NEOPROBE CORP
Form 10QSB
November 14, 2007

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

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**FORM 10-QSB**

(Mark One)

x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2007

o TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE EXCHANGE ACT
For the transition period from to __________ to __________
Commission file number 0-26520

**NEOPROBE CORPORATION**

(Exact name of small business issuer as specified in its charter)

| | |
|---|---|
| Delaware | 31-1080091 |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |

425 Metro Place North, Suite 300, Dublin, OH 43017-1367

(Address of principal executive offices)
(614) 793-7500

(Issuer s telephone number)

(Former name, former address and former fiscal year, if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

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

Yes o No x

State the number of shares outstanding of each of the issuer s classes of common equity, as of the latest practicable date: 66,884,202 shares of common stock, par value $.001 per share (as of the close of business on November 9, 2007).

Transitional Small Business Disclosure Format (Check one):

Yes o No x

**NEOPROBE CORPORATION and SUBSIDIARIES**
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**PART I Financial Information**

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**PART I FINANCIAL INFORMATION**
**Item 1. Financial Statements**
**Neoprobe Corporation and Subsidiaries**
**Consolidated Balance Sheets**

| **ASSETS** | **September 30, 2007 (unaudited)** | **December 31, 2006** |
|---|---|---|
| Current assets: | | |
| Cash | $ 1,219,101 | $ 2,502,655 |
| Accounts receivable, net | 1,387,453 | 1,246,089 |
| Inventory | 1,024,966 | 1,154,376 |
| Prepaid expenses and other | 233,468 | 430,623 |
| Total current assets | 3,864,988 | 5,333,743 |
| Property and equipment | 2,342,856 | 2,238,050 |
| Less accumulated depreciation and amortization | 2,008,655 | 1,882,371 |
| | 334,201 | 355,679 |
| Patents and trademarks | 3,121,636 | 3,131,391 |
| Acquired technology | 237,271 | 237,271 |
| | 3,358,907 | 3,368,662 |
| Less accumulated amortization | 1,701,400 | 1,540,145 |
| | 1,657,507 | 1,828,517 |
| Other assets | 195,596 | 515,593 |
| Total assets | $ 6,052,292 | $ 8,033,532 |

**Continued**

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**Neoprobe Corporation and Subsidiaries**
**Consolidated Balance Sheets, continued**

| LIABILITIES AND STOCKHOLDERS DEFICIT | September 30, 2007 (unaudited) | December 31, 2006 |
|---|---|---|
| Current liabilities: | | |
| Accounts payable | $ 780,950 | $ 668,288 |
| Accrued liabilities and other | 844,107 | 544,215 |
| Capital lease obligations, current portion | 14,872 | 14,841 |
| Deferred revenue, current portion | 263,850 | 348,568 |
| Notes payable to finance companies | - | 136,925 |
| Note payable to CEO, net of discount of $130,567 | 869,433 | - |
| Notes payable to investors, current portion, net of discounts of $270,818 and $53,585, respectively | 3,154,182 | 1,696,415 |
| Total current liabilities | 5,927,394 | 3,409,252 |
| Capital lease obligations, net of current portion | 5,683 | 17,014 |
| Deferred revenue, net of current portion | 70,388 | 40,495 |
| Note payable to CEO, net of discount of $12,398 and $19,030, respectively | 87,602 | 80,970 |
| Notes payable to investors, net of current portion and discounts of $481,298 and $1,468,845, respectively | 2,018,702 | 4,781,155 |
| Other liabilities | 29,879 | 2,673 |
| Total liabilities | 8,139,648 | 8,331,559 |
| Commitments and contingencies | | |
| Stockholders deficit: | | |
| Preferred stock; $.001 par value; 5,000,000 shares authorized at September 30, 2007 and December 31, 2006; none issued and outstanding | - | - |
| Common stock; $.001 par value; 150,000,000 shares authorized, 65,084,134 and 59,624,379 shares issued and outstanding at September 30, 2007 and December 31, 2006, respectively | 65,084 | 59,624 |
| Additional paid-in capital | 136,723,196 | 135,330,668 |
| Accumulated deficit | (138,875,636) | (135,688,319) |
| Total stockholders deficit | (2,087,356) | (298,027) |
| Total liabilities and stockholders deficit | $ 6,052,292 | $ 8,033,532 |

See accompanying notes to the consolidated financial statements.

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**Neoprobe Corporation and Subsidiaries**
**Consolidated Statements of Operations**
**(unaudited)**

| | Three Months Ended September 30, 2007 | Three Months Ended September 30, 2006 | Nine Months Ended September 30, 2007 | Nine Months Ended September 30, 2006 |
|---|---|---|---|---|
| Net sales | $ 1,985,049 | $ 957,952 | $ 5,245,799 | $ 4,179,861 |
| Cost of goods sold | 836,436 | 403,190 | 2,325,772 | 1,741,172 |
| Gross profit | 1,148,613 | 554,762 | 2,920,027 | 2,438,689 |
| Operating expenses: | | | | |
| Research and development | 548,455 | 1,241,899 | 2,287,600 | 2,718,655 |
| Selling, general and administrative | 690,206 | 651,419 | 2,123,075 | 2,257,714 |
| Total operating expenses | 1,238,661 | 1,893,318 | 4,410,675 | 4,976,369 |
| Loss from operations | (90,048) | (1,338,556) | (1,490,648) | (2,537,680) |
| Other income (expenses): | | | | |
| Interest income | 12,601 | 56,520 | 56,858 | 184,511 |
| Interest expense | (862,762) | (371,013) | (1,749,609) | (1,090,973) |
| Other | (1,569) | (3,318) | (3,918) | (1,296) |
| Total other expenses | (851,730) | (317,811) | (1,696,669) | (907,758) |
| Net loss | $ (941,778) | $ (1,656,367) | $ (3,187,317) | $ (3,445,438) |
| Net loss per common share: | | | | |
| Basic | $ (0.01) | $ (0.03) | $ (0.05) | $ (0.06) |
| Diluted | $ (0.01) | $ (0.03) | $ (0.05) | $ (0.06) |
| Weighted average shares outstanding: | | | | |
| Basic | 63,756,043 | 58,560,046 | 61,687,077 | 58,543,859 |
| Diluted | 63,756,043 | 58,560,046 | 61,687,077 | 58,543,859 |

See accompanying notes to the consolidated financial statements.

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**Neoprobe Corporation and Subsidiaries**
**Consolidated Statements of Cash Flows**
**(unaudited)**

| | Nine Months Ended September 30, 2007 | 2006 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net loss | $ (3,187,317) | $ (3,445,438) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization | 306,143 | 301,877 |
| Amortization of debt discount and debt offering costs | 1,077,365 | 595,500 |
| Stock compensation expense | 77,608 | 178,844 |
| Other | 34,020 | 30,146 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (141,364) | 10,215 |
| Inventory | 53,896 | (319,433) |
| Prepaid expenses and other assets | 154,489 | 424,560 |
| Accounts payable | 112,662 | 235,740 |
| Accrued liabilities and other liabilities | 339,099 | (564,501) |
| Deferred revenue | (54,825) | 59,342 |
| Net cash used in operating activities | (1,228,224) | (2,493,148) |
| Cash flows from investing activities: | | |
| Maturities of available-for-sale securities | - | 1,531,000 |
| Purchases of property and equipment | (36,872) | (71,282) |
| Proceeds from sales of property and equipment | - | 4,097 |
| Patent and trademark costs | (5,889) | (26,898) |
| Net cash (used in) provided by investing activities | (42,761) | 1,436,917 |
| Cash flows from financing activities: | | |
| Proceeds from issuance of common stock | 1,300,000 | - |
| Payment of stock offering costs | (21,510) | - |
| Proceeds from note payable | 1,000,000 | - |
| Payment of debt issuance costs | (67,833) | (30,000) |
| Payment of notes payable | (2,211,926) | (197,054) |
| Payments under capital leases | (11,300) | (14,444) |
| Net cash used in financing activities | (12,569) | (241,498) |
| Net decrease in cash | (1,283,554) | (1,297,729) |

| | | |
|---|---|---|
| Cash, beginning of period | 2,502,655 | 4,940,946 |
| Cash, end of period | $ 1,219,101 | $ 3,643,217 |

See accompanying notes to the consolidated financial statements.

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## Notes to the Consolidated Financial Statements
## (unaudited)

### 1. Basis of Presentation

The information presented as of September 30, 2007 and for the three-month and nine-month periods ended September 30, 2007 and September 30, 2006 is unaudited, but includes all adjustments (which consist only of normal recurring adjustments) that the management of Neoprobe Corporation (Neoprobe, the Company, or we) believes to be necessary for the fair presentation of results for the periods presented. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. The results for the interim periods are not necessarily indicative of results to be expected for the year. The consolidated financial statements should be read in conjunction with Neoprobe s audited consolidated financial statements for the year ended December 31, 2006, which were included as part of our Annual Report on Form 10-KSB.

Our consolidated financial statements include the accounts of Neoprobe, our wholly-owned subsidiary, Cardiosonix Ltd. (Cardiosonix), and our 90%-owned subsidiary, Cira Biosciences, Inc. (Cira Bio). All significant inter-company accounts were eliminated in consolidation.

### 2. Stock-Based Compensation

At September 30, 2007, we have three stock-based compensation plans. Under the Amended and Restated Stock Option and Restricted Stock Purchase Plan (the Amended Plan), the 1996 Stock Incentive Plan (the 1996 Plan), and the 2002 Stock Incentive Plan (the 2002 Plan), we may grant incentive stock options, nonqualified stock options, and restricted stock awards to full-time employees, and nonqualified stock options and restricted awards may be granted to our consultants and agents. Total shares authorized under each plan are 2 million shares, 1.5 million shares and 5 million shares, respectively. Although options are still outstanding under the Amended Plan and the 1996 Plan, these plans are considered expired and no new grants may be made from them. Under all three plans, the exercise price of each option is greater than or equal to the closing market price of our common stock on the day prior to the date of the grant.

Options granted under the Amended Plan, the 1996 Plan and the 2002 Plan generally vest on an annual basis over one to three years. Outstanding options under the plans, if not exercised, generally expire ten years from their date of grant or 90 days from the date of an optionee s separation from employment with us.

Compensation cost arising from stock-based awards is recognized as expense using the straight-line method over the vesting period. As of September 30, 2007, there was approximately $63,000 of total unrecognized compensation cost related to unvested stock-based awards, which we expect to recognize over remaining weighted average vesting terms of 0.7 years. For the three-month periods ended September 30, 2007 and 2006, our total stock-based compensation expense was approximately $10,000 and $40,000, respectively. For the nine-month periods ended September 30, 2007 and 2006, our total stock-based compensation expense was approximately $78,000 and $179,000, respectively. We have not recorded any income tax benefit related to stock-based compensation in any of the three-month and nine-month periods ended September 30, 2007 and 2006.

The fair value of each option award is estimated on the date of grant using the Black-Scholes option pricing model to value share-based payments. Expected volatilities are based on the Company s historical volatility, which management believes represents the most accurate basis for estimating expected volatility under the current circumstances. Neoprobe uses historical data to estimate forfeiture rates. The expected term of options granted is based on the vesting period and the contractual life of the options. The risk-free rate is based on the U.S. Treasury yield in effect at the time of the grant.

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A summary of stock option activity under our stock option plans as of September 30, 2007, and changes during the nine-month period then ended is presented below:

| | Nine Months Ended September 30, 2007 | | | |
|---|---|---|---|---|
| | Number of Options | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life | Aggregate Intrinsic Value |
| Outstanding at beginning of period | 5,975,473 | $ 0.42 | | |
| Granted | 40,000 | $ 0.35 | | |
| Exercised | - | - | | |
| Forfeited | (116,667) | $ 0.32 | | |
| Expired | (403,333) | $ 0.42 | | |
| Outstanding at end of period | 5,495,473 | $ 0.42 | 5.1 years | - |
| Exercisable at end of period | 4,586,473 | $ 0.45 | 4.6 years | - |

**3. Comprehensive Income (Loss)**

We had no accumulated other comprehensive income (loss) activity during the three-month and nine-month periods ended September 30, 2007, thus our total comprehensive loss was equal to our net loss for those periods. Due to our net operating loss position, there are no income tax effects on comprehensive income (loss) components for the three-month and nine-month periods ended September 30, 2006.

| | Three Months Ended September 30, 2006 | Nine Months Ended September 30, 2006 |
|---|---|---|
| Net loss | $ (1,656,367) | $ (3,445,438) |
| Unrealized losses on securities | - | (2,018) |
| Total comprehensive loss | $ (1,656,367) | $ (3,447,456) |

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## 4. Earnings Per Share

Basic earnings (loss) per share is calculated using the weighted average number of common shares outstanding during the periods. Diluted earnings (loss) per share is calculated using the weighted average number of common shares outstanding during the periods, adjusted for the effects of convertible securities, options and warrants, if dilutive.

| | Three Months Ended September 30, 2007 | | Three Months Ended September 30, 2006 | |
|---|---|---|---|---|
| | Basic Earnings Per Share | Diluted Earnings Per Share | Basic Earnings Per Share | Diluted Earnings Per Share |
| Outstanding shares | 65,084,134 | 65,084,134 | 58,690,046 | 58,690,046 |
| Effect of weighting changes in outstanding shares | (1,328,091) | (1,328,091) | - | - |
| Contingently issuable shares | - | - | (130,000) | (130,000) |
| Adjusted shares | 63,756,043 | 63,756,043 | 58,560,046 | 58,560,046 |
| Number of anti-dilutive common shares excluded | 40,354,155 | 40,354,155 | 41,365,016 | 41,365,016 |

| | Nine Months Ended September 30, 2007 | | Nine Months Ended September 30, 2006 | |
|---|---|---|---|---|
| | Basic Earnings Per Share | Diluted Earnings Per Share | Basic Earnings Per Share | Diluted Earnings Per Share |
| Outstanding shares | 65,084,134 | 65,084,134 | 58,690,046 | 58,690,046 |
| Effect of weighting changes in outstanding shares | (3,397,057) | (3,397,057) | (16,187) | (16,187) |
| Contingently issuable shares | - | - | (130,000) | (130,000) |
| Adjusted shares | 61,687,077 | 61,687,077 | 58,543,859 | 58,543,859 |
| Number of anti-dilutive common shares excluded | 40,354,155 | 40,354,155 | 41,365,016 | 41,365,016 |

There is no difference in basic and diluted loss per share related to the three-month and nine-month periods ended September 30, 2007 and 2006. The net loss per common share for these periods excludes the effects of common shares issuable upon exercise of outstanding stock options and warrants into our common stock or upon the conversion of convertible debt since such inclusion would be anti-dilutive.

**5. Inventory**

We capitalize certain inventory costs associated with our Lymphoseek® product prior to regulatory approval and product launch, based on management s judgment of probable future commercial use and net realizable value. We could be required to permanently write down previously capitalized costs related to pre-approval or pre-launch inventory upon a change in such judgment, due to a denial or delay of approval by regulatory bodies, a delay in commercialization, or other potential factors. Conversely, our gross margins may be favorably impacted if some or all of the inventory previously written down becomes available and is used for commercial sale. During the nine-month

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periods ended September 30, 2007 and 2006, we capitalized $150,000 and $48,000, respectively, in inventory costs associated with our Lymphoseek product.

The components of inventory are as follows:

| | September 30, 2007 (unaudited) | December 31, 2006 |
|---|---|---|
| Materials and component parts | $ 352,995 | $ 522,225 |
| Work-in-process | 151,741 | 167,188 |
| Finished goods | 520,230 | 464,963 |