NeuroMetrix, Inc.
Form 10-Q
April 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 March 31, 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	**04-3308180**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1000 Winter Street, Waltham, Massachusetts (Address of principal executive offices)	**02451** (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 ¨ (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:

4,389,899 shares of common stock, par value $0.0001 per share, were outstanding as of April 15, 2016.

NeuroMetrix, Inc.

Form 10-Q

Quarterly Period Ended March 31, 2016

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

NeuroMetrix, Inc.

Balance Sheets

(Unaudited)

	March 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$8,739,651	$12,462,872
Accounts receivable, net of allowances of $87,714 and $90,111 at March 31, 2016 and December 31, 2015, respectively	491,259	742,714
Inventories	1,513,322	1,089,084
Prepaid expenses and other current assets	719,569	852,600
Total current assets	11,463,801	15,147,270
Fixed assets, net	650,539	683,534
Other long-term assets	193,830	203,686
Total assets	$12,308,170	$16,034,490
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$1,381,140	$1,060,135
Accrued compensation	800,148	848,689
Accrued expenses	1,084,846	1,055,483
Deferred revenue	3,823	227,172
Total current liabilities	3,269,957	3,191,479
Common stock warrants	185,987	280,303
Total liabilities	3,455,944	3,471,782
Commitments and contingencies (Note 6)		
Stockholders' equity:		
Preferred stock	—	—
Convertible preferred stock	14	21

Common stock, $0.0001 par value; 100,000,000 shares authorized at March 31, 2016 and December 31, 2015; 4,389,899 and 4,047,332 shares issued and outstanding at March 31, 2016 and December 31, 2015, respectively	439	405
Additional paid-in capital	176,512,678	176,127,932
Accumulated deficit	(167,660,905)	(163,565,650)
Total stockholders’ equity	8,852,226	12,562,708
Total liabilities and stockholders’ equity	$12,308,170	$16,034,490

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

NeuroMetrix, Inc.

Statements of Operations

(Unaudited)

	Quarters Ended March 31, 2016	2015
Revenues	$2,275,247	$1,282,960
Cost of revenues	1,482,513	637,261
Gross profit	792,734	645,699
Operating expenses:		
Research and development	1,156,790	902,542
Sales and marketing	2,407,879	1,455,686
General and administrative	1,424,341	1,546,090
Total operating expenses	4,989,010	3,904,318
Loss from operations	(4,196,276)	(3,258,619)
Interest income	6,705	1,089
Change in fair value of warrant liability	94,316	1,186,302
Net loss	$(4,095,255)	$(2,071,228)
Net loss per common share, basic and diluted	$(1.00)	$(1.00)
Weighted average number of common shares outstanding, basic and diluted	4,090,358	2,068,521

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

NeuroMetrix, Inc.

Statements of Cash Flows

(Unaudited)

	Quarters Ended March 31, 2016	2015
Cash flows from operating activities:		
Net loss	$(4,095,255)	$(2,071,228)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	61,638	29,144
Stock-based compensation	66,012	83,999
Change in fair value of warrant liability	(94,316)	(1,186,302)
Changes in operating assets and liabilities:		
Accounts receivable	251,455	(341,355)
Inventories	(424,238)	44,577
Prepaid expenses and other current assets	142,887	344,874
Accounts payable	379,509	311,487
Accrued expenses and compensation	317,732	197,589
Deferred revenue	(223,349)	(56,466)
Net cash used in operating activities	(3,617,925)	(2,643,681)
Cash flows from investing activities:		
Purchases of fixed assets	(28,643)	(175,181)
Net cash used in investing activities	(28,643)	(175,181)
Cash flows from financing activities:		
Payments from issuance of stock and warrants, including public offering and equity plans	(76,653)	—
Net cash used in financing activities	(76,653)	—
Net decrease in cash and cash equivalents	(3,723,221)	(2,818,862)
Cash and cash equivalents, beginning of period	12,462,872	9,221,985
Cash and cash equivalents, end of period	$8,739,651	$6,403,123
Supplemental disclosure of cash flow information:		
Common stock issued to settle employee incentive compensation obligation	$318,761	$281,757
Purchases of fixed assets in accounts payable	$—	$82,161

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

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NeuroMetrix, Inc.

Notes to Unaudited Financial Statements

March 31, 2016

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 March 31, 2016, the Company had an accumulated deficit of $167.7 million. The Company held cash and cash equivalents of $8.7 million as of March 31, 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 third quarter of 2016. 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 third quarter of 2016 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 March 31, 2016, unaudited statements of operations for the quarters ended March 31, 2016 and 2015 and the unaudited statements of cash flows for the quarters ended March 31, 2016 and 2015 have been prepared in accordance with accounting principles generally accepted in the United States of America (US GAAP) 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 US GAAP. 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 March 31, 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, including single use nerve specific electrodes and other accessories are generally recognized upon shipment, assuming all other revenue criteria have been met.

Revenue recognition involves judgments, including assessments of expected returns and expected customer relationship periods. The Company analyzes various factors, including a review of specific transactions, its historical product returns, average customer relationship periods, customer usage, customer balances, and market and economic conditions. Changes in judgments or estimates on these factors could materially impact the timing and amount of revenues and costs recognized. Should market or economic conditions deteriorate, the Company’s actual return or bad debt experience could exceed its estimate. Certain product sales are made with a 30-day or 60-day right of return. Where the Company can reasonably estimate future returns, it recognizes revenues upon shipment and records as a reduction of revenue a provision for estimated returns. Where the Company cannot reasonably estimate future returns, it defers revenues until it gains sufficient experience to estimate returns or until the right of return lapses. As of March 31, 2016 and December 31, 2015, shipments totaling $553,854 and $489,467, respectively, were deferred and recorded as a reduction to accounts receivable. Costs related to these shipments of $392,018 and $378,440 have been reclassified from inventory to prepaid expenses and other current assets as of March 31, 2016 and December 31, 2015, respectively.

Accounts receivable are recorded net of the allowance for doubtful accounts receivable. The allowance for doubtful accounts is the Company’s best estimate of the amount of probable credit losses in our existing accounts receivable. The Company reviews the allowance for doubtful accounts and determines the allowance based on an analysis of customer past payment history, product usage activity, and recent communications with the customer. Individual customer balances which are past due and over 90 days outstanding are reviewed individually for collectability. Account balances are written-off against the allowance when the Company feels it is probable the receivable will not be recovered. The Company does not have any off-balance sheet credit exposure related to our customers.

During the first quarter of 2016, two customers accounted for approximately 25% of total revenue. In comparison, in the first quarter of 2015, one customer accounted for approximately 21% of total revenue. One customer accounted for 27% and one different customer accounted for 46% of accounts receivables as of March 31, 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 Standard 842, *Leases* (ASC 842). ASC 842 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 does not know the effect, if any, ASC-842 will have on the Consolidated Financial Statements.

In November 2015, the FASB issued Accounting Standards Update No. 2015-17, *Balance Sheet Classification of Deferred Taxes* (ASU 2015-17). ASU 2015-17 requires that deferred income tax liabilities and assets be classified as noncurrent in the Company's balance sheet. The standard is effective for public entities for annual and interim periods beginning after December 15, 2016, with early adoption permitted. ASU 2015-17 was adopted on a prospective basis by the Company for the year ended December 31, 2015, thus resulting in the reclassification of $45,000 of current deferred tax liabilities to noncurrent on the accompanying consolidated balance sheet. The prior reporting period was not retrospectively adjusted. The adoption of this guidance had no impact on the Company's results of operations or cash flows.

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 financial position, results of operations or cash flows.

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. ASU 2014-09 will be effective for the first quarter of 2017. 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. The Company is in the process of evaluating the new standard and does not know the effect, if any, ASU 2014-09 will have on the Consolidated Financial Statements or which adoption method will be used.

2. Comprehensive Loss

For the quarters ended March 31, 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 March 31,	
	2016	2015
Options	214,117	202,314
Warrants	15,816,393	1,440,211
Unvested restricted stock	—	208
Convertible preferred stock	5,586,669	392,936
Total	21,617,179	2,035,669

4. Inventories

Inventories consist of the following:

	March 31, 2016	December 31, 2015
Purchased components	$667,457	$ 432,437
Finished goods on consignment	23,814	39,784
Finished goods	822,051	616,863
	$1,513,322	$ 1,089,084

5. Accrued Expenses

Accrued expenses consist of the following:

	March 31, 2016	December 31, 2015
Technology fees	$450,000	$ 450,000
Professional services	222,333	336,229
Consulting fees	185,000	92,000
Sales taxes	40,312	56,284
Personnel related obligations	75,881	15,548
Other	111,320	105,422
	$1,084,846	$ 1,055,483

6. Commitments and Contingencies

Operating Lease

In August 2014, the Company entered into a 5-year operating lease agreement with one 5-year extension option for manufacturing and order fulfillment facilities in Woburn, Massachusetts (the “Woburn Lease”). The Woburn Lease commenced December 15, 2014 and has a monthly base rent of $7,503. In September 2014, the Company entered into a 7-year operating lease agreement with one 5-year extension option for its corporate office and product development activities in Waltham, Massachusetts (the “Waltham Lease”). The term of the Waltham Lease commenced on February 20, 2015 and includes fixed payment obligations that escalate over the initial lease term. Average monthly base rent under the 7-year lease is approximately $37,792. These payment obligations were accrued and recognized over the term of occupancy. Under the Waltham Lease, the landlord was responsible for making certain improvements to the leased space at an agreed upon cost to the landlord. Total costs for the landlord improvements exceeded the agreed upon cost by $275,961. The landlord billed that excess cost to the Company as additional rent which has been included in other long term assets at March 31, 2016. This additional rent has been included in the net calculation of lease payments, so that rent expense is recognized on a straight-line basis over the term of occupancy.

7. Fair Value Measurements

The Fair Value Measurements and Disclosures Topic of the Codification defines fair value, establishes a framework for measuring fair value in applying generally accepted accounting principles, and expands disclosures about fair value measurements. This Codification topic identifies two kinds of inputs that are used to determine the fair value of assets and liabilities: observable and unobservable. Observable inputs are based on market data or independent sources while unobservable inputs are based on the Company's own market assumptions. Once inputs have been characterized, this Codification topic requires companies to prioritize the inputs used to measure fair value into one of three broad levels. Fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities. Fair values identified by Level 2 inputs utilize observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the related assets or liabilities. Fair values identified by Level 3 inputs are unobservable data points and are used to measure fair value to the extent that observable inputs are not available. Unobservable inputs reflect the Company's own assumptions about the assumptions that market participants would use at pricing the asset or liability.

The following tables present information about the Company's assets and liabilities that are measured at fair value on a recurring basis for the periods presented and indicates the fair value hierarchy of the valuation techniques it utilized to determine such fair value. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities. Fair values determined by Level 2 inputs utilize data points that are observable such as quoted prices, interest rates, and yield curves. Fair values determined by Level 3 inputs are unobservable data points for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability.

		Fair Value Measurements at March 31, 2016 Using		
	March 31,2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets:				
Cash equivalents	$ 4,982,025	$ 4,982,025	$ —	$ —
Total	$ 4,982,025	$ 4,982,025	$ —	—
Liabilities:				
Common stock warrants	$ 185,987	$ —	$ —	$ 185,987
Total	$ 185,987	$ —	$ —	$ 185,987

Due to the lack of market quotes relating to our common stock warrants, the fair value of the common stock warrants was determined at March 31, 2016 using the Black-Scholes model, which is based on Level 3 inputs. As of March 31, 2016, inputs used in the Black-Scholes model are presented below. The assumptions used may change as the underlying sources of these assumptions and market conditions change. Based on the Black-Scholes model, the

Company recorded a common stock warrants liability of $0.2 million at March 31, 2016.

	Black-Scholes Inputs to Warrant Liability Valuation at March 31, 2016					
Warrants:	Stock Price	Exercise Price	Expected Volatility	Risk-Free Interest	Expected Term	Dividends
2014 Offering	$ 1.83	$ 8.16	72.1 %	0.9 %	3yr 3mo	none
2013 Offering	$ 1.83	$ 8.00	64.1 %	0.8 %	2yr 2mo	none

The following table provides a summary of changes in the fair value of the Company’s Level 3 financial liabilities between December 31, 2015 and March 31, 2016

	2014 Offering	2013 Offering	Total
Balance at December 31, 2015	$ 227,992	$ 52,311	$280,303
Change in fair value of warrant liability	(65,266)	(29,050)	