of the Act. As a result of the change in U.S. corporate income tax rate, the Company recorded a decrease in its net deferred tax asset of approximately \$14.6 million, which was offset by a decrease in valuation allowance. In addition, the Company analyzed changes in the executive compensation rules pursuant to the Act and determined that approximately \$1.3 million of the deferred tax asset for stock compensation may not be realizable. The Company has previously recorded a valuation allowance against the deferred tax asset so this adjustment has no impact on the 2017 provision. Given the significant changes resulting from and complexities associated with the Act, the financial impacts for the fourth quarter and full year 2017 are provisional and subject to further analysis, interpretation and clarification of the Act, which could result in changes to these estimates during 2018. In order to complete the accounting for these items the Company will need to further analyze executive compensation awards and prepare its 2017 corporate income tax return. The Company will reflect any adjustments to the provisional amounts in the period the accounting is completed, and expects to complete this analysis within the one-year measurement period provided by SAB 118.



As of December 31, 2017 and 2016, the Company's deferred tax assets consisted of the effects of temporary differences attributable to the following (in thousands):

	As of December 31,	
	2017	2016
Deferred tax assets:		
Net operating loss carryforwards	\$29,580	\$40,117
Stock-based compensation	5,598	8,671
Goodwill and Tradename	32	-
Accruals	694	541
Transaction costs	39	732
Other	364	861
Total deferred tax assets	36,307	50,922
Valuation allowance	(30,864)	(41,482)
Deferred tax assets, net of valuation allowance	\$5,443	\$9,440
Deferred tax liabilities:		
Property and equipment	(65 )	(281 )
Intangible assets	(5,378 )	(9,159 )
Goodwill	-	(749 )
Total deferred tax liabilities	(5,443 )	(10,189 )
Net deferred tax liabilities	\$-	\$(749 )

For the years ended December 31, 2017 and 2016, the Company had approximately \$114.6 million and \$104.9 million of federal NOL carryovers, respectively, which substantially begin to expire in 2020 and through 2037. The company also has state NOL carryovers in multiple jurisdictions, including most materially in Pennsylvania, \$26.4 million and \$24.6 million, and in Florida, \$11.3 million and \$10.9 million, as of December 31, 2017 and December 31, 2016, respectively, which substantially begin to expire in 2020 and through 2037. During 2016 the Company performed a 382 study, and as a result of the study, reduced its NOL carryforwards by \$4.8 million, which is the amount of the NOL carryforwards that are expected to expire unutilized pursuant to the Section 382 study. On May 29, 2015 the Company acquired Celleration, Inc. and the company has performed a Section 382 study for Celleration, Inc. The amount of federal NOL carryforwards as of December 31, 2017 and December 31, 2016 disclosed above do not include \$47.9 million of Celleration, Inc. NOL carryforwards that are expected to expire unutilized pursuant to the Section 382 study. The Celleration, Inc. state NOL carryforwards have also been reduced accordingly. On May 5, 2014 the Company acquired the equity interests of Choice and the Company believes the Choice NOL carryforwards as of that date are subject to Section 382 limitations. The amount of federal NOL carryforwards as of December 31, 2017 and December 31, 2016 disclosed above do not include \$2.5 million of Choice NOL carryforwards that the Company has estimated will expire unutilized pursuant to this limitation. Additionally, an ownership change pursuant to Section 382 may have occurred since 2016, or could occur in the future, such that the NOLs available for utilization could be further limited.

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. The ultimate realization of the deferred tax assets is dependent upon the future generation of taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. As of December 31, 2016, the deferred tax liabilities related to goodwill and to a tradename could not be used in this determination since both assets were considered to be assets with an indefinite life for financial reporting purposes. After consideration of all the evidence, both positive and negative, management has recorded a full valuation allowance against net deferred tax assets at December 31, 2017 and December 31, 2016 because management has determined that it is more likely than not that these deferred tax assets will not be realized. The valuation allowance decreased by \$10.6 million and increased by \$8.5 million during the years ended December 31, 2017 and December 31, 2016, respectively. The decrease in tax year ended December 31, 2017 is primarily related to the decrease in the corporate tax rate from 34% to 21% due to the enactment of the Act, \$14.7 million, offset by increases in NOL carryforwards, \$3.7 million. Included in the current year increases to the valuation allowance is a \$0.7 million increase related to discontinued operations. The increase in tax year ended December 31, 2016 is primarily related to increases in NOL carryforwards.

## **16. Related Party**

In November 2015, the Company entered into a manufacturing supply agreement with a company where a Company director is a member of the Board of Directors. During the years ended December 31, 2017 and 2016, the Company incurred costs of approximately \$433,000 and \$491,000, respectively, from this vendor. Approximately \$123,000 and \$102,000 are included in accounts payable related to this related party as of December 31, 2017 and December 31, 2016, respectively.

## 17. Concentration of Risk

The Company had no single customer exceeding 10% of either its 2017 and 2016 revenue or its outstanding accounts receivable balance as of December 31, 2017 or 2016.

## 18. Fair Value Measurement

Fair value is defined as the price that would be received upon selling an asset or the price paid to transfer a liability on the measurement date. It focuses on the exit price in the principal or most advantageous market for the asset or liability in an orderly transaction between willing market participants. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair values are as follows:

Level 1: Observable prices in active markets for identical assets and liabilities.

Level 2: Observable inputs other than quoted prices in active markets for identical assets and liabilities.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities.

### *Impairment*

Goodwill and other indefinite-lived intangible assets are tested for impairment annually, at the end of the fourth quarter of each fiscal year, and between annual tests if an event occurs or circumstances change that would indicate it is more likely than not that the carrying amount may be impaired. Additionally, the Company continually evaluates whether events or changes in circumstances might indicate that the remaining estimated useful life of long-lived assets may warrant revision, or that the remaining balance may not be recoverable. The factors used to determine fair value are subject to management's judgement and expertise and include, but are not limited to, the present value of future cash flows, net of estimated operating costs, internal forecasts, anticipated capital expenditures and various discount rates commensurate with the risk and current market conditions associated with realizing the expected cash flows projected. These assumptions represent Level 3 inputs. Impairment of the Company's goodwill for the year ended December 31, 2017 was \$10.3 million. Impairment of the Company's goodwill and MIST Therapy tradename for the year ended December 31, 2016 was \$10.9 million.

## *Warrant Liabilities*

On December 31, 2016, the Company recomputed the fair value of its warrant liability of outstanding warrants to purchase an aggregate of 81,628 shares of common stock as \$20,000 using the Binomial option pricing model (Level 3 inputs) using the following assumptions: expected volatility of 65.74%-72.16%, risk-free rate of 0.85%-1.47%, expected term of 0.86-3.41 years, and expected dividends of 0.00%. The Company recorded a gain on the change in fair value of these warrant liabilities of \$841,000 during the year ended December 31, 2016.

The Company amended and restated the Warrant on each of October 25, 2016, January 26, 2017, March 7, 2017 and April 6, 2017. In addition, on June 1, 2017, the Company further amended the amended and restated Warrant. The amended and restated Warrant, as amended, is exercisable for 210,000 shares of the Company's common stock at an exercise price of \$4.70 per share. See Note 12 – *Debt* for additional details. In connection with the amendments of January, March, April and June 2017, the Company recomputed the fair value of the original warrant and amended warrant using the Binomial option pricing model (Level 3 inputs) using the following assumptions: expected volatility of 65.33%-78.98%, risk-free rate of 1.49%-1.95%, expected term of 3.34-5.00 years, and expected dividends of 0.00%. As a result, the Company recorded warrant modification expense of \$803,000 during the year ended December 31, 2017, which represents the incremental value of the amended warrant as compared to the original warrant, both valued as of the respective amendment dates.

On December 31, 2017, the Company recomputed the fair value of its warrant liability of outstanding warrants to purchase an aggregate of 210,000 shares of common stock as \$130,000 using the Binomial option pricing model (Level 3 inputs) using the following assumptions: expected volatility of 73.37% risk-free rate of 2.09%, expected term of 4.07 years, and expected dividends of 0.00%. The Company recorded a gain on the change in fair value of these warrant liabilities of \$692,000 during the year ended December 31, 2017.

The issuance of common stock in connection with the Private Placement and Public Offering triggered an adjustment to the exercise price of certain warrants originally issued in November 2012 from \$55.10 per share to \$5.00 per share to \$4.00 per share with a corresponding adjustment to the number of shares underlying such warrants from 6,629 shares to 29,034 shares to 36,231 shares. The impact of such adjustment is included in the change in fair value of the warrant liabilities during the year ended December 31, 2017.

Warrants that contain exercise reset provisions and contingent consideration liabilities are Level 3 derivative liabilities measured at fair value on a recurring basis using pricing models for which at least one significant assumption is unobservable as defined in ASC 820. The fair value of contingent consideration liabilities that are classified as Level 3 were estimated using a discounted cash flow technique with significant inputs that are not observable in the market and thus represents a Level 3 fair value measurement as defined in ASC 820. The significant inputs in the Level 3 measurement not supported by market activity include the probability assessments of expected future cash flows related to the acquisitions, appropriately discounted considering the uncertainties associated with the obligation, and as calculated in accordance with the terms of the acquisition agreements. See Note 13 – *Commitments and Contingencies* for details on the contingent consideration. The development and determination of the unobservable inputs for Level 3 fair value measurements and the fair value calculations are the responsibility of the Company's Chief Financial Officer and are approved by the Chief Executive Officer.

The following table sets forth a summary of the changes in the fair value of Level 3 warrant liabilities and contingent consideration that are measured at fair value on a recurring basis (in thousands):

	Year Ended December 31,	
	2017	2016
Warrant Liabilities		
Beginning balance	\$ 20	\$ 861
Change in fair value of warrant liability	(693 )	(841 )
Warrant modification expense	803	-
Ending balance	\$ 130	\$ 20
	Year Ended December 31,	
	2017	2016
Contingent Consideration		
Beginning balance	\$ 1,816	\$ 17,028
Payments of contingent consideration	(1,851 )	(5,147 )
Change in fair value of contingent consideration	35	(10,065 )
Ending balance	\$ -	\$ 1,816

Assets and liabilities measured at fair value on a recurring basis are as follows (in thousands):

	December 31, 2017			
	Level 1	Level 2	Level 3	Total Impairments
Assets:				
Intangible assets	\$ -	\$ -	\$ 22,069	\$ -
Goodwill	-	-	1,659	10,300

Total assets	\$ -	\$ -	\$ 23,728	\$ 10,300
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December 31, 2016

	Level 1	Level 2	Level 3	Total Impairments
Assets:				
Intangible assets	\$ -	\$ -	\$ 26,605	\$ -
Goodwill	-	-	11,959	10,895
Total assets	\$ -	\$ -	\$ 38,564	\$ 10,895

F-30

December 31, 2017  
Level 1    Level 2    Level 3

Liabilities:

Warrant liabilities	\$ -	\$ -	\$ 130
Total liabilities	\$ -	\$ -	\$ 130

December 31, 2016  
Level 1    Level 2    Level 3

Liabilities:

Warrant liabilities	\$ -	\$ -	\$ 20
Contingent consideration	-	-	1,816
Total liabilities	\$ -	\$ -	\$ 1,836

## 19. Defined Contribution Plan

The Company maintains the Alliqua, Inc. 401(k) Profit Sharing Plan and Trust (“Plan”) in accordance with the provisions of Section 401(k) of the Code. The Plan covers substantially all full-time employees of the Company. Participants may contribute up to 100% of their total compensation to the Plan, not to exceed the limit as defined in the Code. Under this plan, the Company matches 50% of the employee’s contributions up to 6% of the employee’s annual compensation, as defined by the plan. Employees are eligible for the match after a six-month waiting period and the Company match vests immediately. The Company’s contribution to the plan was \$97,000 and \$105,000 for the years ended December 31, 2017 and 2016, respectively.

## 20. Subsequent Events

### *Asset Purchase Agreement*

On January 5, 2018, the Company entered into the Asset Purchase Agreement pursuant to which the Company agreed to sell the Purchased Assets to Celularity. As consideration for the Purchased Assets, Celularity has agreed to pay the Company \$29 million in cash. No debt or significant liabilities will be assumed by Celularity in the Asset Sale Transaction.

Under the terms of the Asset Purchase Agreement, the Company will retain certain specified assets, including, among other things, cash, accounts receivable, and its hydrogel contract manufacturing business, including its SilverSeal and

Hydrex product lines.

The transactions contemplated by the Asset Purchase Agreement must be approved by the affirmative vote of a majority of the voting power of issued and outstanding shares of the Company's common stock. In addition, to the receipt of the approval of the Company's stockholders, each party's obligation to consummate the Asset Sale Transaction is conditioned upon certain other customary closing conditions.

*Senior Secured Term Loan Facility*

On February 5, 2018, the Company entered into the Forbearance and Amendment Agreement pursuant to which the lender agreed to defer the commencement of the Company's remaining principal payments and agreed to extend the forbearance period and to forbear from exercising any rights and remedies related to the Company's default of a covenant pertaining to (i) trailing twelve-month revenue under the Credit Agreement as of (A) September 30, 2016, (B) December 31, 2016 (C) March 31, 2017 (D) June 30, 2017 (E) September 30, 2017 and (F) December 31, 2017 and (ii) failure to maintain on a consolidated basis, a monthly minimum cash balance of at least \$2,000,000, until the earlier of April 30, 2018, the termination of the Asset Purchase Agreement, or the date when the lender becomes aware of any other default.