

TRANSGENOMIC INC  
Form 10-Q  
November 16, 2015  
Table of Contents

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934  
For the quarterly period ended September 30, 2015

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: 000-30975

TRANSGENOMIC, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

91-1789357  
(I.R.S. Employer Identification No.)

12325 Emmet Street, Omaha, Nebraska  
(Address of principal executive offices)  
(402) 452-5400  
(Registrant's telephone number, including area code)

68164  
(Zip 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  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  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" and "smaller reporting 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

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

As of October 31, 2015, the number of shares of common stock outstanding was 13,915,691.



Table of Contents

TRANSGENOMIC, INC.  
INDEX

	Page No.
PART I. <u>FINANCIAL INFORMATION</u>	<u>3</u>
Item 1. <u>Financial Statements</u>	<u>3</u>
<u>Condensed Consolidated Balance Sheets at September 30, 2015 (Unaudited) and December 31, 2014</u>	<u>3</u>
<u>Unaudited Condensed Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2015 and 2014</u>	<u>4</u>
<u>Unaudited Condensed Consolidated Statements of Comprehensive Loss for the Three and Nine Months Ended September 30, 2015 and 2014</u>	<u>5</u>
<u>Unaudited Condensed Consolidated Statements of Stockholders' Equity for the Nine Months Ended September 30, 2015</u>	<u>6</u>
<u>Unaudited Condensed Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2015 and 2014</u>	<u>7</u>
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	<u>8</u>
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>25</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>33</u>
Item 4. <u>Controls and Procedures</u>	<u>33</u>
PART II. <u>OTHER INFORMATION</u>	<u>34</u>
Item 1. <u>Legal Proceedings</u>	<u>34</u>
Item 1A. <u>Risk Factors</u>	<u>34</u>
Item 6. <u>Exhibits</u>	<u>34</u>
<u>Signatures</u>	<u>37</u>

Table of Contents

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

TRANSGENOMIC, INC. AND SUBSIDIARY  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Dollars in thousands, except per share data)

	September 30, 2015 (unaudited)	December 31, 2014
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$2,787	\$1,609
Accounts receivable, net	9,252	5,389
Other current assets	534	1,050
Assets held for sale	3,531	5,599
Total current assets	16,104	13,647
<b>PROPERTY AND EQUIPMENT:</b>		
Equipment	5,596	7,590
Furniture, fixtures & leasehold improvements	1,566	1,855
	7,162	9,445
Less: accumulated depreciation	(6,859)	(8,087)
	303	1,358
<b>OTHER ASSETS:</b>		
Goodwill	6,918	6,918
Intangibles, net	1,000	7,879
Other assets	125	204
	\$24,450	\$30,006
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt	\$6,275	\$462
Accounts payable	3,732	3,898
Accrued compensation	566	682
Accrued expenses	2,368	2,295
Deferred revenue	137	298
Other liabilities	1,067	1,068
Liabilities held for sale	2,002	2,554
Total current liabilities	16,147	11,257
<b>LONG TERM LIABILITIES:</b>		
Long-term debt, less current maturities	525	7,375
Common stock warrant liability	175	145
Accrued preferred stock dividend	—	3,130
Other long-term liabilities	886	1,546
Total liabilities	17,733	23,453
<b>STOCKHOLDERS' EQUITY:</b>		
Preferred stock, \$0.01 par value, 15,000,000 shares authorized, 4,029,502 shares issued and outstanding	40	40
Common stock, \$0.01 par value, 150,000,000 shares authorized, 13,915,691 and 8,084,471 shares issued and outstanding, respectively	139	81
Additional paid-in capital	200,285	189,680
Accumulated other comprehensive income	326	340

Edgar Filing: TRANSGENOMIC INC - Form 10-Q

Accumulated deficit	(194,073	) (183,588	)
Total stockholders' equity	6,717	6,553	
	\$24,450	\$30,006	

See notes to unaudited condensed consolidated financial statements.

3

---

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY  
 UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (Dollars in thousands, except per share data)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
NET SALES	\$3,960	\$4,064	\$13,670	\$11,595
COST OF GOODS SOLD:	2,196	2,347	6,732	6,891
Gross profit	1,764	1,717	6,938	4,704
OPERATING EXPENSES:				
Selling, general and administrative	3,103	5,063	12,270	14,855
Research and development	561	641	1,704	2,171
Impairment of long-lived assets	7,024	—	7,024	—
	10,688	5,704	20,998	17,026
OPERATING LOSS FROM CONTINUING OPERATIONS	(8,924	) (3,987	) (14,060	) (12,322
OTHER INCOME (EXPENSE):				
Interest expense, net	(174	) (162	) (550	) (490
Warrant revaluation	385	(50	) (30	) 200
Other, net	(6	) (1	) (19	) (1
	205	(213	) (599	) (291
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	(8,719	) (4,200	) (14,659	) (12,613
INCOME TAX BENEFIT	(486	) (1,456	) (466	) (1,204
LOSS FROM CONTINUING OPERATIONS	(8,233	) (2,744	) (14,193	) (11,409
INCOME FROM DISCONTINUED OPERATIONS, NET OF TAXES	934	2,664	578	3,260
NET LOSS	(7,299	) (80	) (13,615	) (8,149
PREFERRED STOCK DIVIDENDS	(331	) (304	) (993	) (839
NET LOSS FROM CONTINUING OPERATIONS AVAILABLE TO COMMON STOCKHOLDERS	(8,564	) (3,048	) (15,186	) (12,248
NET INCOME FROM DISCONTINUED OPERATIONS AVAILABLE TO COMMON STOCKHOLDERS	934	2,664	578	3,260
NET LOSS AVAILABLE TO COMMON STOCKHOLDERS	\$(7,630	) \$(384	) \$(14,608	) \$(8,988
BASIC AND DILUTED LOSS PER COMMON SHARE FROM CONTINUING OPERATIONS	\$(0.62	) \$(0.41	) \$(1.29	) \$(1.67
BASIC AND DILUTED INCOME PER COMMON SHARE FROM DISCONTINUED OPERATIONS	\$0.07	\$0.36	\$0.05	\$0.44
BASIC AND DILUTED LOSS PER COMMON SHARE	\$(0.55	) \$(0.05	) \$(1.24	) \$(1.22
BASIC AND DILUTED WEIGHTED-AVERAGE SHARES OF COMMON STOCK OUTSTANDING	13,763,240	7,353,695	11,784,583	7,353,695

See notes to unaudited condensed consolidated financial statements.

4

---

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY  
 UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS  
 (Dollars in thousands)

	Three Months Ended September 30,		Nine Months Ended September 30,		
	2015	2014	2015	2014	
Net Loss	\$ (7,299	) \$ (80	) \$ (13,615	) \$ (8,149	)
Other comprehensive loss - foreign currency translation adjustment - discontinued operations	(22	) (45	) (14	) (11	)
Comprehensive Loss	\$ (7,321	) \$ (125	) \$ (13,629	) \$ (8,160	)

See notes to unaudited condensed consolidated financial statements.



Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY  
 UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY  
 Nine Months Ended  
 September 30, 2015  
 (Dollars in thousands, except per share data)

	Preferred Stock		Common Stock			Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total
	Outstanding Shares	Par Value	Outstanding Shares	Par Value					
Balance, December 31, 2014	4,029,502	\$40	8,084,471	\$81	\$189,680	\$ (183,588 )	\$ 340	\$6,553	
Net loss	—	—	—	—	—	(13,615 )	—	(13,615 )	
Foreign currency translation adjustment	—	—	—	—	—	—	(14 )	(14 )	
Stock-based compensation	—	—	—	—	527	—	—	527	
Private placement, net	—	—	5,047,411	50	8,919	—	—	8,969	
Conversion of convertible promissory notes	—	—	783,809	8	1,159	—	—	1,167	
Reversal of dividends on preferred stock	—	—	—	—	—	3,130	—	3,130	
Balance, September 30, 2015	4,029,502	\$40	13,915,691	\$139	\$200,285	\$ (194,073 )	\$ 326	\$6,717	

See notes to unaudited condensed consolidated financial statements.

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY  
 UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (Dollars in thousands)

	Nine Months Ended September 30,	
	2015	2014
<b>CASH FLOWS USED IN OPERATING ACTIVITIES:</b>		
Net loss	\$(13,615	) \$(8,149
Less income from discontinued operations, net of tax	578	3,260
Loss from continuing operations	(14,193	) (11,409
Adjustments to reconcile net loss to net cash flows used in operating activities:		
Depreciation and amortization	1,527	1,493
Stock-based compensation	489	997
Impairment of long-lived assets	7,024	—
Provision for losses on doubtful accounts	2,731	2,681
Warrant revaluation	30	(200
Loss on sale of fixed assets	14	—
Deferred interest	61	236
Deferred tax provision	122	590
Changes in operating assets and liabilities:		
Accounts receivable	(6,613	) (5,524
Other current assets	224	(312
Accounts payable	(162	) 547
Accrued expenses and other liabilities	(911	) (31
Net cash used in continuing operations	(9,657	) (10,932
Net cash provided by (used in) discontinued operations	229	(277
Net cash used in operating activities	(9,428	) (11,209
<b>CASH FLOWS PROVIDED BY INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(280	) (121
Other assets	(9	) (56
Net cash used in continuing operations	(289	) (177
Net cash provided by discontinued operations	1,910	3,650
Net cash provided by investing activities	1,621	3,473
<b>CASH FLOWS PROVIDED BY FINANCING ACTIVITIES:</b>		
Principal payments on capital lease obligations	(35	) (113
Issuance of preferred stock, net	—	6,906
Issuance of common stock, net	8,969	—
Proceeds from borrowings	923	6,440
Principal payment on note payable	(874	) (6,242
Net cash flows provided by financing activities	8,983	6,991
EFFECT OF FOREIGN CURRENCY EXCHANGE RATE CHANGES ON CASH	2	(1
NET CHANGE IN CASH AND CASH EQUIVALENTS	1,178	(746
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	1,609	1,626
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$2,787	\$880
<b>SUPPLEMENTAL CASH FLOW INFORMATION</b>		
Cash paid during the period for:		
Interest	\$365	\$181
<b>SUPPLEMENTAL DISCLOSURE OF NON-CASH INFORMATION</b>		

Conversion of convertible promissory notes	1,012	—
See notes to unaudited condensed consolidated financial statements.		

7

---

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
Three and Nine Months Ended September 30, 2015 and 2014

1. BUSINESS DESCRIPTION

Business Description.

Transgenomic, Inc. (“we”, “us”, “our”, the “Company” or “Transgenomic”) is a global biotechnology company advancing personalized medicine for the detection and treatment of cancer and inherited diseases through our proprietary molecular technologies and world-class clinical and research services. A key goal is to bring our Multiplexed ICE COLD-PCR (“MX-ICP”) product to the clinical market through strategic licensing agreements, enabling the use of blood and other bodily fluids for more effective and patient-friendly diagnosis, monitoring and treatment of cancer.

MX-ICP is a simple, proprietary technology that amplifies the ability to detect genetic mutations by 100 - 400 fold. This technology has been validated internally on all currently available sequencing platforms, including Sanger, Next Gen Sequencing and Digital PCR. By enhancing the level of detection of genetic mutations and suppressing the normal, “wild-type” DNA, several benefits are provided. It is generally understood that most current technologies are unable to consistently identify mutations that occur in less than approximately 5% of a sample. However, many mutations found at much lower levels, even down to 0.01%, are known to be clinically relevant and can have significant consequences to a patient: both in terms of how they will respond to a given drug or treatment and how a given tumor is likely to change over time. More importantly, in our view, significantly improving the level of detection while using blood, saliva and even urine as a source for DNA, rather than depending on painful, expensive and potentially dangerous tumor biopsies, is an important advancement in patient care with respect to cancer detection, treatment and monitoring and can result in significant cost savings for the healthcare system by replacing invasive procedures with the simple collection of blood or other bodily fluids. By broadening the types of samples that can be used for testing and allowing all sequencing platforms to provide improved identification of low level mutations, MX-ICP has the potential to make testing more patient friendly, enable genetic monitoring of disease progression, effectively guide treatment protocols, and reduce the overall cost of diagnosis and monitoring while improving patient outcomes.

Historically, our operations were organized and reviewed by management along our major product lines and presented in two business segments: Laboratory Services and Genetic Assays and Platforms. Beginning with the quarter ended September 30, 2015, our operations are now organized as one business segment, our Laboratory Services segment. Our laboratories specialize in genetic testing for cardiology, neurology and mitochondrial disorders, and for oncology. Our Patient Testing laboratories located in New Haven, Connecticut and Omaha, Nebraska are certified under the Clinical Laboratory Improvement Amendment (“CLIA”) as high complexity laboratories and our Omaha facility is accredited by the College of American Pathologists. Our Biomarker Identification laboratory located in Omaha provides pharmacogenomics research services supporting Phase II and Phase III clinical trials conducted by pharmaceutical and biotechnology companies. Our laboratories employ a variety of genomic testing service technologies, including our new, high performance MX-ICP technology. ICE COLD-PCR is a proprietary ultra-high sensitivity platform technology with breakthrough potential to enable wide adoption of personalized, precision medicine in cancer and other diseases. It can be run in any laboratory that contains standard PCR systems. MX-ICP enables detection of multiple known and unknown mutations from virtually any sample type, including tissue biopsies, blood, urine, saliva, cell-free DNA (“cfDNA”) and circulating tumor cells (“CTCs”) at levels greater than 1,000-fold higher than standard DNA sequencing techniques. It is easy to implement and use within existing workflows.

Our condensed consolidated balance sheets, statements of operations and statements of cash flows for all periods presented reflect our former Genetic Assays and Platforms activities as discontinued operations (See Note 3 - "Discontinued Operations").

#### Going Concern

The condensed consolidated financial statements have been prepared using accounting principles generally accepted in the United States of America applicable for a going concern, which assume that we will realize our assets and discharge our liabilities in the ordinary course of business. We have incurred substantial operating losses and have used cash in our operating activities for the past few years. As of September 30, 2015, we had negative working capital of \$43,000. Our ability to continue as a going concern is dependent upon a combination of generating additional revenue, improving cash collections, potentially selling underutilized assets and, if necessary, raising additional financing to meet our obligations and pay our liabilities arising from normal business operations when they come due. The outcome of these matters cannot be predicted with any certainty at this time and raises substantial doubt that we will be able to continue as a going concern. These condensed consolidated financial statements do not include any adjustments to the amounts and classification of assets and liabilities that may be necessary should we be unable to

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

continue as a going concern. We cannot be certain that additional financing will be available on acceptable terms, or at all, and our failure to raise capital when needed could limit our ability to continue our operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation.

The condensed consolidated balance sheet as of December 31, 2014 was derived from our audited balance sheet as of that date and has been adjusted for the reclassification of assets that are now held for sale. The accompanying condensed consolidated financial statements as of and for the three and nine months ended September 30, 2015 and 2014 are unaudited and reflect all adjustments (consisting of only normal recurring adjustments) that are, in the opinion of management, necessary for a fair presentation of the financial position and operating results for the interim periods. These unaudited condensed consolidated financial statements and notes should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2014 contained in our Annual Report on Form 10-K, filed with the Securities and Exchange Commission on April 15, 2015. The results of operations for the interim periods presented are not necessarily indicative of the results for fiscal year 2015. Certain prior year amounts have been reclassified to conform to the current year presentation in our condensed consolidated financial statements, which consists of the effects of reclassifications from the presentation of our discontinued operations.

Principles of Consolidation.

The condensed consolidated financial statements include the accounts of Transgenomic, Inc. and our wholly owned subsidiary. All inter-company balances and transactions have been eliminated in consolidation.

Risks and Uncertainties.

Certain risks and uncertainties are inherent in our day-to-day operations and in the process of preparing our financial statements. The more significant of those risks are presented below and throughout the notes to the unaudited condensed consolidated financial statements.

Use of Estimates.

The preparation of condensed consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of net sales and expenses during the reporting period. In addition, estimates and assumptions associated with the determination of the fair value of certain assets and related impairments require considerable judgment by management. Actual results could differ from the estimates and assumptions used in preparing these condensed consolidated financial statements.

Fair Value.

Unless otherwise specified, book value approximates fair market value. The common stock warrant liability is recorded at fair value. See Note 9 - "Fair Value" for additional information.

Cash and Cash Equivalents.

Cash and cash equivalents include cash and investments with original maturities at the date of acquisition of three months or less.

Concentrations of Cash.

From time to time, we may maintain a cash position with financial institutions in amounts that exceed federally insured limits. We have not experienced any losses on such accounts as of September 30, 2015.

Accounts Receivable.

The following is a summary of activity for the allowance for doubtful accounts during the three and nine months ended September 30, 2015 and 2014:



Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

	Dollars in Thousands			
	Beginning Balance	Additions	Deductions	Ending Balance
Three Months Ended September 30, 2015	\$8,158	\$1,057	\$(175)	) \$9,040
Three Months Ended September 30, 2014	\$3,700	\$1,158	\$(400)	) \$4,458
Nine Months Ended September 30, 2015	\$7,679	\$3,787	\$(2,426)	) \$9,040
Nine Months Ended September 30, 2014	\$3,497	\$2,681	\$(1,720)	) \$4,458

While payment terms are generally 30 days, we have also provided extended payment terms in certain cases. In addition, we operate globally and the payment terms for some of our international customers may be greater than 90 days. Accounts receivable are carried at original invoice amount and shown net of allowance for doubtful accounts and contractual allowances. The estimate made for doubtful accounts is based on a review of all outstanding amounts on a quarterly basis. The estimate for contractual allowances is based on contractual terms or historical reimbursement rates and is recorded when revenue is recorded. We determine the allowance for doubtful accounts and contractual allowances by regularly evaluating individual payor receivables and considering a payor's financial condition, credit history, reimbursement rates and current economic conditions. Accounts receivable are written off when deemed uncollectible and after all collection efforts have been exhausted. Recoveries of accounts receivable previously written off are recorded as a reduction in bad debt expense when received.

**Property and Equipment.**

Property and equipment are carried at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the related assets as follows:

Leasehold improvements	1 to 10 years
Furniture and fixtures	3 to 7 years
Production equipment	3 to 7 years
Computer equipment	3 to 7 years
Research and development equipment	2 to 7 years

Depreciation expense related to property and equipment was \$0.1 million for each of the three months ended September 30, 2015 and 2014, which included \$0.1 million related to equipment acquired under capital leases during each period. Depreciation expense related to property and equipment was \$0.3 million for each of the nine months ended September 30, 2015 and 2014. Included in depreciation expense for each of the nine months ended September 30, 2015 and 2014 was \$0.2 million related to equipment acquired under capital leases.

We test our property and equipment for impairment when factors are present that indicate the carrying value of an asset (group) may not be recoverable. As part of our review for impairment of long-lived assets at September 30, 2015, we recorded an impairment charge of approximately \$0.9 million related to property and equipment during the three months ended September 30, 2015. See Note 4 - "Intangibles and Other Assets" for further discussion regarding the impairment of our long-lived assets.

**Goodwill and Intangible Assets.**

Goodwill is tested for impairment annually. We perform this impairment analysis during the fourth quarter of each year or whenever events indicate that the carrying amount of goodwill may not be recoverable. We test our intangible assets for impairment when factors are present that indicate the carrying value of an intangible asset (group) may not be recoverable. Impairment occurs when the carrying value is determined to be not recoverable, thereby causing the carrying value of the goodwill or intangible asset (group) to exceed its fair value. If impaired, the asset's carrying value is reduced to its fair value. We performed an interim testing of impairment of goodwill and long-lived assets as of September 30, 2015, due to the significant decline in the market price of our stock. As a result of this testing, we



recorded impairment charges related to our long-lived assets during the three months ended September 30, 2015 but determined that no impairment of goodwill was needed to be recorded. See Note 4 - "Intangibles and Other Assets" for further discussion regarding the impairment of our long-lived assets.

Stock-Based Compensation.

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

All stock-based awards to date have exercise prices equal to the market value of the shares at the date of grant and have 10-year contractual terms. Unvested awards as of September 30, 2015 had vesting periods of up to three years from the date of grant. None of the awards outstanding at September 30, 2015 are subject to performance or market-based vesting conditions.

We measure and recognize compensation expense for all stock-based awards made to employees and directors. Compensation expense is based on the calculated fair value of the awards as measured at the grant date and is expensed over the service period of the awards.

During the three and nine months ended September 30, 2015, we recorded compensation expense for all stock awards of \$0.2 million and \$0.5 million, respectively, within selling, general and administrative expense. During the three and nine months ended September 30, 2014, we recorded compensation expense for all stock awards of \$0.4 million and \$1.0 million, respectively. As of September 30, 2015, the unrecognized compensation expense related to unvested stock awards was \$0.6 million, which is expected to be recognized over a weighted-average period of 1.4 years.

We granted stock options to purchase an aggregate of 33,550 shares of our common stock during the quarter ended September 30, 2015. The fair value of the stock options granted was estimated on the grant date using the Black-Scholes option pricing model with the following assumptions: risk-free interest rates of 1.91% based on the U.S. Treasury yield in effect at the time of grant; dividend yields of zero percent; expected lives of 6.00 years, based on expected exercise activity behavior; and volatility of 84% based on the historical volatility of our common stock over a time that is consistent with the expected life of the options.

Included in the stock awards outstanding as of September 30, 2015 were stock appreciation rights (“SARs”) to purchase 98,333 shares of our common stock. The SARs grants were issued solely to our executive officers and these rights will vest over three years from the date of grant.

**Net Sales Recognition.**

Revenue is realized and earned when all of the following criteria are met:

- Persuasive evidence of an arrangement exists;
- Delivery has occurred or services have been rendered;
- The seller’s price to the buyer is fixed or determinable; and
- Collectability is reasonably assured.

For our Laboratory Services business, net sales from Patient Testing laboratories are recognized on an individual test basis and take place when the test report is completed, reviewed and sent to the client, less the reserve for insurance, Medicare and Medicaid contractual adjustments. There are no deferred net sales associated with our Patient Testing services. Adjustments to the allowances, based on actual receipts from third party payors, are reflected in the estimated contractual allowance applied prospectively. In our Biomarker Identification laboratory, we perform pharmacogenomics research services on a project-by project-basis. When we receive payment in advance, we recognize revenue when we deliver the service. These projects typically do not extend beyond one year. At each of September 30, 2015 and December 31, 2014, deferred net sales associated with pharmacogenomics research projects included in the balance sheet in deferred revenue was \$0.1 million.

Net sales of products in our Genetic Assays and Platforms business, reported as discontinued operations (See Note 3 - “Discontinued Operations”), are recognized in accordance with the terms of the sales arrangement. Such recognition is based on receipt of an unconditional customer order and transfer of title and risk of ownership to the customer, typically upon shipment of the product under a purchase order. Our sales terms do not provide for the right of return unless the product is damaged or defective. Net sales from certain services associated with the analytical instruments, to be performed subsequent to shipment of the products, are deferred and recognized when the services are provided. Such services, mainly limited to installation and training services that are not essential to the functionality of the instruments, typically are performed in a timely manner subsequent to shipment of the instrument. We also enter into

various service contracts that cover installed instruments. These contracts cover specific time periods, and net sales associated with these contracts are deferred and recognized ratably over the service period.

**Common Stock Warrants.**

Certain of our issued and outstanding warrants to purchase common stock do not qualify to be treated as equity and, accordingly, are recorded as a liability (“Common Stock Warrant Liability”). The Common Stock Warrant Liability was initially recorded at fair value using a Monte Carlo simulation model. We are required to present these instruments at fair value at each reporting date and any changes in fair values are recorded as an adjustment to earnings. The Common Stock Warrant Liability is

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

considered a Level Three financial instrument for purposes of fair value measurement. See Note 9 - “Fair Value” for additional information.

Translation of Foreign Currency.

Our foreign subsidiary, which is included within discontinued operations uses the British Pound Sterling, which is the local currency of the country in which it is located, as its functional currency. Its assets and liabilities are translated into U.S. Dollars at the exchange rates in effect at the balance sheet date. A cumulative translation loss of fourteen thousand dollars was reported as other comprehensive income on the accompanying unaudited condensed consolidated statement of comprehensive loss for the nine months ended September 30, 2015. A cumulative translation loss of eleven thousand dollars was reported as accumulated other comprehensive income for the nine months ended September 30, 2014.

Loss Per Share.

Basic loss per share is calculated based on the weighted-average number of common shares outstanding during each period. Diluted loss per share includes shares issuable upon exercise of outstanding stock options, warrants or conversion rights that have exercise or conversion prices below the market value of our common stock. Options, warrants and conversion rights pertaining to 10,392,728 and 5,524,030 shares of our common stock have been excluded from the computation of diluted loss per share at September 30, 2015 and 2014, respectively, because the effect is anti-dilutive due to the net loss.

Recent Accounting Pronouncements.

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers. This guidance requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to a customer. ASU No. 2014-09 will replace most existing revenue recognition guidance in generally accepted accounting principles in the U.S. when it becomes effective. In July 2015, the FASB decided to defer the effective date of this new accounting guidance by one year. As a result, ASU No. 2014-09 will be effective for us for all annual and interim reporting periods beginning after December 15, 2017 and early adoption would be permitted as of the original effective date. The new standard permits the use of either the retrospective or cumulative effect transition method. We do not expect to early adopt this guidance and we have not selected a transition method. We are currently evaluating the impact this guidance will have on our financial condition, results of operations and cash flows.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40). The new guidance addresses management’s responsibility to evaluate whether there is substantial doubt about an entity’s ability to continue as a going concern and to provide related footnote disclosures. The standard will be effective for the first interim period within annual reporting periods beginning after December 15, 2016. Early adoption is permitted. We do not expect to early adopt this guidance and do not believe that the adoption of this guidance will have a material impact on our consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-03, Interest-Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs, which requires that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of the related debt liability, rather than as a deferred charge asset. ASU No. 2015-03 is effective for us beginning on January 1, 2016. ASU No. 2015-03 is not expected to have a material impact on our financial condition, results of operations or cash flows.

3. DISCONTINUED OPERATIONS

On September 8, 2015, we entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Edge BioSystems, Inc. (“Buyer”), pursuant to which we agreed to sell to Buyer, and Buyer agreed to purchase from us, our manufacturing, marketing and selling of high quality polymer and silica based beads and resin and chromatography columns business (collectively, the “Columns Business”). The Columns Business was part of our former segment, Genetic Assays and Platforms. Pursuant to the Asset Purchase Agreement, Buyer acquired substantially all of the assets used solely in connection with the Columns Business and assumed certain liabilities of the Columns Business for a total cash purchase price of approximately \$2.1 million (the “Asset Sale”), which was paid on September 8, 2015 upon the closing of the Asset Sale. During the three and nine months ended September 30, 2015, we recorded a gain on the sale of the Columns Business of \$1.5 million.

Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

On September 25, 2015, we entered into a binding term sheet with ADSTEC Corporation (“ADSTEC”), effective as of September 30, 2015, to set forth the terms and conditions by which ADSTEC will purchase from us certain of the assets constituting, and assume certain of the liabilities related to the remainder of our Genetic Assays and Platforms business, including certain of our inventory and our facilities located in Glasgow, Scotland and Irvington Road, Omaha, Nebraska, for a purchase price of approximately \$0.3 million, subject to adjustment in certain circumstances (collectively, the “Transaction”). We anticipate that definitive agreements relating to the Transaction will be entered into during the fourth quarter of 2015. The final terms of the Transaction are subject to the negotiation and finalization of the definitive agreements relating to the Transaction, and the material terms of the Transaction may differ from those set forth in the binding term sheet.

Together, the Asset Sale and the Transaction represent the divestiture of our Genetic Assays and Platforms business resulting in a strategic shift that will have a major effect on our operations and financial results. Therefore, the divested and to be divested operations of our Genetic Assays and Platforms business meet the criteria to be reported as discontinued operations. The related assets, liabilities, results of operations and cash flows are classified as assets held for sale, liabilities held for sale and discontinued operations for all periods presented.

Results of the discontinued operations consisted of the following:

(in thousands)	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Net sales	\$1,877	\$2,308	\$5,720	\$7,792
Cost of goods sold	1,452	1,810	4,623	5,394
Gross profit	425	498	1,097	2,398
Selling, general and administrative expense	493	518	1,453	1,577
Operating (loss) income from discontinued operations	(68	) (20	) (356	) 821
Gain on sale of product line	1,532	4,114	1,532	4,114
Income from discontinued operations before income taxes	1,464	4,094	1,176	4,935
Income tax expense	530	1,430	598	1,675
Income from discontinued operations	\$934	\$2,664	\$578	\$3,260

The \$1.5 million of gain on sale of product line for the three and nine months ended September 30, 2015 is a result of the sale of the Columns Business in September 2015. The \$4.1 million of gain on sale of product line for the three and nine months ended September 30, 2014 is a result of the sale of our Surveyor technology, which was reported within the prior period Genetic Assays and Platforms segment results, in July 2014. We anticipate that we will record a loss on sale once we complete the sale of the remaining assets of the Genetic Assays and Platforms business, which is expected to close during the fourth quarter of 2015.

Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

Assets and liabilities of the discontinued operations are classified as assets held for sale and liabilities held for sale in the condensed consolidated balance sheets and consisted of the following:

	Dollars in Thousands	
	September 30, 2015	December 31, 2014
<b>ASSETS</b>		
Accounts receivable, net	\$1,086	\$2,238
Inventory, net	2,201	3,005
Other current assets	146	141
Total current assets	3,433	5,384
Property and equipment, net	67	124
Other assets	31	91
Total Assets	\$3,531	\$5,599
<b>LIABILITIES</b>		
Accounts payable	\$560	\$973
Accrued compensation	374	447
Accrued expenses	238	255
Deferred revenue	682	737
Total current liabilities	1,854	2,412
Other liabilities	148	142
Total Liabilities	\$2,002	\$2,554

Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

## 4. INTANGIBLES AND OTHER ASSETS

We review our amortizable long-lived assets for impairment annually or whenever events indicate that the carrying amount of the asset (group) may not be recoverable. An impairment loss may be needed if the sum of the future undiscounted cash flows is less than the carrying amount of the asset (group). The amount of the loss would be determined by comparing the fair market value of the asset to the carrying amount of the asset (group).

We performed an interim testing of impairment as of September 30, 2015 due to the significant decline in the market price of our stock. As a result of this testing, we recorded impairment charges related to our long-lived assets of approximately \$7.0 million during the three months ended September 30, 2015. The impairment charges include \$0.9 million related to property and equipment and \$6.1 million related to amortizable intangibles (see table below).

Long-lived intangible assets as of September 30, 2015 and December 31, 2014 consisted of the following:

	Dollars in Thousands			
	September 30, 2015			
	Cost	Accumulated Amortization	Impairment Charge	Net Book Value
Intangibles—technology	\$9,009	\$4,611	\$4,398	\$—
Intangibles—assay royalties	1,434	973	461	—
Intangibles—third party payor relationships	367	116	251	—
Intangibles—tradenames and trademarks	824	439	385	—
Intangibles—customer relationships	652	130	522	—
Intangibles—covenants not to compete	184	184	—	—
Patents	1,083	229	148	706
Intellectual property	466	172	—	294
	\$14,019	\$6,854	\$6,165	\$1,000

	Dollars in Thousands		
	December 31, 2014		
	Cost	Accumulated Amortization	Net Book Value
Intangibles—technology	\$9,009	\$3,995	\$5,014
Intangibles—assay royalties	1,434	819	615
Intangibles—third party payor relationships	367	98	269
Intangibles—tradenames and trademarks	824	351	473
Intangibles—customer relationships	652	98	554
Intangibles—covenants not to compete	184	138	46
Patents	815	87	728
Intellectual property	266	86	180
	\$13,551	\$5,672	\$7,879





Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

	Estimated Useful Life
Technology	7-10 years
Assay royalties	7 years
Third party payor relationships	15 years
Tradenames and trademarks	7 years
Customer relationships	15 years
Covenants not to compete	3 years
Patents	Life of the patent
Intellectual property	7 years

Other assets include U.S. security deposits and deferred tax assets, net of applicable valuation allowances.

Amortization expense for intangible assets was \$0.4 million and \$0.4 million during the three months ended September 30, 2015 and 2014, respectively. Amortization expense for intangible assets was \$1.1 million and \$1.0 million during the nine months ended September 30, 2015 and 2014, respectively. Amortization expense for intangible assets is expected to be \$1.2 million, \$0.1 million, \$0.1 million, \$0.1 million and \$0.1 million for the years ending December 31, 2015, 2016, 2017, 2018 and 2019, respectively.

## 5. DEBT

	Dollars in Thousands	
	September 30, 2015	December 31, 2014
Revolving Line of Credit <sup>(1)</sup>	\$2,275	\$3,000
Term Loan <sup>(2)</sup>	4,000	4,087
Convertible Promissory Notes <sup>(3)</sup>	525	750
Total debt	6,800	7,837
Current portion of long-term debt	(6,275	) (462
Long-term debt, net of current maturities	\$525	\$7,375

Revolving Line of Credit. Amounts advanced under the Revolving Line initially bore interest at an annual rate equal to the greater of (a) 4.25% or (b) the Wall Street Journal prime rate plus 1%. Interest is payable on a monthly basis, with the balance payable at the maturity of the Revolving Line. Under the Amendment to the Loan Agreement, which we entered into on August 2, 2013, amounts advanced under the Revolving Line bear interest at an annual rate equal to the greater of (x) 6.25% or (y) the Wall Street Journal prime rate plus 3%. The current (1) interest rate is 6.25%. Under the Loan Agreement, we paid the Lenders an upfront fee of \$20,000, and will pay the Lenders an additional commitment fee of \$20,000 on each one-year anniversary of March 13, 2013, the Effective Date, during the term of the Revolving Line. In addition, a fee of 0.5% per annum is payable quarterly on the unused portion of the Revolving Line. The Revolving Line matures on September 1, 2016, and therefore, all amounts due under the Revolving Line of Credit are classified as a current liability in the condensed consolidated balance sheet as of September 30, 2015.

(2) Term Loan. We received \$4.0 million under the Term Loan on the Effective Date. Pursuant to the terms of the Loan Agreement, as amended by the Sixth Amendment (as defined in “-Revolving Line and Term Loan” below), we made a principal payment of approximately \$148,000 on April 1, 2015 and will not be obligated to make monthly payments of principal to the Lenders until April 1, 2016. The current interest rate is 9.1%. The Term Loan matures on September 1, 2016, and therefore, all amounts due under the Term Loan are classified as a current liability in

the condensed consolidated balance sheet as of September 30, 2015.

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

We paid the Lenders an upfront fee of \$40,000 for the Term Loan, and will pay the Lenders an additional final payment of \$120,000 at maturity or prepayment of the Term Loan. In addition, if we repay the Term Loan prior to maturity, we will pay the Lenders a prepayment penalty of 1% of the total outstanding balance under the Term Loan.

**Additional Terms**

The Loan Agreement contains affirmative and negative covenants. Under the Term Loan, we are required to maintain a minimum liquidity ratio and achieve a minimum amount of revenue, and we also agreed not to (a) pledge or otherwise encumber our assets other than to the Lenders, (b) enter into additional borrowings or guarantees, (c) repurchase our capital stock, or (d) enter into certain mergers or acquisitions without the Lenders' consent. Additionally, the Loan Agreement contains a subjective acceleration clause at the discretion of the Lenders.

To secure the repayment of any amounts borrowed under the Revolving Line and the Term Loan, we granted the Lenders a security interest in all of our assets. The occurrence of an event of default under the Loan Agreement could result in the acceleration of our obligations under the Loan Agreement, would increase the applicable interest rate under the Revolving Line or Term Loan (or both) by 5% and would permit the Lenders to exercise remedies with respect to the collateral under the Loan Agreement.

(3) Convertible Promissory Notes. The Notes accrue interest at a rate of 6% per year and mature on December 31, 2016.

**Revolving Line and Term Loan.**

On March 13, 2013 (the "Effective Date"), we entered into a Loan and Security Agreement with affiliates of Third Security, LLC (the "Lenders") for (a) a revolving line of credit (the "Revolving Line") with borrowing availability of up to \$4.0 million, subject to reduction based on our eligible accounts receivable, and (b) a term loan (the "Term Loan" and, together with the Revolving Line, the "Loan Agreement") of \$4.0 million. Proceeds were used to pay off a three year senior secured promissory note payable to PGxHealth, LLC, which was entered into on December 29, 2010 in conjunction with our acquisition of the FAMILION family of genetic tests, and for general corporate and working capital purposes.

On August 2, 2013, we entered into an amendment to the Loan Agreement (the "Amendment"). The Amendment, which became effective as of June 30, 2013, reduced our future minimum revenue covenants under the Loan Agreement and modified the interest rates applicable to the amounts advanced under the Revolving Line.

On November 14, 2013, we entered into a second amendment to the Loan Agreement (the "Second Amendment"). The Second Amendment, which became effective as of October 31, 2013, reduced our future minimum revenue covenants under the Loan Agreement.

On January 27, 2014, we entered into a third amendment to the Loan Agreement (the "Third Amendment"). Pursuant to the Third Amendment, the Lenders agreed to waive certain events of default under the Loan Agreement, and the parties amended certain provisions of the Loan Agreement, including the minimum liquidity ratio that we must maintain during the term of the Loan Agreement.

On March 3, 2014, we entered into a fourth amendment to the Loan Agreement (the "Fourth Amendment"). Pursuant to the terms of the Fourth Amendment, we were not required to make any principal or interest payments under the Term Loan for the period from March 1, 2014 through March 31, 2015. The interest on the debt that was deferred and not

paid was capitalized as part of the Term Loan. The amount of interest that was capitalized from March 1, 2014 to March 31, 2015 was \$0.4 million.

On October 22, 2014, we entered into a fifth amendment to the Loan Agreement (the “Fifth Amendment”). Pursuant to the Fifth Amendment, the parties amended certain provisions of the Loan Agreement, including reducing the minimum liquidity and revenue covenants under the Loan Agreement. The Fifth Amendment also reduced the aggregate amount that we may borrow under the Revolving Line from \$4.0 million to \$3.0 million.

On April 1, 2015, we entered into a sixth amendment to the Loan Agreement (the “Sixth Amendment”). Pursuant to the Sixth Amendment, among other things, (a) the Lenders waived specified events of default under the terms of the Loan Agreement, (b) commencing April 1, 2015, we began making monthly interest payments with respect to the Term Loan to the Lenders, (c) we will not be obligated to make monthly payments of principal under the Term Loan to the Lenders until April 1, 2016, (d) we made an initial prepayment of a portion of the Term Loan balance in the amount of approximately \$148,000 on April 1, 2015 and will make

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

one or more additional prepayments to the Lenders under the Loan Agreement upon the occurrence of certain events, as defined in the Loan Agreement, and (e) we are not required to comply with the minimum liquidity ratio under the terms of the Loan Agreement until the earliest to occur of a specified event, as defined in the Loan Agreement, or March 31, 2016. The Sixth Amendment also extends the time period in which we must provide certain reports and statements to the Lenders and amends the circumstances pursuant to which we may engage in certain sales or transfers of our business or property without the consent of the Lenders.

As of June 30, 2015, we were in compliance with all financial covenants of the Loan Agreement, but were not in compliance with the restrictions limiting the amount that we may borrow under the Revolving Line. Accordingly, on August 10, 2015, we received a waiver from the Lenders relating to this non-compliance and paid the Lenders an aggregate of \$0.7 million, which brought us back into compliance with the terms of the Revolving Line.

On September 4, 2015, we entered into a seventh amendment to the Loan Agreement (the “Seventh Amendment”). The Seventh Amendment, among other things, (a) provided that the Lenders will waive specified events of default under the terms of the Loan Agreement, (b) reduced our future minimum revenue covenants under the Loan Agreement, (c) reduced our borrowing availability under the Revolving Line to approximately \$2.3 million, and (d) limited our borrowing base under the Loan Agreement to the amount of the Revolving Line.

As of September 30, 2015, we were in compliance with all financial covenants of the Loan Agreement.

Convertible Promissory Notes.

On December 31, 2014, we entered into an Unsecured Convertible Promissory Note Purchase Agreement (the “Note Purchase Agreement”) with an accredited investor (the “Investor”), pursuant to which we agreed to issue and sell to the Investor in a private placement an unsecured convertible promissory note (the “Initial Note”). We issued the Initial Note in the aggregate principal amount of \$750,000 to the Investor on December 31, 2014. Pursuant to the terms of the Initial Note, interest accrued at a rate of 6% per year and the Initial Note was set to mature on December 31, 2016. Under the Initial Note, the outstanding principal and unpaid interest accrued was convertible into shares of our common stock as follows: (i) commencing upon the date of issuance of the Initial Note (but no earlier than January 1, 2015), the Investor was entitled to convert, on a one-time basis, up to 50% of the outstanding principal and unpaid interest accrued under the Initial Note, into shares of our common stock at a conversion price equal to the lesser of (a) the average closing price of the common stock on the principal securities exchange or securities market on which our common stock is then traded (the “Market”) for the 20 consecutive trading days immediately preceding the date of conversion, and (b) \$2.20 (subject to adjustment for stock splits, stock dividends, other distributions, recapitalizations and the like); and (ii) commencing February 15, 2015, the Investor was entitled to convert, on a one-time basis, any or all of the remaining outstanding principal and unpaid interest accrued under the Initial Note, into shares of our common stock at a conversion price equal to 85% of the average closing price of our common stock on the Market for the 15 consecutive trading days immediately preceding the date of conversion. The Initial Note has been converted in full into 502,786 shares of our common stock, in accordance with the terms of the Initial Note.

On January 15, 2015, we entered into the Note Purchase Agreement with seven accredited investors (the “Additional Investors”) and, on January 20, 2015, issued and sold to the Additional Investors, in a private placement, notes (the “Additional Notes”) in an aggregate principal amount of \$925,000. The Additional Notes have the same terms and conditions as the Initial Note. As of September 30, 2015, \$400,000 of the aggregate principal amount of the Additional Notes, and accrued interest thereon, has been converted into an aggregate of 281,023 shares of our common stock.

#### 6. COMMITMENTS AND CONTINGENCIES

From time to time we are subject to claims of various amounts, which arise out of the normal course of business. In the opinion of management, the disposition of pending claims will not have a material adverse effect on our financial position, results of operations or cash flows.

We lease certain equipment, vehicles and operating facilities under non-cancellable operating leases that expire on various dates through 2022. The future minimum lease payments required under these leases are \$0.2 million for the remainder of 2015, \$0.8 million in 2016, \$0.8 million in 2017, \$0.5 million in 2018, \$0.2 million in 2019 and \$0.6 million thereafter. Rent expense for the nine months ended September 30, 2015 and 2014 was \$0.4 million and \$0.5 million, respectively. At September 30, 2015, firm commitments to vendors totaled \$0.5 million.

Table of Contents

7. INCOME TAXES

Annually we file U.S. Federal, state and foreign income tax returns. All U.S. Federal and most state loss carryforwards remain subject to adjustment in the event of an income tax examination.

The income tax benefit for both the three and nine months ended September 30, 2015 was \$0.5 million. The income tax benefit for the three and nine months ended September 30, 2014 was \$1.5 million and \$1.2 million, respectively. We maintain a full valuation allowance on our net deferred tax assets, having concluded we are not more likely than not going to realize the benefit of our deferred tax assets.

An income tax benefit results from intraperiod tax accounting that requires recording tax expense on income in discontinued operations offset by a tax benefit in continuing operations. That benefit is partially reduced by an increase in our valuation allowance on deferred tax assets.

Our effective tax rate for the three and nine months ended September 30, 2015 was 5.57% and 3.18%, respectively, which is primarily the result of valuation allowances against the net operating losses for the U.S. and results in us not recording net deferred tax assets in the U.S.

Our goodwill is an indefinite-lived asset that is not amortized for financial reporting purposes. However, goodwill is tax deductible and therefore amortized for tax purposes, which results in increased deferred tax assets and deferred tax liabilities. Since we maintain a full valuation allowance on net deferred tax assets, and indefinite lived assets are not used in such net calculation, we record income tax expense associated with the tax amortization of goodwill. During both the three and nine months ended September 30, 2015, the amount of income tax expense related to the tax amortization of goodwill was \$0.1 million.

During each of the three and nine months ended September 30, 2015 and 2014, there were no material changes to the liability for uncertain tax positions.

8. STOCKHOLDERS' EQUITY

Common Stock.

Pursuant to our Third Amended and Restated Certificate of Incorporation, as amended, we currently have 150,000,000 shares of common stock authorized for issuance.

On February 2, 2012, we entered into definitive agreements with institutional and other accredited investors and raised approximately \$22.0 million in a private placement financing (the "Private Placement"), which included an aggregate of \$3.0 million in convertible notes issued in December 2011 to entities affiliated with Third Security, LLC, a related party, that automatically converted into shares of our common stock and warrants to purchase such common stock on the same terms as all investors in the Private Placement. Pursuant to the purchase agreement, we issued an aggregate of 1,583,333 shares of our common stock at a price per share of \$12.00, as well as five-year warrants to purchase up to an aggregate of 823,333 shares of our common stock with an exercise price of \$15.00 per share. In connection with the conversion of the convertible notes issued by us to the entities affiliated with Third Security, LLC, the entities received an aggregate of 250,000 shares of our common stock and 125,000 warrants on the same terms as all investors in the Private Placement. Craig-Hallum Capital Group LLC served as the sole placement agent for the offering. In consideration for services rendered as the placement agent in the offering, we agreed to (a) pay to the placement agent cash commissions equal to \$1,330,000, or 7.0% of the gross proceeds received in the offering; (b) issue to the placement agent a five-year warrant to purchase up to 31,666 shares of our common stock (representing 2% of the shares sold in the Private Placement) with an exercise price of \$15.00 per share and other terms that are the same as the terms of the warrants issued in the Private Placement; and (c) reimburse the placement agent for reasonable out-of-pocket expenses, including fees paid to the placement agent's legal counsel, incurred in connection with the offering, which reimbursable expenses were not to exceed \$125,000. The costs incurred to complete the Private Placement were recorded as a reduction in equity in the amount of \$1.5 million. Net proceeds from this offering were used for general corporate and working capital purposes, primarily to accelerate development of several of our key initiatives.



Edgar Filing: TRANSGENOMIC INC - Form 10-Q

On January 24, 2013, we entered into a Securities Purchase Agreement with certain institutional and other accredited investors pursuant to which we: (a) sold to the investors an aggregate of 1,383,333 shares of our common stock at a price per share of \$6.00 for aggregate gross proceeds of approximately \$8.3 million; and (b) issued to the investors warrants to purchase up to an aggregate of 691,655 shares of our common stock with an exercise price of \$9.00 per share (the "Offering"). The warrants may be exercised, in whole or in part, at any time from January 30, 2013 until January 30, 2018 and contain both cash and "cashless

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

exercise” features. Affiliates of Third Security, LLC purchased an aggregate of 500,000 shares of common stock and warrants to purchase an aggregate of 250,000 shares of common stock in the Offering on the same terms as the other investors. Net proceeds from the Offering were used for general corporate and working capital purposes, primarily to accelerate development of several of our key initiatives.

In connection with the Offering, we entered into a registration rights agreement with the investors (the “Registration Rights Agreement”). The Registration Rights Agreement required that we file with the Securities and Exchange Commission a registration statement to register for resale the shares of common stock sold and the shares of common stock issuable upon exercise of the warrants (the “Warrant Shares”) by March 16, 2013. The registration statement was filed with the Securities and Exchange Commission on March 15, 2013 and was declared effective by the Securities and Exchange Commission on March 29, 2013.

The Offering required the repricing and issuance of additional common stock warrants to the holders of warrants issued in the Private Placement. The exercise price of the warrants decreased from \$15.00 per share to \$12.96 per share and the number of shares issuable upon exercise of the warrants increased from 948,333 to 1,097,600.

On October 22, 2014, we entered into a Securities Purchase Agreement with certain accredited investors (the “October 2014 Investors”), pursuant to which we, in a private placement, issued and sold to the October 2014 Investors (the “2014 Private Placement”) an aggregate of 730,776 shares of our common stock at a price per share of \$3.25 for an aggregate purchase price of approximately \$2.4 million, and warrants to purchase up to an aggregate of 365,388 shares of our common stock with an initial exercise price of \$4.00 per share that are exercisable for the period from April 22, 2015 through April 22, 2020. In connection with the 2014 Private Placement, we also issued a warrant to purchase up to an aggregate of 9,230 shares of our common stock to one advisor. The warrants issued in the 2014 Private Placement include both cash and “cashless exercise” features.

The 2014 Private Placement required the repricing and issuance of additional common stock warrants to the holders of warrants issued in the February 2012 common stock and warrant sale. The exercise price of the warrants decreased from \$11.73 per share to \$10.86 per share and the number of shares issuable upon exercise of the warrants increased from 1,212,665 to 1,309,785.

On December 31, 2014, we entered into the Note Purchase Agreement with the Investor pursuant to which we agreed to issue and sell the Initial Note to the Investor (the “Note Private Placement”). See Note 5 - “Debt-Convertible Promissory Notes” for additional information regarding the terms of the Initial Note. Pursuant to the terms of the Note Purchase Agreement, we are subject to certain registration obligations and we may be required to effect one or more other registrations to register for resale the shares of our common stock issued or issuable under the Initial Note in connection with certain “piggy-back” registration rights granted to the Investor.

The Note Private Placement required the repricing and issuance of additional common stock warrants to the holders of warrants issued in the February 2012 common stock and warrant sale. The exercise price of the 2012 warrants decreased from \$10.86 per share to \$10.25 per share and the number of shares issuable upon exercise of the warrants increased from 1,309,785 to 1,387,685.

On January 15, 2015, we entered into the Note Purchase Agreement with the Additional Investors and, on January 20, 2015, issued and sold to the Additional Investors, in a private placement, the Additional Notes in an aggregate principal amount of \$925,000 (the “Additional Note Private Placement”). The Additional Notes have the same terms and conditions as the Initial Note.

The Additional Note Private Placement required the repricing and issuance of additional common stock warrants to the investors in our February 2012 common stock and warrant financing. The exercise price of these warrants decreased from \$10.25 per share to \$9.59 per share and the number of shares issuable upon exercise of the warrants

increased from 1,387,685 to 1,483,161.

On February 27, 2015, we entered into a purchase agreement with Craig-Hallum Capital Group LLC (the “Underwriter”) relating to our sale and issuance of 3,573,899 shares of our common stock and corresponding warrants to purchase up to 714,780 shares of our common stock (the “2015 Offering”). Each share of common stock was sold in combination with a warrant to purchase 0.20 of a share of common stock. The purchase price to the public for each share of common stock and accompanying warrant was \$1.95.

The purchase price paid by the Underwriter to us for the common stock and accompanying warrants was \$1.8135. The net proceeds from the 2015 Offering, after deducting the Underwriter’s discount and other estimated 2015 Offering expenses, were approximately \$6.2 million.

The accompanying warrants are exercisable immediately upon their initial issuance date at an exercise price of \$2.24 per share and will expire five years from the date of issuance. The exercise price will also be subject to adjustment in the event of

20

---

Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

certain stock dividends and distributions, stock splits, stock combinations, reclassifications or similar events affecting our common stock.

The 2015 Offering required the repricing and issuance of additional common stock warrants to the investors in our February 2012 common stock and warrant financing. The exercise price of these warrants decreased from \$9.59 per share to \$7.56 per share and the number of shares issuable upon exercise of the warrants increased from 1,483,161 to 1,881,396.

On June 30, 2015, we entered into a Securities Purchase Agreement with certain accredited investors (the “July 2015 Investors”) pursuant to which, on July 7, 2015, we sold to the July 2015 Investors, and the July 2015 Investors purchased from us, (a) an aggregate of approximately 1.5 million shares of our common stock at a price per share of \$1.42, (b) warrants (the “Series B Warrants”) to purchase up to an aggregate of 0.7 million shares of our common stock with an exercise price of \$0.01 per share, and (c) warrants (the “Series A Warrants” and, together with the Series B Warrants, the “July 2015 Warrants”) to purchase up to an aggregate of 1.2 million shares of our common stock, with an exercise price of \$1.66 per share (collectively, the “July 2015 Offering”). The purchase price for the Series B Warrants was \$1.42 per share of our common stock subject to the Series B Warrants. Each of the July 2015 Warrants has a term of 5 and 1/2 years. The Series B Warrants are immediately exercisable. The Series A Warrants will be exercisable beginning on January 7, 2016, six months from the date of issuance. The aggregate gross proceeds to us from the July 2015 Offering were approximately \$3.0 million.

Craig-Hallum Capital Group LLC (the “2015 Placement Agent”) served as the sole placement agent for the Offering. In consideration for services rendered as the placement agent in the July 2015 Offering, we (a) paid to the 2015 Placement Agent cash commissions equal to approximately \$212,783, or 7.0% of the gross proceeds received in the July 2015 Offering; (b) issued to the 2015 Placement Agent a five-year warrant to purchase up to 107,033 shares of our common stock with an exercise price of \$1.66 per share and which is subject to other terms that are the same as the terms of the Series A Warrants; and (c) reimbursed the 2015 Placement Agent for reasonable out-of-pocket expenses, including fees paid to the 2015 Placement Agent’s legal counsel, incurred in connection with the July 2015 Offering, which reimbursable expenses did not exceed \$50,000.

The July 2015 Offering required the repricing and issuance of additional common stock warrants to the investors in our February 2012 common stock and warrant financing. The exercise price of these warrants decreased from \$7.56 per share to \$6.50 per share and the number of shares issuable upon exercise of the warrants increased from 1,881,396 to 2,188,177.

**Common Stock Warrants.**

During the nine months ended September 30, 2015 and 2014, we issued warrants to purchase 3,466,841 and 115,432 shares of common stock, respectively. None of the issued warrants were exercised during such periods. The warrants issued in the nine months ended September 30, 2015 included 800,492 warrants issued due to repricing requirements of the Private Placement and 2,666,349 warrants issued in connection with the 2015 Offering and the July 2015 Offering. The warrants issued in the nine months ended September 30, 2014 were all issued due to repricing requirements of the Private Placement. Warrants to purchase an aggregate of 6,351,826 shares of common stock were outstanding at September 30, 2015.

Warrant Holder	Issue Year	Expiration	Underlying Shares	Exercise Price
Affiliates of Third Security, LLC <sup>(1)</sup>	2010	December 2015	431,027	\$6.96
Various Institutional Holders <sup>(2)</sup>	2012	February 2017	1,899,729	\$6.50
Affiliates of Third Security, LLC <sup>(2)</sup>	2012	February 2017	288,448	\$6.50
Various Institutional Holders <sup>(3)</sup>	2013	January 2018	441,655	\$9.00
Affiliates of Third Security, LLC <sup>(3)</sup>	2013	January 2018	250,000	\$9.00

Edgar Filing: TRANSGENOMIC INC - Form 10-Q

Various Institutional Holders <sup>(4)</sup>	2014	April 2020	374,618	\$4.00
Various Institutional Holders <sup>(5)</sup>	2015	February 2020	714,780	\$2.24
Various Institutional Holders <sup>(6)</sup>	2015	December 2020	1,284,405	\$1.66
Various Institutional Holders <sup>(6)</sup>	2015	December 2020	667,164	\$0.01
			6,351,826	

(1) This warrant was issued in connection with the issuance of warrants to purchase shares of our Series A Preferred Stock to affiliates of Third Security, LLC in December 2010. The number of underlying shares shown reflects the number of shares of common stock issuable upon conversion of the shares of Series A Preferred Stock for which this warrant is currently exercisable.

Table of Contents

TRANSGENOMIC, INC. AND SUBSIDIARY

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

- These warrants were issued in connection with the Private Placement completed in February 2012 and are classified as a liability in our financial statements. See Note 9 - “Fair Value” for additional information. These
- (2) warrants also contain certain anti-dilution provisions that provide for an adjustment to the exercise price and number of shares issuable upon exercise of the warrant in the event that we engage in certain issuances of shares of our common stock at a price lower than the exercise price of the warrant.
  - (3) These warrants were issued in connection with the Offering, which was completed in January 2013.
  - (4) These warrants were issued in connection with the 2014 Private Placement, which was completed in October 2014.
  - (5) These warrants were issued in connection with the 2015 Offering, which was completed in February 2015.
  - (6) These warrants were issued in connection with the July 2015 Offering, which was completed in July 2015.
- Issuance of Series B Preferred Stock

On March 5, 2014, we entered into a Series B Convertible Preferred Stock Purchase Agreement (the “Series B Purchase Agreement”) with affiliates of Third Security, LLC (the “2014 Third Security Investors”), pursuant to which we, in a private placement, sold and issued an aggregate of 1,443,297 shares of our Series B Preferred Stock, par value \$0.01 per share (the “Series B Preferred Stock”), at a price per share of \$4.85 for an aggregate purchase price of approximately \$7.0 million. Each share of Series B Preferred Stock issued pursuant to the Series B Purchase Agreement is initially convertible into shares of our common stock at a rate of 1-for-1, which conversion rate is subject to further adjustment as set forth in the Certificate of Designation of Series B Convertible Preferred Stock.

In connection with the Series B financing, we also entered into a Registration Rights Agreement, dated March 5, 2014, with the 2014 Third Security Investors, pursuant to which we granted certain demand, “piggy-back” and S-3 registrations rights covering the resale of the shares of common stock underlying the Series B Preferred Stock issued pursuant to the Series B Purchase Agreement and all shares of common stock issuable upon any dividend or other distribution with respect thereto.

The Series B financing required the repricing and issuance of additional common stock warrants to the holders of warrants issued in the Private Placement. The exercise price of the warrants decreased from \$12.96 per share to \$11.73 per share and the number of shares issuable upon exercise of the warrants increased from 1,097,600 to 1,212,665.

#### Preferred Stock Dividends

We have cumulative undeclared dividends on our Series A Convertible Preferred Stock and Series B Preferred Stock (collectively “Preferred Stock”). At December 31, 2014, we had a recorded liability of \$3.1 million for these undeclared dividends. Since dividends should generally not be recognized as a liability until declared, the \$3.1 million liability was reversed in 2015 with an offset to accumulated deficit.

For the three and nine months ended September 30, 2015 and 2014, we had undeclared dividends. In accordance with the FASB’s Accounting Standards Codification Topic 260-10-45-11, “Earnings per Share”, these dividends were added to the net loss per share calculation.

At September 30, 2015 and December 31, 2014, we had cumulative undeclared dividends on our Preferred Stock of \$4.1 million and \$3.1 million, respectively.

## 9. FAIR VALUE

FASB guidance on fair value measurements, which defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements for our financial assets and liabilities, as well as for other assets and liabilities that are carried at fair value on a recurring basis in our consolidated financial statements.

FASB guidance establishes a three-level fair value hierarchy based upon the assumptions (inputs) used to price assets or liabilities. The three levels of inputs used to measure fair value are as follows:

Level 1—Unadjusted quoted prices in active markets for identical assets or liabilities;

Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

Level 2—Observable inputs other than those included in Level 1, such as quoted prices for similar assets and liabilities in active markets or quoted prices for identical assets or liabilities in inactive markets; and

Level 3—Unobservable inputs reflecting our own assumptions and best estimate of what inputs market participants would use in pricing the asset or liability.

**Debt.**

Our long term debt is considered a Level 3 liability for which book value approximates fair market value due to the variable interest rate it bears.

**Common Stock Warrant Liability.**

Certain of our issued and outstanding warrants to purchase shares of common stock do not qualify to be treated as equity and, accordingly, are recorded as a liability. The Common Stock Warrant Liability represents the fair value of the 1.2 million warrants issued in February 2012, which, through a series of changes in exercise price since February 2012, are now exercisable into 2.2 million shares of common stock. We are required to record these instruments at fair value at each reporting date and changes are recorded as a non-cash adjustment to earnings. The gains or losses included in earnings are reported in other income (expense) in our Statement of Operations. Management does not believe that this liability will be settled by a use of cash.

The Common Stock Warrant Liability is considered a Level 3 financial instrument and is valued using a Monte Carlo simulation model. This method is well suited to valuing options with non-standard features, such as anti-dilution protection. A Monte Carlo simulation model uses repeated random sampling to simulate significant uncertainty in inputs. Assumptions and inputs used in the valuation of the common stock warrants are broken down into four sections: Static Business Inputs; Static Technical Inputs; Simulated Business Inputs; and Simulated Technical Inputs. Static Business Inputs include: our equity value, which was estimated using our stock price of \$0.92 as of September 30, 2015; the amount of the down-round financing; the timing of the down-round financing; the expected exercise period of 1.36 years from the valuation date; and the fact that no other potential fundamental transactions are expected during the term of the common stock warrants.

Static Technical Inputs include: volatility of 104% and the risk-free interest rate of 0.45% based on the 1.5-year U.S. Treasury yield interpolated from the one-year and two-year U.S. Treasury bonds.

Simulated Business Inputs include: the probability of down-round financing, which was estimated to be 25% for simulated equity values below the down-round financing cut-off point.

Simulated Technical Inputs include: our equity value follows a geometric Brownian motion and is simulated over weekly periods; and a down-round financing event that was randomly simulated in an iteration based on the 25% discrete probability of a down-round financing for those iterations where our simulated equity value at the expected timing of a down-round financing event was below the down-round financing cut-off point.

During the three months ended September 30, 2015 and 2014, the changes in the fair value of the liability measured using significant unobservable inputs (Level 3) was comprised of the following:

	Dollars in Thousands	
	For the Three Months Ended	
	September 30,	September 30,
	2015	2014
Beginning balance at July 1	\$560	\$350
Total (gains) or losses:		
Recognized in earnings	(385	) 50
Balance at September 30	\$175	\$400



During the nine months ended September 30, 2015 and 2014, the changes in the fair value of the liability measured using significant unobservable inputs (Level 3) was comprised of the following:

23

---

Table of Contents

## TRANSGENOMIC, INC. AND SUBSIDIARY

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Three and Nine Months Ended September 30, 2015 and 2014

	Dollars in Thousands	
	For the Nine Months Ended	
	September 30,	September 30,
	2015	2014
Beginning balance at January 1	\$ 145	\$ 600
Total (gains) or losses:		
Recognized in earnings	30	(200 )
Balance at September 30	\$ 175	\$ 400

The change in unrealized gains or losses of Level 3 liabilities was included in earnings and was reported in other income (expense) in our Statement of Operations.

## 10. STOCK OPTIONS

## Stock Options.

The following table summarizes stock option activity during the nine months ended September 30, 2015:

	Number of Options	Weighted-Average Exercise Price
Outstanding at January 1, 2015	685,984	\$ 6.56
Granted	641,560	1.51
Forfeited	(39,469 )	4.88
Expired	(88,361 )	10.60
Outstanding at September 30, 2015	1,199,714	\$ 3.62
Exercisable at September 30, 2015	325,111	\$ 6.68

During the nine months ended September 30, 2015, we granted options to purchase 641,560 shares of our common stock at a weighted-average exercise price of \$1.51 per share under our 2006 Equity Incentive Plan, as amended (the “Plan”). Options to purchase an aggregate of 237,546 shares of our common stock were granted during the nine months ended September 30, 2014.

As of September 30, 2015, there were 325,111 options exercisable and 981,938 options were vested or expected to vest with an aggregate intrinsic value of zero.

## Stock Appreciation Rights (“SARs”)

The following table summarizes SARs activity under the Plan during the nine months ended September 30, 2015:

	Number of SARs	Weighted-Average Exercise Price
Outstanding at January 1, 2015	98,333	\$ 4.14
Outstanding at September 30, 2015	98,333	\$ 4.14
Exercisable at September 30, 2015	55,833	\$ 4.32

All outstanding SARs were issued solely to our executive officers.

As of September 30, 2015, 55,833 shares subject to outstanding SARs were exercisable and 98,333 shares were vested or expected to vest. The weighted-average exercise price of these SARs was \$4.14 per share and the aggregate intrinsic value was zero.

#### 11. SUBSEQUENT EVENTS

Events or transactions that occur after the balance sheet date, but before the financial statements are complete, are reviewed to determine if they should be recognized. We have no material subsequent events to disclose.

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Information

This Quarterly Report on Form 10-Q, including this Management's Discussion and Analysis, contains forward-looking statements. These statements are based on management's current views, assumptions or beliefs of future events and financial performance and are subject to uncertainty and changes in circumstances. Readers of this report should understand that these statements are not guarantees of performance or results. Many factors could affect our actual financial results and cause them to vary materially from the expectations contained in the forward-looking statements. These factors include, among other things: our expected revenue, income (loss), receivables, operating expenses, supplier pricing, availability and prices of raw materials, Medicare/Medicaid/insurance reimbursements, product pricing, foreign currency exchange rates, sources of funding operations and acquisitions, our ability to raise funds, sufficiency of available liquidity, future interest costs, future economic circumstances, industry conditions, our ability to execute our operating plans, the success of our cost savings initiatives, the competitive environment and related market conditions, actions of governments and regulatory factors affecting our business, retaining key employees and other risks as described in our reports filed with the Securities and Exchange Commission. In some cases these statements are identifiable through the use of words such as "anticipate," "believe," "estimate," "expect," "intend," "plan," "project," "target," "can," "could," "may," "should," "will," "would" or the negative versions of these terms and other similar expressions. You are cautioned not to place undue reliance on these forward-looking statements. The forward-looking statements we make are not guarantees of future performance and are subject to various assumptions, risks and other factors that could cause actual results to differ materially from those suggested by these forward-looking statements. Actual results may differ materially from those suggested by the forward-looking statements that we make for a number of reasons, including those described in Part I, Item 1A, "Risk Factors," of our Annual Report on Form 10-K for the fiscal year ended December 31, 2014, which we filed with the Securities and Exchange Commission on April 15, 2015. We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law.

The following discussion should be read together with our financial statements and related notes contained in this Quarterly Report on Form 10-Q and with the financial statements, related notes and Management's Discussion and Analysis included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014, which we filed with the Securities and Exchange Commission on April 15, 2015. Results for the three and nine months ended September 30, 2015 are not necessarily indicative of results that may be attained in the future.

Overview

Transgenomic, Inc. ("we", "us", "our", the "Company" or "Transgenomic") is a global biotechnology company advancing personalized medicine in cardiology, oncology and inherited diseases through advanced diagnostic technologies, such as our revolutionary multiplexed ICE COLD-PCR™, or MX-ICP, technology and our unique genetic tests provided through our Laboratory Services business. We also provide specialized clinical and research services to biopharmaceutical companies developing targeted therapies.

Our diagnostic technologies are designed to improve medical diagnoses and patient outcomes. Our strategy seeks to optimize, through channel partnerships, the commercial potential of our assets aimed at large genetic testing markets. This allows us to focus resources on our areas of strength, including developing and marketing tests for rare genetic disorders and other genetic-mediated conditions in the U.S., where we are a market leader, and developing biomarkers, genetic tests and companion diagnostics using proprietary technology that is unsurpassed for the identification and detection of low-level genetic mutations and is a prerequisite for improved diagnosis and treatment of cancer and other diseases.

MX-ICP is a simple, proprietary technology that amplifies the ability to detect genetic mutations by 100 - 400 fold. This technology has been validated internally on all currently available sequencing platforms, including Sanger, Next

Gen Sequencing and Digital PCR. By enhancing the level of detection of genetic mutations and suppressing the normal, “wild-type” DNA, several benefits are provided. It is generally understood that most current technologies are unable to consistently identify mutations that occur in less than approximately 5% of a sample. However, many mutations found at much lower levels, even down to 0.01%, are known to be clinically relevant and can have significant consequences to a patient: both in terms of how they will respond to a given drug or treatment and how a given tumor is likely to change over time. More importantly, in our view, significantly improving the level of detection while using blood, saliva and even urine as a source for DNA, rather than depending on painful, expensive and potentially dangerous tumor biopsies, is an important advancement in patient care with respect to cancer detection, treatment and monitoring and can result in significant cost savings for the healthcare system by replacing invasive procedures

## Table of Contents

with the simple collection of blood or other bodily fluids. By broadening the types of samples that can be used for testing and allowing all sequencing platforms to provide improved identification of low level mutations, MX-ICP has the potential to make testing more patient friendly, enable genetic monitoring of disease progression, effectively guide treatment protocols, and reduce the overall cost of diagnosis and monitoring while improving patient outcomes.

Historically, our operations were organized and reviewed by management along our major product lines and presented in two business segments: Laboratory Services and Genetic Assays and Platforms. Beginning with the quarter ended September 30, 2015, our operations are now organized as one business segment, our Laboratory Services segment. Our laboratories specialize in genetic testing for cardiology, neurology and mitochondrial disorders, and for oncology. Our Patient Testing laboratories located in New Haven, Connecticut and Omaha, Nebraska are certified under the Clinical Laboratory Improvement Amendment (“CLIA”) as high complexity laboratories and our Omaha facility is accredited by the College of American Pathologists. Our Biomarker Identification laboratory located in Omaha provides pharmacogenomics research services supporting Phase II and Phase III clinical trials conducted by pharmaceutical and biotechnology companies. Our laboratories employ a variety of genomic testing service technologies, including our new, high performance MX-ICP technology. ICE COLD-PCR is a proprietary ultra-high sensitivity platform technology with breakthrough potential to enable wide adoption of personalized, precision medicine in cancer and other diseases. It can be run in any laboratory that contains standard PCR systems. MX-ICP enables detection of multiple known and unknown mutations from virtually any sample type, including tissue biopsies, blood, urine, saliva, cell-free DNA (“cfDNA”) and circulating tumor cells (“CTCs”) at levels greater than 1,000-fold higher than standard DNA sequencing techniques. It is easy to implement and use within existing workflows.

Our condensed consolidated balance sheets, statements of operations and statements of cash flows for all periods presented reflect our former Genetic Assays and Platforms activities as discontinued operations (See Note 3 - “Discontinued Operations” in the Notes to Unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report on Form 10-Q).

### Third Quarter 2015 Overview and Recent Highlights

On July 1, 2015, we announced the availability of our ICEme™ Mutation Enrichment Kits to cancer researchers worldwide. The kits, which were launched on June 30, 2015, are based on our Multiplexed ICE-COLD PCR™ (“MX-ICP”) technology and they are customizable to meet researchers’ specific needs. The initial menu includes 17 clinically actionable mutations/exons for use as single mutation tests or in combination. MX-ICP is validated and available for use on all sequencing platforms.

On August 5, 2015, we announced the launch of a new pilot clinical study of our MX-ICP liquid biopsy technology. Four leading biopharmaceutical firms have joined the pilot program, which was initiated with an undisclosed market-leading oncology company earlier this year. The primary aim of the pilot study is to validate the accuracy and utility of using MX-ICP-based liquid biopsies to guide and monitor cancer clinical trials. The study will include a variety of cancers and several different sequencing platforms.

On August 10, 2015, we announced the establishment of a Clinical-Commercial Advisory Board (CCAB) for oncology applications of our MX-ICP technology. The CCAB is headed by Dr. Scott Patterson, a recognized expert in the application of genetic biomarkers to cancer drug development. Also joining as inaugural CCAB members are Dr. Bruce E. Johnson, Chief Clinical Research Officer at the Dana-Farber Cancer Institute, and molecular pathologist Professor Paul Waring of the University of Melbourne, who is a pioneer in the application of genomic technology to cancer diagnostics and drug development. Additional CCAB members are expected to be announced in the coming months.

On August 19, 2015, we announced the launch of our MX-ICP EGFR Analysis lung cancer panel that covers key actionable mutations while providing precision detection levels down to as low as 0.01%. The panel uses our MX-ICP technology. The panel adds to the mutations included in our first epidermal growth factor receptor (“EGFR”) tests launched in May 2015 adding mutations in EGFR exons 18-21 that are associated with resistance to tyrosine kinase inhibitor (“TKI”) cancer drugs and broadening the testing options available to the oncologist. Our EGFR panels address all of the known mutations that affect EGFR status and the likely efficacy of TKI drugs for the patient’s cancer.

On September 8, 2015, we entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Edge BioSystems, Inc. (“Buyer”), pursuant to which we agreed to sell to Buyer, and Buyer agreed to purchase from us, our manufacturing, marketing and selling of high quality polymer and silica based beads and resin and chromatography columns business (collectively, the “Columns Business”). Pursuant to the Asset Purchase Agreement, Buyer acquired substantially all of the assets used solely in connection with the Columns Business and assumed certain liabilities of the Columns Business for a total cash purchase price of approximately \$2.1 million (the “Asset Sale”), which was paid on September 8, 2015 upon the closing of the Asset Sale.

## Table of Contents

On September 17, 2015, we announced that we had granted our first license for commercial rights to our liquid biopsy technology. We granted the exclusive license to the University of Melbourne to use our MX-ICP technology for research and clinical applications in Australia.

On September 25, 2015, we entered into a binding term sheet with ADSTEC Corporation (“ADSTEC”), effective as of September 30, 2015, to set forth the terms and conditions by which ADSTEC will purchase from us certain of the assets constituting, and assume certain of the liabilities related to, our Genetic Assays and Platforms business, including certain of our inventory and our facilities located in Glasgow, Scotland and Irvington Road, Omaha, Nebraska, for a purchase price of approximately \$0.3 million, subject to adjustment in certain circumstances (collectively, the “Transaction”). We anticipate that definitive agreements relating to the Transaction will be entered into during the fourth quarter of 2015. The final terms of the Transaction are subject to the negotiation and finalization of the definitive agreements relating to the Transaction, and the material terms of the Transaction may differ from those set forth in the binding term sheet.

On November 5, 2015, we announced the launch of our new comprehensive MX-ICP Non-Small Cell Lung Cancer (“NSCLC”) Analysis panel that covers the key actionable mutations that are relevant to the targeted treatment of NSCLC, one of the most common types of cancer and the leading cause of cancer deaths in the U.S. The panel uses our MX-ICP technology that generates highly accurate results from small amounts of blood or tissue samples at precision detection levels down to as low as 0.01%. It is available for clinical diagnostic use through our CLIA laboratory.

### Uncertainties

We have historically operated at a loss and have not consistently generated sufficient cash from operating activities to cover our operating and other cash expenses. We have been able to historically finance our operating losses through borrowings or from the issuance of additional equity. At September 30, 2015, we had cash and cash equivalents of \$2.8 million. Our ability to continue as a going concern is dependent upon a combination of generating additional revenue, improving cash collections, potentially selling underutilized assets and, if necessary, raising additional financing to meet our obligations and pay our liabilities arising from normal business operations when they come due. The outcome of these matters cannot be predicted with any certainty at this time and raises substantial doubt that we will be able to continue as a going concern.

The uncertainty of current general economic conditions could negatively impact our business in the future. There are many factors that affect the market demand for our products and services that we cannot control. Our Laboratory Services business is dependent upon reimbursement from government and private payors that continually look for ways to reduce costs, including by unilaterally reducing reimbursement for services such as those that we provide. The government issued new reimbursement codes in 2013, which were set at pricing levels that were generally lower than the levels for identical tests in 2012. Certain private payors also used the issuance of the new codes as an opportunity to unilaterally lower their reimbursement rates. There are no assurances that reimbursements from certain of these providers will remain at levels that will allow us to be profitable.

We have translation risk that occurs when transactions are consummated in a currency other than British Pound Sterling, which is the functional currency of our foreign subsidiary. These transactions, which are most often consummated in Euros, must be translated into British Pound Sterling. In addition, results of operations and the balance sheet of our foreign subsidiary are translated from British Pound Sterling to our reporting currency, which is the U.S. Dollar. As a result, we are subject to exchange rate risk. Fluctuations in foreign currency exchange rates could impact our business and financial results.

### Results of Continuing Operations

Net sales for the three months ended September 30, 2015 decreased by \$0.1 million, or 3%, compared to the same period in 2014. Our gross profit margin increased to 45% for the three months ended September 30, 2015 from 42% for the three months ended September 30, 2014. Loss from operations was \$8.9 million for the three months ended



Edgar Filing: TRANSGENOMIC INC - Form 10-Q

September 30, 2015, compared to \$4.0 million for the three months ended September 30, 2014.

Three Months Ended September 30, 2015 and 2014

Net Sales. Net sales were as follows:

	Dollars in Thousands		Change		
	Three Months Ended				
	September 30,		\$	%	
	2015	2014			
Total Net Sales	\$3,960	\$4,064	\$(104	) (3	)%

27

---

Table of Contents

Net sales decreased by \$0.1 million, or 3%, during the three months ended September 30, 2015 as compared to the same period in 2014. The decrease reflects \$0.2 million less in sales of our contract laboratory services, partially offset by a \$0.1 million increase in revenues from patient testing services.

Cost of Goods Sold. Cost of goods sold includes material costs for the products that we sell and other direct costs (primarily personnel costs, rent, supplies and depreciation) associated with the operations of our laboratories.

Gross Profit. Gross profit and gross margins were as follows:

	Dollars in Thousands				
	Three Months Ended		Margin %		
	September 30, 2015	2014	2015	2014	
Gross Profit	\$1,764	\$1,717	45	% 42	%

Gross profit was \$1.8 million, or 45% of total net sales, during the third quarter of 2015, compared to \$1.7 million, or 42% of total net sales, during the same quarter of 2014. This increase in gross margin resulted from a reduction in our laboratories' direct costs, mainly due to lower costs for operating supplies.

Selling, General and Administrative Expenses. Selling, general and administrative expenses primarily consist of personnel costs, marketing, travel costs, professional fees, facility costs and bad debt provisions. Our selling, general and administrative costs decreased by \$2.0 million to \$3.1 million during the three month period ended September 30, 2015 as compared to the same period in 2014. \$1.0 million of the decrease from the prior year is the result of an accrued liability that we reversed during the three months ended September 30, 2015. Excluding the accrued liability reversal, our selling, general and administrative costs decreased by \$1.0 million during the three month period ended September 30, 2015 as compared to the same period in 2014. This decrease was due to lower personnel costs as a result of lower headcount, lower marketing and promotion costs and lower stock compensation costs in the third quarter of 2015 as compared to the third quarter of 2014.

Research and Development Expenses. Research and development expenses primarily include personnel costs, intellectual property fees, outside services, collaboration expenses, laboratory supplies and facility costs and are expensed in the period in which they are incurred. For the three months ended September 30, 2015, research and development expenses totaled \$0.6 million as compared to \$0.7 million for the three months ended September 30, 2014. Research and development expenses totaled 14% and 16% of net sales during the three months ended September 30, 2015 and 2014, respectively. The reduction in expenses during the three months ended September 30, 2015 resulted from reduced spending on supplies and patent costs.

Impairment of long-lived assets. We performed an interim testing of impairment of long-lived assets as of September 30, 2015 due to the significant decline in the market price of our stock. As a result of this testing, we recorded impairment charges of approximately \$7.0 million during the three months ended September 30, 2015. The impairment charge includes \$0.9 million related to property and equipment and \$6.1 million of charges related to amortizable intangibles. There were no impairment charges during the three months ended September 30, 2014.

Other Income (Expense). Other expense for the three months ended September 30, 2015 and 2014 includes interest expense of \$0.2 million and \$0.2 million, respectively. In addition, we recorded other income for the three months ended September 30, 2015 and other expense for the three months ended September 30, 2014 for the revaluation of common stock warrants, which was due to the change in fair value of the common stock warrant liability. The income and expense associated with the change in fair value of the warrants is a non-cash item.

Income Tax Benefit. Income tax benefit, net of expense, was \$0.5 million and \$1.5 million for the three months ended September 30, 2015 and 2014, respectively. For both years, the net income tax benefit included less than \$0.1 million for a deferred tax liability related to the tax deductibility of our goodwill, which is an indefinite-lived asset. We expect this deferred income tax expense to be approximately \$0.2 million annually going forward. The three months ended September 30, 2015 and 2014 also included a tax benefit of \$0.5 million and \$1.5 million, respectively. The income tax benefit results from intraperiod tax accounting that requires recording tax expense on income in discontinued operations offset by a tax benefit in continuing operations. That benefit is partially reduced by an increase in our valuation allowance on deferred tax assets.

Nine Months Ended September 30, 2015 and 2014

Net Sales. Net sales for the nine months ended September 30, 2015 increased by \$2.1 million, or 18%, compared to the same period in 2014. The increase was due to higher test volumes from both patient testing and our contract laboratory services. Net sales were as follows:

28

---

Table of Contents

	Dollars in Thousands				
	Nine Months Ended				
	September 30,		Change		
	2015	2014	\$	%	%
Total Net Sales	\$13,670	\$11,595	\$2,075	18	%

Cost of Goods Sold. Cost of goods sold includes material costs for the products that we sell and other direct costs (primarily personnel costs, rent, supplies and depreciation) associated with the operations of our laboratories.

Gross Profit. Gross profit and gross margins were as follows:

	Dollars in Thousands				
	Nine Months Ended				
	September 30,		Margin %		
	2015	2014	2015	2014	%
Gross Profit	\$6,938	\$4,704	51	% 41	%

Gross profit was \$6.9 million, or 51% of total net sales, during the first nine months of 2015, compared to \$4.7 million, or 41% of total net sales, during the same period in 2014. The higher margins in the current year period were due to increased revenue from higher test volumes along with lower costs for operating supplies in our laboratories.

Selling, General and Administrative Expenses. Selling, general and administrative expenses primarily consist of personnel costs, marketing, travel costs, professional fees, facility costs and bad debt provisions. Our selling, general and administrative costs decreased by \$2.6 million to \$12.3 million during the nine month period ended September 30, 2015 compared to the same period in 2014. \$1.0 million of the decrease from prior year is the result of an accrued liability that we reversed during 2015. Excluding the accrued liability reversal, our selling, general and administrative costs decreased by \$1.6 million during the nine month period ended September 30, 2015 as compared to the same period in 2014. The decrease was due to lower personnel costs on lower headcount and lower stock compensation costs in the first nine months of 2015 as compared to the same period in 2014.

Research and Development Expenses. Research and development expenses primarily include personnel costs, intellectual property fees, outside services, collaboration expenses, laboratory supplies and facility costs and are expensed in the period in which they are incurred. For the nine months ended September 30, 2015 and 2014, these costs totaled \$1.7 million and \$2.2 million, respectively. The decrease in research and development costs in the nine months ended September 30, 2015 resulted from reduced spending on supplies and patent costs. Research and development expenses totaled 12% and 19% of net sales during the nine months ended September 30, 2015 and 2014, respectively.

Impairment of long-lived assets. We performed an interim testing of impairment of long-lived assets as of September 30, 2015 due to the significant decline in the market price of our stock. As a result of this testing, we recorded impairment charges of approximately \$7.0 million during the nine months ended September 30, 2015. The impairment charge includes \$0.9 million related to property and equipment and \$6.1 million of charges related to amortizable intangibles. There were no impairment charges during the nine months ended September 30, 2014.

Other Income (Expense). Other expense for the nine months ended September 30, 2015 and 2014 includes interest expense of \$0.6 million and \$0.5 million, respectively. In addition, we recorded other expense for the nine months ended September 30, 2015 and other income for the nine months ended September 30, 2014 for the revaluation of common stock warrants, which was due to the change in fair value of the common stock warrant liability. The income and expense associated with the change in fair value of the warrants is a non-cash item.

Income Tax Benefit. Income tax benefit, net of expense, was \$0.5 million and \$1.2 million for the nine months ended September 30, 2015 and 2014, respectively. For the nine months ended September 30, 2015 and 2014, the net income tax benefit included income tax expense of \$0.1 million and \$0.6 million, respectively, for a deferred tax liability related to the tax deductibility of our goodwill, which is an indefinite-lived asset. We expect this deferred income tax expense to be approximately \$0.2 million annually going forward. The nine months ended September 30, 2015 and 2014 also included a tax benefit of \$0.5 million and \$1.8 million, respectively. The income tax benefit results from intraperiod tax accounting that requires recording tax expense on income in discontinued operations offset by a tax benefit in continuing operations. That benefit is partially reduced by an increase in our valuation allowance on

deferred tax assets.

Discontinued Operations For The Three and Nine Months Ended September 30, 2015 and 2014.

29

---

Table of Contents

During the three months ended September 30, 2015, we decided to divest our Genetic Assays and Platforms business resulting in a strategic shift that will have a major effect on our operations and financial results. Therefore, the divested and to be divested Genetic Assays and Platforms operations meet the criteria to be reported as discontinued operations. The related assets, liabilities, results of operations and cash flows are classified as assets held for sale, liabilities held for sale and discontinued operations for all periods presented.

Revenues and net income (loss) of the discontinued operations consisted of the following:

(in thousands)	Three months ended		Nine months ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Net sales	\$1,877	\$2,308	\$5,720	\$7,792
Operating (loss) income from discontinued operations, before gain on sale of product line and tax	\$(68	) \$(20	) \$(356	) \$821
Gain on sale of product line	1,532	4,114	1,532	4,114
Income tax expense	530	1,430	598	1,675
Income from discontinued operations, net of tax	\$934	\$2,664	\$578	\$3,260

## Liquidity and Capital Resources

Our working capital positions at September 30, 2015 and December 31, 2014 were as follows:

	Dollars in Thousands			
	September 30, 2015	December 31, 2014	Change	
Current assets (including cash and cash equivalents of \$2,787 and \$1,609, respectively)	\$16,104	\$13,647	\$2,457	
Current liabilities	16,147	11,257	4,890	
Working capital	\$(43	) \$2,390	\$(2,433	)

We entered into an Unsecured Convertible Promissory Note Purchase Agreement (the "Note Purchase Agreement"), dated December 31, 2014, with an accredited investor (the "Initial Investor"), pursuant to which we issued and sold, on December 31, 2014, to the Initial Investor in a private placement an unsecured convertible promissory note (the "Initial Note") in the aggregate principal amount of \$750,000. The Initial Note converted in full into 502,786 shares of our common stock, in accordance with the terms of the Initial Note.

Pursuant to the terms of the Note Purchase Agreement, on January 15, 2015, we entered into a purchase agreement with seven additional accredited investors (the "Additional Investors") and issued and sold, on January 20, 2015, to the Additional Investors in a private placement notes in an aggregate principal amount of \$925,000 (the "Additional Notes" and, together with the Initial Note, the "2015 Notes").

The 2015 Notes accrue interest at a rate of 6% per year and mature on December 31, 2016. Under the terms of each of the 2015 Notes, the outstanding principal and unpaid interest accrued is convertible into shares of our common stock as follows: (i) commencing upon the date of issuance of the 2015 Notes (but no earlier than January 1, 2015), the investor holding such 2015 Note is entitled to convert, on a one-time basis, up to 50% of the outstanding principal and unpaid interest accrued under the 2015 Note, into shares of our common stock at a conversion price equal to the lesser of (a) the average closing price of the common stock on the principal securities exchange or securities market on which our common stock is then traded (the "Market") for the 20 consecutive trading days immediately preceding the date of conversion, and (b) \$2.20 (subject to adjustment for stock splits, stock dividends, other distributions, recapitalizations and the like); and (ii) commencing February 15, 2015, the investor holding such 2015 Note is entitled to convert, on a one-time basis, any or all of the remaining outstanding principal and unpaid interest accrued under the 2015 Note, into shares of our common stock at a conversion price equal to 85% of the average closing price of our common stock on the Market for the 15 consecutive trading days immediately preceding the date of conversion.

As of September 30, 2015, \$400,000 of the aggregate principal amount of the Additional Notes has been converted into an aggregate of 281,023 shares of our common stock.



Table of Contents

On February 27, 2015, we entered into a purchase agreement with Craig-Hallum Capital Group LLC, as the underwriter (the “Underwriter”), pursuant to which we sold 3,573,899 shares of our common stock and corresponding warrants to purchase up to 714,780 shares of our common stock. Each share of common stock was sold in combination with a warrant to purchase 0.20 of a share of our common stock. The purchase price to the public for each share of common stock and accompanying warrant was \$1.95.

The purchase price paid by the Underwriter to us for each share of common stock and the accompanying warrants was \$1.8135. The net proceeds, after deducting the Underwriter’s discount and other estimated expenses, were approximately \$6.2 million.

On June 30, 2015, we entered into a Securities Purchase Agreement with certain accredited investors (the “July 2015 Investors”) pursuant to which, on July 7, 2015, we sold to the July 2015 Investors, and the July 2015 Investors purchased from us, (i) an aggregate of approximately 1.5 million shares of our common stock at a price per share of \$1.42, (ii) warrants (the “Series B Warrants”) to purchase up to an aggregate of 0.7 million shares of our common stock with an exercise price of \$0.01 per share, and (iii) warrants (the “Series A Warrants” and, together with the Series B Warrants, the “July 2015 Warrants”) to purchase up to an aggregate of 1.2 million shares of our common stock, with an exercise price of \$1.66 per share (collectively, the “July 2015 Offering”). The purchase price for the Series B Warrants was \$1.42 per share of our common stock subject to the Series B Warrants. Each of the July 2015 Warrants has a term of 5 and 1/2-years. The Series B Warrants are immediately exercisable. The Series A Warrants will be exercisable beginning on January 7, 2016, six months from the date of issuance. The aggregate gross proceeds to us from the July 2015 Offering were approximately \$3.0 million.

Craig-Hallum Capital Group LLC (the “2015 Placement Agent”) served as the sole placement agent for the Offering. In consideration for services rendered as the placement agent in the July 2015 Offering, we (i) paid to the 2015 Placement Agent cash commissions equal to approximately \$212,783, or 7.0% of the gross proceeds received in the July 2015 Offering; (ii) issued to the 2015 Placement Agent a five-year warrant to purchase up to 107,033 shares of our common stock with an exercise price of \$1.66 per share and which is subject to other terms that are the same as the terms of the Series A Warrants; and (iii) reimbursed the 2015 Placement Agent for reasonable out-of-pocket expenses, including fees paid to the 2015 Placement Agent’s legal counsel, incurred in connection with the July 2015 Offering, which reimbursable expenses did not exceed \$50,000.

On September 8, 2015, we entered into an Asset Purchase Agreement (the “Asset Purchase Agreement”) with Edge BioSystems, Inc. (“Buyer”), pursuant to which we agreed to sell to Buyer, and Buyer agreed to purchase from us, our manufacturing, marketing and selling of high quality polymer and silica based beads and resin and chromatography columns business (collectively, the “Columns Business”). Pursuant to the Asset Purchase Agreement, Buyer acquired substantially all of the assets used solely in connection with the Columns Business and assumed certain liabilities of the Columns Business for a total cash purchase price of approximately \$2.1 million (the “Asset Sale”), which was paid on September 8, 2015 upon the closing of the Asset Sale.

On September 25, 2015, we entered into a binding term sheet with ADSTEC Corporation (“ADSTEC”), effective as of September 30, 2015, to set forth the terms and conditions by which ADSTEC will purchase from us certain of the assets constituting, and assume certain of the liabilities related to, our Genetic Assays and Platforms business, including certain of our inventory and our facilities located in Glasgow, Scotland and Irvington Road, Omaha, Nebraska, for a purchase price of approximately \$0.3 million, subject to adjustment in certain circumstances (collectively, the “Transaction”). We anticipate that definitive agreements relating to the Transaction will be entered into during the fourth quarter of 2015. The final terms of the Transaction are subject to the negotiation and finalization of the definitive agreements relating to the Transaction, and the material terms of the Transaction may differ from those set forth in the binding term sheet.

Please see Note 5 - “Debt” and Note 6 - “Commitments and Contingencies” in the Notes to Unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report on Form 10-Q for additional information regarding our outstanding debt and debt servicing obligations.

At September 30, 2015, we had cash on hand of \$2.8 million. Our current operating plan projects improved operating results, improvement in collection rates and monetization of underutilized assets. As with any operating plan, there are



risks associated with our ability to execute it. Therefore, there can be no assurance that we will be able to satisfy our obligations, or achieve the operating improvements as contemplated by the current operating plan. If we are unable to execute this plan, we will need to find additional sources of cash not contemplated by the current operating plan and/or raise additional capital to sustain continuing operations as currently contemplated. We could seek to raise additional funds through various potential sources such as through the sale of assets or sale of debt or equity securities. However, there can be no assurance that the additional funding sources will be available to us on reasonable terms or at all. If we are unable to achieve our operating plan or obtain additional financing, our business would be jeopardized and we may not be able to continue as a going concern.

Analysis of Cash Flows - Nine Months Ended September 30, 2015 and 2014

31

---

## Table of Contents

**Net Change in Cash and Cash Equivalents.** Cash and cash equivalents increased by \$1.2 million during the nine months ended September 30, 2015, compared to a decrease of \$0.7 million during the nine months ended September 30, 2014. These amounts include cash provided by discontinued operations of \$2.1 million, which includes \$1.9 million from the sale of a product line, and \$3.4 million, which includes \$3.7 million from the sale of a product line, for the nine months ended September 30, 2015 and 2014, respectively.

### **Cash Flows From Continuing Operations**

**Cash Flows Used in Operating Activities.** Cash flows used in operating activities totaled \$9.7 million during the nine months ended September 30, 2015, compared to cash flows used in operating activities of \$10.9 million during the nine months ended September 30, 2014. The cash flows used in operating activities in the first nine months of 2015 included the net loss of \$14.2 million and an increase in accounts receivable of \$6.6 million, adjusted for non-cash items, including the provision for losses on doubtful accounts of \$2.7 million, stock compensation expense of \$0.5 million, impairment of long-lived assets of \$7.0 million and depreciation and amortization of \$1.5 million. The cash flows used in operating activities in the first nine months of 2014 included the net loss of \$11.4 million and an increase in accounts receivable of \$5.5 million, adjusted for non-cash items, including the provision for losses on doubtful accounts of \$2.7 million, stock compensation expense of \$1.0 million and depreciation and amortization of \$1.5 million.

**Cash Flows Used in Investing Activities.** Cash flows used in investing activities was \$0.3 million for the nine months ended September 30, 2015 and \$0.2 million for the nine months ended September 30, 2014. Cash flows used in investing activities in the first nine months of 2015 and 2014 included purchases of property and equipment of \$0.3 million and \$0.1 million, respectively.

**Cash Flows Provided by Financing Activities.** Cash flows provided by financing activities totaled \$9.0 million for the nine months ended September 30, 2015, which included net proceeds of approximately \$9.0 million from our common stock offerings during the first nine months of 2015 and \$0.9 million from the issuance of unsecured convertible promissory notes in January 2015. These proceeds were partially offset by payments on our debt and capital lease obligations. Cash flows provided by financing activities during the nine months ended September 30, 2014 included proceeds from the issuance of Series B Convertible Preferred Stock and net borrowing on our debt, partially offset by payments on our capital lease obligations.

### **Off-Balance Sheet Arrangements**

At each of September 30, 2015 and December 31, 2014, we did not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

### **Contractual Obligations and Commitments**

There have been no material changes to our contractual obligations outside the normal course of business as compared to those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014, filed with the Securities and Exchange Commission on April 15, 2015.

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

Accounting policies used in the preparation of our consolidated financial statements may involve the use of management judgments and estimates. Certain of our accounting policies are considered critical as they are both important to the portrayal of our financial statements and require significant or complex judgments on the part of management. Our judgments and estimates are based on experience and assumptions that we believe are reasonable under the circumstances. Further, we evaluate our judgments and estimates from time to time as circumstances change. Actual financial results based on judgments or estimates may vary under different assumptions or circumstances. Our critical accounting policies are discussed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014, filed with the Securities and Exchange Commission on April 15, 2015.

### **Recently Issued Accounting Pronouncements**

## Edgar Filing: TRANSGENOMIC INC - Form 10-Q

Please refer to our Annual Report on Form 10-K for the fiscal year ended December 31, 2014, filed with the Securities and Exchange Commission on April 15, 2015. There have been no changes to those accounting pronouncements listed except as noted in Note 2 - "Summary of Significant Accounting Policies-Recent Accounting Pronouncements" to the Notes to Unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report on Form 10-Q.

Impact of Inflation

32

---

Table of Contents

We do not believe that price inflation or deflation had a material adverse effect on our financial condition or results of operations during the periods presented.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are a smaller reporting company, as defined by Rule 12b-2 of the Securities Exchange Act of 1934, as amended, and are not required to provide the information required under this item.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures.

Management performed, with the participation of our Chief Executive Officer and Interim Chief Financial Officer, an evaluation of the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Our disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Interim Chief Financial Officer, to allow timely decisions regarding required disclosures. Based on the evaluation, our Chief Executive Officer and Interim Chief Financial Officer concluded that, as of September 30, 2015, our disclosure controls and procedures were not effective because of the material weaknesses in our internal control over financial reporting, as described in Management's Report On Internal Control Over Financial Reporting in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2014, which continue to exist as of September 30, 2015. Specifically, management determined that we did not maintain effective control over proper timing and recognition of revenue and over the elements used in our analysis and evaluation of the allowance for doubtful accounts to ensure that the allowance for doubtful accounts was reasonably stated.

Remediation of Material Weaknesses in Internal Control over Financial Reporting.

We are in the process of improving our controls to remediate the material weaknesses in internal control over financial reporting that existed as of December 31, 2014. The actions we are taking are subject to ongoing senior management review, as well as audit committee oversight. We have hired a divisional controller who will assist in the remediation efforts. The remedial actions include, among other steps, a reconciliation of proof of delivery (fax confirmation) to invoice, to unbilled reports and to error processing queues. In addition, effective beginning with the quarter ended March 31, 2015, an additional review process was added to the allowance for doubtful accounts analysis such that current and historical trends of payments are given more weight in the determination of the allowance amount. While implementation of these remediation actions are in process, it will take time for such actions to be fully integrated and confirmed to be effective and sustainable. Until such time, the material weaknesses described above will continue to exist.

Changes in Internal Control over Financial Reporting.

We have evaluated the changes in our internal control over financial reporting that occurred during the three months ended September 30, 2015 and concluded that there have not been any changes that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to a number of claims of various amounts that arise out of the normal course of our business. In our opinion, the disposition of pending claims will not have a material adverse effect on our financial position, results of operations or cash flows.

Item 1A. Risk Factors

There have been no material changes in our risk factors from those previously disclosed in Part 1, Item 1A, "Risk Factors," of our Annual Report on Form 10-K for the year ended December 31, 2014 that was filed with the Securities and Exchange Commission on April 15, 2015, except for the addition of the following additional risk factor:

If we fail to comply with the continued listing requirements of the NASDAQ Capital Market, our common stock may be delisted and the price of our common stock and our ability to access the capital markets could be negatively impacted.

Our common stock is currently listed on the NASDAQ Capital Market. In order for our shares to continue to be listed on the NASDAQ Capital Market, we must satisfy the continued listing requirements of The NASDAQ Stock Market LLC, or NASDAQ, including, among other things, a minimum closing bid price requirement. If our shares trade for 30 consecutive business days below a closing bid price of \$1.00, NASDAQ will send us a deficiency notice, advising us that we have been afforded a "compliance period" of 180 calendar days to regain compliance with the closing bid price requirement. The closing bid price of our common stock has been below \$1.00 at various periods during the quarter ended September 30, 2015 and the quarter ending December 31, 2015.

A delisting of our common stock from the NASDAQ Capital Market could materially reduce the liquidity of our common stock and result in a corresponding material reduction in the market price of our common stock. In addition, delisting could harm our ability to raise capital through alternative financing sources on terms acceptable to us, or at all, and may result in the potential loss of confidence by investors and fewer business development opportunities, which would have a material adverse effect on our financial condition and results of operations.

Item 6. Exhibits

(a) Exhibits

- |      |  |
|------|--|
| †2.1 | Asset Purchase Agreement among the Registrant, Scoli Acquisition Sub, Inc. and Axial Biotech, Inc. dated August 27, 2012 (incorporated by reference to Exhibit 2.1 to the Registrant's Quarterly Report on Form 10-Q filed on November 8, 2012). |
| 3.1  | Third Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Quarterly Report on Form 10-Q filed on November 14, 2005).   |
| 3.2  | Certificate of Amendment of Third Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on May 29, 2012).                           |
| 3.3  | Certificate of Amendment of Third Amended and Restated Certificate of Incorporation of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on January 28, 2014).                       |

Edgar Filing: TRANSGENOMIC INC - Form 10-Q

3.4 Certificate of Amendment of Certificate of Designation of Series A Convertible Preferred Stock of the Registrant (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on March 6, 2014).

3.5 Certificate of Designation of Series B Convertible Preferred Stock of the Registrant (incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K filed on March 6, 2014).

3.6 Amended and Restated Bylaws of the Registrant (incorporated by reference to Exhibit 3(ii) to the Registrant's Current Report on Form 8-K filed on May 25, 2007).

4.1 Form of Certificate of the Registrant's Common Stock (incorporated by reference to Exhibit 4 to the Registrant's Registration Statement on Form S-1 (Registration No. 333-32174) filed on March 10, 2000).

34

---

Table of Contents

- 4.2 Form of Series A Convertible Preferred Stock Warrant issued to Third Security Senior Staff 2008 LLC, Third Security Staff 2010 LLC and Third Security Incentive 2010 LLC (incorporated by reference to Exhibit 4.2 to the Registrant's Current Report on Form 8-K filed on January 4, 2011).
- 4.3 Registration Rights Agreement, dated December 29, 2010, by and among the Registrant, Third Security Senior Staff 2008 LLC, Third Security Staff 2010 LLC and Third Security Incentive 2010 LLC (incorporated by reference to Exhibit 4.3 to the Registrant's Current Report on Form 8-K filed on January 4, 2011).
- 4.4 First Amendment to Registration Rights Agreement dated November 8, 2011 (incorporated by reference to Exhibit 4.2 to the Registrant's Current Report on Form 8-K filed on November 14, 2011).
- 4.5 Form of Warrant to Purchase Common Stock issued by the Registrant to the Third Security Entities on February 7, 2012 (incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed on February 7, 2012).
- 4.6 Form of Warrant to Purchase Common Stock issued by the Registrant to the Investors on February 7, 2012 (incorporated by reference to Exhibit 10.3 to the Registrant's Current Report on Form 8-K filed on February 7, 2012).
- 4.7 Form of Registration Rights Agreement entered into by and among the Registrant, the Third Security Entities and the Investors dated February 2, 2012 (incorporated by reference to Exhibit 10.4 to the Registrant's Current Report on Form 8-K filed on February 7, 2012).
- 4.8 Registration Rights Agreement, entered into by and among the Registrant and the Investors, dated January 24, 2013 (incorporated by reference to Exhibit 10.3 to the Registrant's Current Report on Form 8-K/A filed on January 31, 2013).
- 4.9 Form of Warrant issued by the Registrant to the Investors on January 30, 2013 (incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K/A filed on January 31, 2013).
- 4.10 Registration Rights Agreement, dated as of March 5, 2014, by and among the Registrant, Third Security Senior Staff 2008 LLC, Third Security Staff 2014 LLC and Third Security Incentive 2010 LLC (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on March 6, 2014).
- 4.11 Securities Purchase Agreement, dated as of October 22, 2014, by and among Transgenomic, Inc. and the Investors (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on October 22, 2014).
- 4.12 Form of Warrant to Purchase Common Stock issued by the Registrant to Craig-Hallum Capital Group LLC on February 27, 2015 (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on February 27, 2015).
- 4.13

Edgar Filing: TRANSGENOMIC INC - Form 10-Q

Unsecured Convertible Promissory Note Purchase Agreement, dated as of December 31, 2014, by and among Transgenomic, Inc. and the Investors (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on January 7, 2015).

- 4.14 Form of Unsecured Convertible Promissory Note issued by Transgenomic, Inc. to the Investor pursuant to the Unsecured Convertible Promissory Note Purchase Agreement, dated as of December 31, 2014 (incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K filed on January 7, 2015).
- 4.15 Form of Warrant to Purchase Common Stock (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K filed on February 27, 2015).
- 4.16 Registration Rights Agreement, by and among Transgenomic, Inc. and the Investors, dated June 30, 2015 (incorporated by reference to Exhibit 4.1 to the Registrant's Amendment No. 1 to Current Report on Form 8-K/A filed on July 7, 2015).
- 4.17 Form of Series B Warrant, issued by Transgenomic, Inc. to an Investor on July 7, 2015 (incorporated by reference to Exhibit 4.2 to the Registrant's Amendment No. 1 to Current Report on Form 8-K/A filed on July 7, 2015).
- 4.18 Form of Series A Warrant, issued by Transgenomic, Inc. to the Investors on July 7, 2015 (incorporated by reference to Exhibit 4.3 to the Registrant's Amendment No. 1 to Current Report on Form 8-K/A filed on July 7, 2015).



Table of Contents

4.19	Form of Warrant, issued by Transgenomic, Inc. to the Placement Agent on July 7, 2015 (incorporated by reference to Exhibit 4.4 to the Registrant’s Amendment No. 1 to Current Report on Form 8-K/A filed on July 7, 2015).
10.1	Limited Waiver and Seventh Amendment to Loan and Security Agreement (Term Loan and Revolving Loan), by and among Transgenomic, Inc., Third Security Senior Staff 2008 LLC, as administrative agent and a lender, and the other lenders party thereto, dated as of September 4, 2015.
10.2	Asset Purchase Agreement, by and between Transgenomic, Inc. and Edge BioSystems, Inc., dated September 8, 2015.
10.3	Confidential and Binding Term Sheet, by and between Transgenomic, Inc. and ADSTEC Corporation, effective as of September 30, 2015.
31.1	Certification of Paul Kinnon, President, Chief Executive Officer and Interim Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, as amended.
32.1	Certification of Paul Kinnon, President, Chief Executive Officer and Interim Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, as amended.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
†	Pursuant to Item 601(b)(2) of Regulation S-K, the schedules to this agreement have been omitted. The Registrant agrees to furnish supplementally a copy of any omitted schedule to the Securities and Exchange Commission upon request.

Table of Contents

SIGNATURES

Pursuant to the requirements 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.

TRANSGENOMIC, INC.

Date: November 16, 2015

By: /S/ PAUL KINNON

Paul Kinnon

President, Chief Executive Officer and Interim  
Chief Financial Officer (Principal Executive  
Officer and Principal Financial Officer)