NeuroMetrix, Inc.
Form 10-Q
July 21, 2016

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

**(Mark One)**

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

**For the quarterly period ended June 30, 2016**

**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 001-33351**

**NEUROMETRIX, INC.**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware**<br>(State or other jurisdiction of<br>incorporation or organization) | **04-3308180**<br>(I.R.S. Employer<br>Identification No.) |
| **1000 Winter Street, Waltham, Massachusetts**<br>(Address of principal executive offices) | **02451**<br>(Zip Code) |

**(781) 890-9989**

(Registrant's telephone number, including area code)

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 x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 x No ¨

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

| | | | |
|---|---|---|---|
| Large accelerated filer ¨ | Accelerated filer ¨ | Non-accelerated filer ¨<br>(Do not check if a smaller reporting company) | Smaller reporting company x |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No x

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date:

5,118,273 shares of common stock, par value $0.0001 per share, were outstanding as of July 15, 2016.

**NeuroMetrix, Inc.**

**Form 10-Q**

**Quarterly Period Ended June 30, 2016**

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**PART I – FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**NeuroMetrix, Inc.**

**Balance Sheets**

**(Unaudited)**

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | $11,330,857 | $12,462,872 |
| Accounts receivable, net | 328,981 | 742,714 |
| Inventories | 1,048,053 | 1,089,084 |
| Prepaid expenses and other current assets | 1,070,855 | 852,600 |
| Total current assets | 13,778,746 | 15,147,270 |
| Fixed assets, net | 614,961 | 683,534 |
| Other long-term assets | 183,974 | 203,686 |
| Total assets | $14,577,681 | $16,034,490 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | $644,862 | $1,060,135 |
| Accrued compensation | 506,689 | 848,689 |
| Accrued expenses | 1,342,150 | 1,055,483 |
| Deferred revenue | 412,304 | 227,172 |
| Total current liabilities | 2,906,005 | 3,191,479 |
| Common stock warrants | 108,678 | 280,303 |
| Total liabilities | 3,014,683 | 3,471,782 |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock | — | — |
| Convertible preferred stock | 21 | 21 |
| | 492 | 405 |

| | | |
|---|---|---|
| Common stock, $0.0001 par value; 100,000,000 shares authorized; 4,918,273 and 4,047,332 shares issued and outstanding at June 30, 2016 and December 31, 2015, respectively | | |
| Additional paid-in capital | 183,318,910 | 176,127,932 |
| Accumulated deficit | (171,756,425) | (163,565,650) |
| Total stockholders' equity | 11,562,998 | 12,562,708 |
| Total liabilities and stockholders' equity | $14,577,681 | $16,034,490 |

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

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**NeuroMetrix, Inc.**

**Statements of Operations**

**(Unaudited)**

| | Quarters Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Revenues | $2,647,422 | $1,224,987 | $4,922,669 | $2,507,947 |
| Cost of revenues | 1,572,370 | 595,032 | 3,054,883 | 1,232,293 |
| Gross profit | 1,075,052 | 629,955 | 1,867,786 | 1,275,654 |
| Operating expenses: | | | | |
| Research and development | 1,127,850 | 982,253 | 2,284,640 | 1,884,795 |
| Sales and marketing | 2,832,279 | 1,762,282 | 5,240,158 | 3,217,968 |
| General and administrative | 1,292,305 | 1,224,822 | 2,716,646 | 2,770,912 |
| Total operating expenses | 5,252,434 | 3,969,357 | 10,241,444 | 7,873,675 |
| Loss from operations | (4,177,382) | (3,339,402) | (8,373,658) | (6,598,021) |
| Interest income | 4,553 | 500 | 11,258 | 1,589 |
| Change in fair value of warrant liability | 77,309 | 2,135,696 | 171,625 | 3,321,998 |
| Net loss | $(4,095,520) | $(1,203,206) | $(8,190,775) | $(3,274,434) |
| Net loss per common share applicable to common stockholders, basic and diluted | $(5.37) | $(2.07) | $(6.56) | $(3.13) |
| Weighted average number of common shares outstanding, basic and diluted | 4,456,712 | 2,297,308 | 4,273,535 | 2,183,546 |

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

**NeuroMetrix, Inc.**

**Statements of Cash Flows**

**(Unaudited)**

| | Six Months Ended June 30, 2016 | 2015 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $(8,190,775 ) | $(3,274,434 ) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation | 124,396 | 95,486 |
| Stock-based compensation | 121,989 | 172,402 |
| Change in fair value of warrant liability | (171,625 ) | (3,321,998 ) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 413,733 | (8,446 ) |
| Inventories | 41,031 | (541,860 ) |
| Prepaid expenses and other current and long-term assets | (198,543 ) | (165,454 ) |
| Accounts payable | (356,769 ) | 262,191 |
| Accrued expenses and compensation | 235,924 | 5,032 |
| Deferred revenue | 185,132 | 587,139 |
| Net cash used in operating activities | (7,795,507 ) | (6,189,942 ) |
| | | |
| Cash flows from investing activities: | | |
| Purchases of fixed assets | (55,823 ) | (503,028 ) |
| Net cash used in investing activities | (55,823 ) | (503,028 ) |
| | | |
| Cash flows from financing activities: | | |
| Net proceeds from issuance of stock and warrants, including public and private offerings and equity plans | 6,719,315 | 13,316,324 |
| Repurchase of Series A-4 preferred stock and warrants | — | (3,206,357 ) |
| Net cash provided by financing activities | 6,719,315 | 10,109,967 |
| | | |
| Net (decrease)/increase in cash and cash equivalents | (1,132,015 ) | 3,416,997 |
| Cash and cash equivalents, beginning of period | 12,462,872 | 9,221,985 |
| Cash and cash equivalents, end of period | $11,330,857 | $12,638,982 |
| Supplemental disclosure of cash flow information: | | |
| Common stock issued to settle employee incentive compensation obligation | $318,761 | $281,757 |

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

**NeuroMetrix, Inc.**

**Notes to Unaudited Financial Statements**

**June 30, 2015**

## 1. Business and Basis of Presentation

### Our Business-An Overview

NeuroMetrix, Inc., or the Company, a Delaware corporation, was founded in June 1996. The Company develops wearable medical technology and point-of-care tests that help patients and physicians better manage chronic pain, nerve diseases, and sleep disorders. The Company markets Quell ® and SENSUS® which are wearable therapeutic devices designed for relief of chronic, intractable pain. Quell was commercially launched in the United States during the second quarter of 2015. The Company also markets DPNCheck®, which is a quantitative nerve conduction test that is used by physicians and health care professionals to evaluate systemic neuropathies such as diabetic peripheral neuropathy, or DPN. The Company's historical neurodiagnostic business is based on the ADVANCE System which is a comprehensive platform for the performance of traditional nerve conduction studies and invasive electromyography procedures and which is primarily used in physician offices and clinics.

The accompanying financial statements have been prepared on a basis which assumes that the Company will continue as a going concern and which contemplates the realization of assets and satisfaction of liabilities and commitments in the normal course of business. The Company has suffered recurring losses from operations and negative cash flows from operating activities. At June 30, 2016, the Company had an accumulated deficit of $171.8 million. The Company held cash and cash equivalents of $11.3 million as of June 30, 2016. The Company believes that these resources and the cash to be generated from expected product sales will be sufficient to meet its projected operating requirements into the first quarter of 2017. The Company continues to face significant challenges and uncertainties and, as a result, the Company's available capital resources may be consumed more rapidly than currently expected due to (a) decreases in sales of the Company's products and the uncertainty of future revenues from new products; (b) changes the Company may make to the business that affect ongoing operating expenses; (c) changes the Company may make in its business strategy; (d) regulatory developments affecting the Company's existing products and products under development; (e) changes the Company may make in its research and development spending plans; and (f) other items affecting the Company's forecasted level of expenditures and use of cash resources. Accordingly, the Company will need to raise additional funds to support its operating and capital needs in the first quarter of 2017 and beyond. These factors raise substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. The Company intends to obtain additional funding through public or private financing, collaborative arrangements with strategic partners, or through additional credit lines or other debt financing sources to increase the funds available to fund operations. However, the Company may not be able to secure such financing in a timely manner or on favorable terms, if at all. Furthermore, if the Company issues equity or debt securities to raise additional funds, its existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of the Company’s existing stockholders. If the Company raises additional funds through collaboration, licensing or other similar arrangements, it may be necessary to relinquish valuable rights to its products or proprietary technologies, or grant licenses on terms that are not favorable to the Company. Without additional funds, the Company may be forced to delay, scale back or eliminate some of its sales and marketing efforts, research and development activities, or other operations and potentially delay product development in an effort to provide sufficient funds to continue its operations. If any of these events occurs, the Company’s ability to achieve its development and commercialization goals would be adversely affected.

Certain prior period amounts have been adjusted to reflect the Company's 1-for-4 reverse stock split effected December 2015.

**Unaudited Interim Financial Statements**

The accompanying unaudited balance sheet as of June 30, 2016, unaudited statements of operations for the quarters and six months ended June 30, 2016 and 2015 and the unaudited statements of cash flows for the six months ended June 30, 2016 and 2015 have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. The accompanying balance sheet as of December 31, 2015 has been derived from audited financial statements prepared at that date, but does not include all disclosures required by accounting principles generally accepted in the United States of America. In the opinion of management, the financial statements include all normal and recurring adjustments considered necessary for a fair statement of the Company’s financial position and operating results. Operating results for the quarter ended June 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016 or any other period. These financial statements and notes should be read in conjunction with the financial statements for the year ended December 31, 2015 included in the Company’s Annual Report on Form 10-K, as filed with the Securities and Exchange Commission, or the SEC, on February 12, 2016 (File No. 001-33351), or the Company’s 2015 Form 10-K.

**Revenues**

The Company recognizes revenue when the following criteria have been met: persuasive evidence of an arrangement exists, delivery has occurred and risk of loss has passed, the seller’s price to the buyer is fixed or determinable, and collection is reasonably assured. Revenues associated with the Company’s medical devices and consumables are generally recognized upon shipment, assuming all other revenue recognition criteria have been met. Revenue associated with shipments made to distributors who have the right to return any unsold product is recognized once the product is sold by the distributor to the end customer (i.e. under a sell-through model), assuming all other revenue recognition criteria have been met. Cash received prior to all the conditions for revenue recognition being met is recorded as deferred revenue. Deferred revenue recorded prior to cash receipt is recorded as an offset to accounts receivable.

As of June 30, 2016 the total value of shipments made to sell-through distributors but not yet sold through to end customers totaled $979,000. Of this total, $566,696 was recorded as a reduction to accounts receivable and $412,304 was recorded in deferred revenue, as cash had been received. As of December 31, 2015, the total value of shipments that had been made to sell-through distributors but have not yet been sold through to end customers totaled $489,467. Of this total, $262,295 was recorded as a reduction to accounts receivable and $227,172 was recorded in deferred revenue, as cash had been received. Related costs of goods sold of $713,000 and $378,440 have been deferred and recorded in prepaid expenses and other current assets as of June 30, 2016 and December 31, 2015, respectively.

Revenue recognition involves judgments, including assessments of expected returns from customers who have the right to return product for any reason under 30-day or 60-day rights of return. Where the Company can reasonably estimate future returns, it recognizes revenues and records as a reduction of revenue a provision for estimated returns. The Company analyzes various factors, including its historical product returns in arriving at this judgment. Changes in judgments or estimates could materially impact the timing and amount of revenues and costs recognized. The provision for expected returns recorded as a reduction to accounts receivable was $215,535 and $65,111 as of June 30, 2016 and December 31, 2015, respectively.

Accounts receivable are recorded net of the allowance for doubtful accounts which represents the Company’s best estimate of probable credit losses. Allowance for doubtful accounts was $25,000 as of June 30, 2016 and December 31, 2015.

One customer accounted for approximately 11% and 12% of total revenue for the three-months and six-months ended June 30, 2016, respectively, and for approximately 20% and 21% of total revenue for the three-months and six-months ended June 30, 2015, respectively. Two customers accounted for 37% and one different customer accounted for 46% of accounts receivables as of June 30, 2016 and December 31, 2015, respectively.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make significant estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during reporting periods. Actual results could differ from those estimates.

**Recent Accounting Pronouncements**

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, *Leases (Topic 842)* (“ASU 2016-02”). ASU 2016-02 requires that lessees will need to recognize virtually all of their leases on the balance sheet, by recording a right-of-use asset and lease liability. The provisions of this guidance are effective for annual periods beginning after December 31, 2018, and for interim periods therein. The Company is in the process of evaluating the new standard and assessing the impact, if any, ASU 2016-02 will have on the Company’s Financial Statements.

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, *Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern (*“ASU 2014-15”). ASU 2014-15 requires management to assess an entity’s ability to continue as a going concern, and to provide related footnote disclosures in certain circumstances. The standard is effective for public entities for annual and interim periods beginning after December 15, 2016, with early adoption permitted. The Company is evaluating the provisions of ASU 2014-15 and assessing the impact, if any, it may have on the Company’s Financial Statements.

In May 2014, the FASB and the International Accounting Standards Board (“IASB”) jointly issued Accounting Standards Update (“ASU”) No. 2014-09, *Revenue from Contracts with Customers* (“ASU 2014-09”), a comprehensive new revenue recognition standard that will supersede nearly all existing revenue recognition guidance. The objective of ASU 2014-09 is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers,* which delayed the effective date of the new standard from January 1, 2017 to January 1, 2018. An entity can elect to adopt ASU 2014-09 using one of two methods, either full retrospective adoption to each prior reporting period, or recognizing the cumulative effect of adoption at the date of initial application. In March 2016, the FASB issued ASU No. 2016-08, *Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)*, which clarifies the implementation guidance on principal versus agent considerations. The Company is in the process of evaluating the new standard and assessing the impact, if any, ASU 2014-09 will have on the Company’s Financial Statements or which adoption method will be used.

## 2. Comprehensive Loss

For the quarters and six months ended June 30, 2016 and 2015, the Company had no components of other comprehensive income or loss other than net loss itself.

## 3. Net Loss Per Common Share

Basic net loss per common share is computed by dividing net loss by the weighted average number of common shares outstanding during the period. Unvested restricted shares, although legally issued and outstanding, are not considered outstanding for purposes of calculating basic net income per share. Diluted net loss per common share is computed by dividing net loss by the weighted average number of common shares outstanding during the period plus the dilutive effect of the weighted average number of outstanding instruments such as options, warrants, and restricted stock. Because the Company has reported a net loss for all periods presented, diluted loss per common share is the same as basic loss per common share, as the effect of utilizing the fully diluted share count would have reduced the net loss per common share. Therefore, in calculating net loss per share amounts, shares underlying the following potentially dilutive weighted average number of common stock equivalents were excluded from the calculation of diluted net income per common share because their effect was anti-dilutive for each of the periods presented:

| | Quarters Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Options | 218,259 | 205,457 | 216,188 | 199,889 |
| Warrants | 18,811,918 | 2,339,584 | 17,314,155 | 1,697,000 |
| Unvested restricted stock | — | 114 | — | 161 |
| Convertible preferred stock | 6,901,868 | 2,225,327 | 6,244,269 | 1,999,788 |
| Total | 25,932,045 | 4,770,482 | 23,774,612 | 3,896,838 |

The deemed dividend recorded in the June 2016 Offering (as defined below) represented the fair value of consideration transferred plus the fair value of repurchased Series C Preferred Stock, less the fair value of the newly issued Series D Preferred Stock and warrants. The Beneficial Conversion Feature, or BCF, recorded in the May 2015 Offering (as defined below) has been recognized as deemed dividends. These items have been reflected as an adjustment in the calculation of earnings per share. See Note 9, Stockholders' Equity, for further details.

| | Quarters Ended June 30, | | Six Months Ended June 30, | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Net loss | $(4,095,520) | $(1,203,206) | $(8,190,775) | $(3,274,434) |
| Deemed dividend attributable to preferred stockholders in connection with beneficial conversion features | — | (4,140,446) | — | (4,140,446) |
| Deemed dividend attributable to preferred stockholders in connection with preferred stock modifications | (19,846,377) | — | (19,846,377) | — |
| Return of capital to common shareholders attributable to the repurchase of preferred shares and related embedded beneficial conversion feature | — | 589,751 | — | 589,751 |
| Net loss applicable to common stockholders | $(23,941,897) | $(4,753,901) | $(28,037,152) | $(6,825,129) |
| Net loss per common share applicable to common stockholders, basic and diluted | $(5.37) | $(2.07) | $(6.56) | $(3.13) |
| Weighted average number of common shares outstanding, basic and diluted | 4,456,712 | 2,297,308 | 4,273,535 | 2,183,546 |

## 4. Inventories

Inventories consist of the following:

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Purchased components | $466,346 | $ 432,437 |
| Finished goods on consignment | 5,789 | 39,784 |
| Finished goods | 575,918 | 616,863 |
| | $1,048,053 | $ 1,089,084 |

## 5. Accrued Expenses

Accrued expenses consist of the following:

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Technology fees | $450,000 | $ 450,000 |
| Professional services | 327,930 | |