Alliqua BioMedical, Inc.
Form 10-Q
October 26, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: September 30, 2018

OR

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

For the transition period from _____ to _____

Commission file number: **001-36278**

Alliqua BioMedical, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**58-2349413**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
2150 Cabot Blvd West, Suite B	
	19047
Langhorne, PA	
(Address of principal executive office)	(Zip Code)

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

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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes þ No ¨

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

Large accelerated filer ¨ Accelerated filer ¨

Non-accelerated filer þ

Smaller reporting company þ Emerging growth company ¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨

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

As of October 26, 2018, the registrant had 5,005,210 shares of common stock outstanding.

ALLIQUA BIOMEDICAL, INC.

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

	September 30, 2018 (Unaudited)	December 31, 2017
ASSETS:		
Current Assets:		
Cash and cash equivalents	$11,095	$2,181
Accounts receivable, net	172	99
Inventory, net	183	93
Prepaid expenses and other current assets	341	41
Current assets of discontinued operations	445	5,062
Total current assets	12,236	7,476
Improvements and equipment, net	279	522
Other assets	178	173
Assets of discontinued operations - noncurrent	-	24,769
Total assets	$12,693	$32,940
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$305	$684
Accrued expenses and other current liabilities	256	712
Warrant liability	186	130
Current liabilities of discontinued operations	2,351	15,443
Total current liabilities	3,098	16,969
Other long-term liabilities	53	59
Long term liabilities of discontinued operations	-	245
Total liabilities	3,151	17,273
Commitments and Contingencies		
Stockholders' Equity		

Preferred Stock, par value $0.001 per share, 1,000,000 shares authorized, no shares issued and outstanding	-	-
Common Stock, par value $0.001 per share, 95,000,000 shares authorized; 5,005,210 and 4,986,034 shares issued and outstanding as of September 30, 2018 and December 31, 2017, respectively	5	5
Additional paid-in capital	166,674	165,672
Accumulated deficit	(157,137)	(150,010)
Total stockholders' equity	9,542	15,667
Total liabilities and stockholders' equity	$12,693	$32,940

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

ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(in thousands, except share and per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Revenue, net of returns, allowances and discounts	$348	$499	$1,756	$1,354
Cost of revenues	361	400	1,371	1,335
Gross profit/(loss)	(13)	99	385	19
Operating expenses				
Selling, general and administrative	745	1,522	3,892	4,057
Business development costs	212	-	413	635
Total operating expenses	957	1,522	4,305	4,692
Loss from operations	(970)	(1,423)	(3,920)	(4,673)
Other (expense) income				
Interest income	8	1	12	5
Change in fair value of warrant liability	(22)	35	(56)	404
Loss on early extinguishment of debt, net	-	(182)	(1,706)	(182)
Total other (expense) income	(14)	(146)	(1,750)	227
Loss from continuing operations before tax	(984)	(1,569)	(5,670)	(4,446)
Income tax expense	-	(3)	-	(9)
Loss from continuing operations	(984)	(1,572)	(5,670)	(4,455)
Discontinued operations:				
Gain/(loss) from discontinued operations, net of tax of $0, for the three and nine months ended September 30, 2018 and 2017	204	(2,828)	(7,003)	(11,145)
Gain on sale of assets, net of tax of ($0.026) million and $0.5 million for the three and nine months ended September 30, 2018, respectively	26	1,700	5,546	1,700
Income/(loss) from discontinued operations, net of tax	230	(1,128)	(1,457)	(9,445)

Net loss	$(754)	$(2,700)	$(7,127)	$(13,900)
Net loss per basic and diluted common share:				
Loss from continuing operations	$(0.20)	$(0.33)	$(1.16)	$(1.08)
Income/(loss) from discontinued operations	0.04	(0.59)	(1.43)	(2.70)
Gain on sale of assets	0.01	0.36	1.13	0.41
Total from discontinued operations	0.05	(0.23)	(0.30)	(2.29)
Net loss per basic and diluted common share	$(0.15)	$(0.56)	$(1.46)	$(3.37)
Weighted average shares used in computing net loss per basic and diluted common share	4,984,923	4,753,789	4,902,657	4,125,653

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

ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands)

	Nine Months Ended September 30,	
	2018	2017
Operating Activities		
Net loss	$(7,127)	$(13,900)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,802	4,111
Amortization of deferred lease incentive	(19)	(34)
Deferred income tax expense	-	9
Provision for doubtful accounts	177	169
Reserve for note receivable	-	350
Provision for excess and slow moving inventory	(8)	12
Stock-based compensation expense	1,004	1,604
Deferred rent	2	2
Amortization of debt issuance and discount costs	254	631
Loss on early extinguishment of debt	1,706	182
Warrant modification expense	-	803
Change in fair value of warrant liability	56	(404)
Fair value adjustment of contingent consideration liability	-	35
Gain on sale of assets	(5,546)	(1,700)
Changes in operating assets and liabilities:		
Accounts receivable	2,465	(499)
Inventory	(202)	414
Prepaid expenses and other assets	(146)	439
Accounts payable	498	(1,023)
Accrued expenses and other liabilities	(2,500)	(1,000)
Net Cash Used in Operating Activities	(7,584)	(9,799)
Investing Activities		
Proceeds from sale of assets	29,000	3,412
Purchase of improvements and equipment	89	(126)
Issuance of bridge loan	-	(350)
Release of escrow deposit	300	-
Net Cash Provided by Investing Activities	29,389	2,936
Financing Activities		
Contingent purchase price payments	-	(675)

Net proceeds from bridge loan	1,712	-
Repayment of long-term debt	(14,135)	(1,618)
Fees paid on early extinguishment of debt	(466)	(32)
Net proceeds from issuance of common stock	-	5,865
Payment of withholding taxes related to stock-based employee compensation	(2)	(151)
Net Cash (Used In) Provided by Financing Activities	(12,891)	3,389
Net Increase (Decrease) in Cash and Cash Equivalents	8,914	(3,474)
Cash and Cash Equivalents - Beginning of period	2,181	5,580
Cash and Cash Equivalents - End of period	$11,095	$2,106
Supplemental Disclosure of Cash Flows Information		
Cash paid during the period for:		
Interest	$362	$1,008
Non-cash investing and financing activities:		
2016 Accrued bonus awarded in equity	$-	$374
2015 Accrued bonus awarded in equity	-	-
Common stock issued for contingent purchase price payments	-	1,175

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

ALLIQUA BIOMEDICAL, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Description of Business and Basis of Presentation

Alliqua BioMedical, Inc. (the "Company") manufactures high water content, electron beam cross-linked, aqueous polymer hydrogels, or gels, used for wound care, medical diagnostics, transdermal drug delivery and cosmetics. The Company believes that it is one of the leading manufacturers of high-performance gels in the United States. The Company specializes in custom gels by capitalizing on proprietary manufacturing technologies. The Company has, historically, served as a contract manufacturer, supplying its gels to third parties who incorporate them into their own products.

Recent Developments

On October 11, 2018, the Company, Embark Merger Sub Inc., a Delaware corporation and a wholly-owned subsidiary of the Company ("Merger Sub"), and Adynxx, Inc., a privately-held Delaware corporation ("Adynxx"), entered into an Agreement and Plan of Merger and Reorganization (the "Merger Agreement"), pursuant to which, among other things, subject to the satisfaction or waiver of the conditions set forth in the Merger Agreement, Merger Sub will merge with and into Adynxx, with Adynxx becoming a wholly-owned subsidiary of the Company and the surviving corporation of the merger (the "Merger"). Subject to the terms and conditions of the Merger Agreement, at the effective time of the Merger (the "Effective Time"), (a) each outstanding share of Adynxx common stock, on an as-converted basis taking into consideration all outstanding common stock, preferred stock, restricted stock and all other securities convertible or exercisable for Adynxx common stock, will be converted into the right to receive the number of shares of the Company's common stock (the "Company Common Stock") equal to the exchange ratio described below; (b) each outstanding Adynxx stock option that has not previously been exercised prior to the Effective Time will be assumed by the Company; and (c) each outstanding warrant to acquire Adynxx capital stock that has not previously been exercised prior to the Effective Time will be assumed by the Company.

Under the exchange ratio formula in the Merger Agreement, as of immediately after the Merger, but excluding the effect of certain financings (as further described in the Merger Agreement), the former Adynxx securityholders are expected to own approximately 86% of the aggregate number of shares of the Company Common Stock issued and outstanding following the consummation of the Merger (the "Post-Closing Shares"), and the stockholders of the Company as of immediately prior to the Merger are expected to own approximately 14% of the aggregate number of Post-Closing Shares. This exchange ratio will be fixed immediately prior to the Effective Time to reflect the Company's and Adynxx's equity capitalization as of immediately prior to such time. In addition, to the extent Adynxx consummates a Permitted Financing, as specifically defined in the Merger Agreement, in excess of $10.0 million dollars prior to the Effective Time, the exchange ratio may be further adjusted in a manner that would reduce the

percentage of the aggregate number of Post-Closing Shares held by stockholders of the Company as of immediately prior to the Merger.

Immediately following the Merger, the name of the Company will be changed from “Alliqua BioMedical, Inc.” to “Adynxx, Inc.” At the Effective Time, the Merger Agreement contemplates that the Board of Directors of the Company will consist of such directors selected by Adynxx, with the Company having the right to designate one member. The executive officers of the Company immediately after the Effective Time will be designated by Adynxx; the merger will be a change of control and accounted for as a reverse business combination whereby Adynxx will be deemed the accounting acquiror.

The Merger Agreement contains customary representations, warranties and covenants made by the Company and Adynxx, including covenants relating to obtaining the requisite approvals of the stockholders of the Company and Adynxx, indemnification of directors and officers, and the Company’s and Adynxx’s conduct of their respective businesses between the date of signing the Merger Agreement and the closing of the Merger. Consummation of the Merger is subject to certain closing conditions, including, among other things, approval by the stockholders of the Company and Adynxx. The Merger Agreement contains certain termination rights for both the Company and Adynxx, and further provides that, upon termination of the Merger Agreement under specified circumstances, the Company or Adynxx, as applicable, may be required to pay the other party a termination fee of $0.249 million.

The Merger Agreement contemplates that the Company will also seek approval from its stockholders to effect a reverse stock split, if applicable, with the split ratio to be mutually agreed to by the Company and Adynxx within the range approved by the Company’s stockholders immediately prior to the Effective Time. In addition, the Merger Agreement requires the Company to use commercially reasonable efforts to consummate a spin-off of its hydrogel contract manufacturing business prior to the closing of the Merger.

The Company’s operations contemplated under the Merger Agreement are classified as Held for Use.

On May 7, 2018, the Company completed its previously announced Asset Sale Transaction (the "AST") with Celularity, Inc. ("Celularity"), pursuant to which the Company sold substantially all of its assets to Celularity, including certain assets comprising its MIST, Biovance and Interfyl Product Lines (the "Purchased Assets"). As consideration for the Purchased Assets, Celularity paid $29.0 million to the Company in cash. No debt or significant liabilities were assumed by Celularity in the AST. Under the terms of the Asset Purchase Agreement (the "APA"), the Company retained certain specified assets, including, among other things, cash, accounts receivable, and its hydrogel contract manufacturing business, including its SilverSeal and Hydress product lines. Approximately $14.8 million of the consideration received from Celularity was used to pay down in full all outstanding debt and related costs owed to Perceptive Credit Holdings LP ("Perceptive").

The transactions contemplated by the APA were approved by the affirmative vote of a majority of the voting power of issued and outstanding shares of the Company's common stock on April 27, 2018.

The Company's operations sold under the APA have been reclassified to discontinued operations in the second quarter of 2018, when the shareholders of the Company approved the sale. The AST was completed on May 7, 2018.

Basis of Presentation

The condensed consolidated financial statements contained in this report are unaudited. In the opinion of management, the condensed consolidated financial statements include all adjustments, which are of a normal recurring nature, necessary to present fairly the Company's financial position as of September 30, 2018 and results of operations and cash flows for the three and nine months ended September 30, 2018 and 2017. While management believes that the disclosures presented are adequate to make the information not misleading, these unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto in the Company's latest year-end financial statements, which are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017 (the "2017 Annual Report"). The results of the Company's operations for any interim period are not necessarily indicative of the results of operations for any other interim period or for the full year.

Principles of Consolidation

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

Reclassifications

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

Discontinued Operations

In addition to the aforementioned AST with Celularity, effective August 31, 2017 the Company entered into an Asset Purchase Agreement ("the Argentum Purchase Agreement") with Argentum Medical, LLC. ("Argentum") whereby the Company agreed to sell to Argentum all of the Company's rights, including (i) all distribution rights, exclusivity rights, intellectual property rights and marketing rights to the TheraBond product line and (ii) the unsold inventory of TheraBond products and work in process previously purchased by the Company in existence as of the closing, which occurred upon execution and delivery of the Argentum Purchase Agreement. In consideration for the sale of the TheraBond product line and the unsold TheraBond inventory to Argentum by the Company, Argentum agreed to pay (i) $3.6 million for the TheraBond product line and certain other agreements between the parties and (ii) up to $0.1 million for the unsold TheraBond inventory upon the Company's completion of its obligations to deliver all remaining and qualifying unsold TheraBond inventory, as specified in the Argentum Purchase Agreement. Of the $3.6 million of consideration, $0.3 million was initially deposited in an indemnity escrow account under standard terms and conditions. This amount was classified under current assets of discontinued operations on the Company's balance sheet as of December 31, 2017. As of September 30, 2018, the full $0.3 million escrow has been received.

Summarized operating results of discontinued operations for the three and nine months ended September 30, 2018 and 2017 are presented in the following table (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Revenue, net of returns, allowances and discounts	$-	$4,748	$6,681	$14,009
Cost of revenues	(1)	1,252	1,790	3,827
Gross profit	1	3,496	4,891	10,182
Selling, general and administrative	(203)	5,781	11,282	18,812
Other (income)/expense	-	(66)	-	(66)
Loss on extinguishment of debt	-	32	-	32
Interest expense	-	577	612	1,746
Warrant modification expense	-	-	-	803
Income/(loss) from discontinued operations, net of tax	204	(2,828)	(7,003)	(11,145)

Non-cash amortization expense of $0 and $1.1 million is included in selling, general and administrative expense for the three months ended September 30, 2018 and 2017, respectively. Non-cash amortization expense of $1.4 million and $3.5 million is included in selling, general and administrative expense for the nine months ended September 30, 2018 and 2017, respectively.

During the three and nine months ended September 30, 2018, the Company recorded a net gain of approximately $5.5 million (net of state income tax of $0.488 million) on the sale of the assets related to the purchase agreement with Celularity, as shown in the following table (in thousands):

Proceeds from sale		
Total Consideration		29,000
Less: Net book value of assets sold to Celularity		
Inventory, net	(1,578)	
Intangibles, net	(20,557)	
Goodwill	(1,659)	
Fixed Assets, net	(904)	
Other current assets	15	
Total net book value of assets		(24,683)
Add: Net book value of liabilities extinguished due to sale		
Milestone payment	1,000	
Other liabilities	717	

Total net book value of liabilities	1,717
Less: State tax expense	(488)
Net gain on sale of assets	$5,546

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

	September 30, 2018	December 31, 2017
Accounts receivable, net	$ 445	$ 3,161
Inventory, net	-	1,458
Prepaid expenses and other current assets	-	443
Total current assets	445	5,062
Fixed assets, net	-	1,041
Intangible assets, net	-	22,069
Goodwill, net	-	1,659
Total assets of discontinued operations	445	29,831
Accounts payable	2,322	957
Accrued expenses and other current liabilities	29	3,557
Senior secured term loan, net	-	10,929
Total current liabilities	$ 2,351	$ 15,443
Other long-term liabilities	-	245
Total liabilities of discontinued operations	$ 2,351	$ 15,688

Significant Accounting Policies and Estimates

The Company's significant accounting policies are disclosed in Note 2 — *Summary of Significant Accounting Policies* in the 2017 Annual Report. Since the date of the 2017 Annual Report, there have been no material changes to the Company's significant accounting policies. The preparation of the condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the condensed consolidated financial statements and accompanying notes. These estimates and assumptions include valuing equity securities and derivative financial instruments issued in financing transactions, allowance for doubtful accounts, inventory reserves, deferred taxes and related valuation allowances. Actual results could differ from the estimates.

Recent Accounting Principles

In August 2018, the FASB issued ASU 2018-13, "Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement". The amendments in this update is to improve the effectiveness of disclosures in the notes to the financial statements by facilitating clear communication of

the information required by GAAP that is most important to users of each entity's financial statements. The amendments in this Update apply to all entities that are required, under existing GAAP, to make disclosures about recurring or nonrecurring fair value measurements. The amendments in this update are effective for all entities for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. The Company does not expect that this guidance will have a material impact on its consolidated financial statements.

In July 2018, the FASB issued ASU 2018-11, "Leases (Topic 842): Target Improvements". The amendments in this Update also clarify which Topic (Topic 842 or Topic 606) applies for the combined component. Specifically, if the non-lease component or components associated with the lease component are the predominant component of the combined component, an entity should account for the combined component in accordance with Topic 606. Otherwise, the entity should account for the combined component as an operating lease in accordance with Topic 842. An entity that elects the lessor practical expedient also should provide certain disclosures. The Company is currently evaluating the adoption of this guidance and does not expect that this guidance will have a material impact on its consolidated financial statements. The Company has not adopted this Standard and will do so when specified by the FASB.

In July 2018, the FASB issued ASU 2018-10, “Codification Improvements to Topic 842, Leases”. The amendments in this Update affect narrow aspects of the guidance issued in the amendments in Update 2016-02 as described in the table below. The amendments in this Update related to transition do not include amendments from proposed Accounting Standards Update, Leases (Topic 842): Targeted Improvements, specific to a new and optional transition method to adopt the new lease requirements in Update 2016-02. That additional transition method will be issued as part of a forthcoming and separate Update that will result in additional amendments to transition paragraphs included in this Update to conform with the additional transition method. The Company is currently evaluating the adoption of this guidance and does not expect that this guidance will have a material impact on its consolidated financial statements. The Company has not adopted this Standard and will do so when specified by the FASB.

In June 2018, the FASB issued ASU 2018-07, “Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting”. The amendments in this update is to maintain or improve the usefulness of the information provided to the users of financial statements while reducing cost and complexity in financial reporting. The areas for simplification in this Update involve several aspects of the accounting for nonemployee share-based payment transactions resulting from expanding the scope of Topic 718, to include share-based payment transactions for acquiring goods and services from nonemployees. Some of the areas for simplification apply only to nonpublic entities. The amendments in this update are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Company does not expect that this guidance will have a material impact on its consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, “Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income”. The amendments in this Update allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. Consequently, the amendments eliminate the stranded tax effects resulting from the Tax Cuts and Jobs Act and will improve the usefulness of information reported to financial statement users. However, because the amendments only relate to the reclassification of the income tax effects of the Tax Cuts and Jobs Act, the underlying guidance that requires that the effect of a change in tax laws or rates be included in income from continuing operations is not affected. The amendments in this Update also require certain disclosures about stranded tax effects. The amendments in this update are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. The Company does not expect that this guidance will have a material impact on its consolidated financial statements.

2. Going Concern

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

The Company has experienced recurring losses since its inception. For the nine months ended September 30, 2018, the Company incurred a net loss of $7.1 million, utilized $7.6 million in cash from operations and had an accumulated deficit of $157.1 million. Prior to closing of the APA on May 7, 2018, these factors raised substantial doubt as to the Company's ability to continue as a going concern. However, upon closing the APA, the Company received gross proceeds of $29.0 million and part of the proceeds, $14.8 million, were utilized to satisfy its obligations under the Credit Agreement and Guaranty (the "CAG") with Perceptive. As of September 30, 2018, the Company had a cash balance of approximately $11.1 million.

Given the Company's current cash position and reduced cash burn, the Company believes substantial doubt has been mitigated and it has sufficient resources to support its planned operations for a year from the date these financial statements are issued.

3. Revenue Recognition

On January 1, 2018, the Company adopted Accounting Standards Codification ("ASC") Topic 606, "Revenue from Contracts with Customers" ("ASC 606"). The core principle of ASC 606 requires that an entity recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the Company expects to be entitled in exchange for those goods or services. ASC 606 defines a five-step process to achieve this core principle and, in doing so, it is possible more judgment and estimates may be required within the revenue recognition process than required under existing accounting principles generally accepted in the United States of America ("U.S. GAAP") including identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation.

The Company adopted ASC 606 for all applicable contracts using the modified retrospective method, which would have required a cumulative-effect adjustment, if any, as of the date of adoption. The adoption of ASC 606 did not have a material impact on the Company's condensed consolidated financial statements as of the date of adoption. As a result, a cumulative-effect adjustment was not required.

The Company recognizes revenue predominately from one type of revenue, contract manufacturing and recognizes an immaterial amount from the sale of products. Revenue from both contract manufacturing and products is recognized at the point where the customer obtains control of the goods and the Company satisfies its performance obligation, which generally is at the time it ships the product to the customer. To achieve this core principle, the Company applies the following five steps:

Step 1 – Identify the Contract with the Customer – A contract exists when (a) the parties to the contract have approved the contract and are committed to perform their respective obligations, (b) the entity can identify each party's rights regarding the goods or services to be transferred, (c) the entity can identify the payment terms for the goods or services to be transferred, (d) the contract has commercial substance and it is probable that the entity will collect substantially all of the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

Step 2 – Identify Performance Obligations in the Contract – Upon execution of a contract, the Company identifies as performance obligations each promise to transfer to the customer either (a) goods or services that are distinct or (b) a series of distinct goods or services that are substantially the same and have the same pattern of transfer to the customer. To the extent a contract includes multiple promised goods or services, the Company must apply judgement to determine whether the goods or services are capable of being distinct within the context of the contract. If these criteria are not met, the goods or services are accounted for as a combined performance obligation.

Step 3 – Determine the Transaction Price – The transaction price is determined based on the consideration to which the Company will be entitled in exchange for transferring products or services to the customer. Generally, all contracts include fixed consideration. If a contract did include variable consideration, the Company would determine the amount of variable consideration that should be included in the transaction price based on expected value method. Variable consideration would be included in the transaction price, if in the Company's judgement, it is probable that a significant future reversal of cumulative revenue under the contract would not occur.

Step 4 – Allocate the Transaction Price – After the transaction price has been determined, the next step is to allocate the transaction price to each performance obligation in the contract. If the contract only has one performance obligation, the entire transaction price will be applied to that obligation. If the contract has multiple performance obligations, the transaction price is allocated to the performance obligations based on the relative standalone selling price (SSP) at contract inception.

Step 5 – Satisfaction of the Performance Obligations (and Recognize Revenue) – When an asset is transferred, and the customer obtains control of the asset (or the services are rendered), the Company recognizes revenue. At contract inception, the Company determines if each performance obligation is satisfied at a point in time or over time. Revenue from both product sales and contract manufacturing is recognized at the point where the customer obtains control of

the goods and the Company satisfies its performance obligation, which generally is at the time it ships the product to the customer.

Disaggregation of Revenue

The Company recognizes revenue predominately from contract manufacturing and recognizes an immaterial amount from products. Revenue from both products and contract manufacturing is recognized at the point where the customer obtains control of the goods and the Company satisfies its performance obligation, which generally is at the time it ships the product to the customer.

As of September 30, 2018, or December 31, 2017, the Company did not have any contract assets or contract liabilities from contracts with customers. During the three and nine months ended September 30, 2018 and 2017, there was no revenue recognized from performance obligations satisfied (or partially satisfied) in previous periods. As of September 30, 2018, there were no remaining performance obligations that the Company had not satisfied.

4. Net Loss Per Common Share

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

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

	As of September 30,	
	2018	2017
Stock options	343,573	879,182
Warrants	399,621	514,561
Non-vested restricted stock	20,000	194,674
Total	763,194	1,588,417

5. Inventory

Inventory consists of the following (in thousands):

	September 30, 2018	December 31, 2017
Raw materials	$ 130	$ 98
Work in process	53	-
Finished goods	-	-
Less: Inventory reserve for excess and slow moving inventory	-	(5)
Total	$ 183	$ 93

6. Accrued Expenses and Other Current Liabilities

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

	September 30, 2018	December 31, 2017
Salaries, benefits and incentive compensation	$ 108	$ 509
Professional fees	123	176
Other	25	27
Total accrued expenses and other current liabilities	$ 256	$ 712

7. Debt

Senior Secured Term Loan Facility

On May 29, 2015, the Company entered into the CAG with Perceptive. The CAG provided a senior secured term loan in a single borrowing to the Company in the principal amount of $15.5 million.

On March 13, 2018, the Company, AquaMed Technologies, Inc., a wholly owned subsidiary of the Company, and Perceptive entered into an Amendment Agreement, pursuant to which the parties agreed to certain amendments and modifications to the terms of the CAG. The Amendment Agreement provided for, an additional bridge term loan to the Company in the aggregate principal amount of $2.0 million pursuant to a Bridge Loan Note ("BLN"). Under the Amendment Agreement, the Company agreed to pay an upfront fee of $0.25 million and all fees, costs and expenses payable pursuant to the CAG (including reasonable attorney's fees of Perceptive). The BLN bore interest at a rate per annum equal to the sum of (i) the greater of (x) LIBOR and (y) 1%, plus (ii) an applicable margin of 9.75%. The BLN matured on the earlier of (i) May 7, 2018 and (ii) the closing date in connection with the APA.

On May 7, 2018, the Company paid approximately $14.8 million in full satisfaction of all debt obligations due Perceptive.

8. Commitments and Contingencies

License Agreement with Noble Fiber Technologies, LLC

On July 15, 2011, the Company entered into a license agreement with Noble Fiber Technologies, LLC, whereby the Company has the exclusive right and license to manufacture and distribute “SilverSeal Hydrogel Wound Dressings” and “SilverSeal Hydrocolloid Wound Dressings”. The license is granted for ten years with an option to be extended for consecutive renewal periods of two years after the initial term. Royalties are to be paid equal to 9.75% of net sales of licensed products. Total royalties, for the three and nine months ended September 30, 2018 and 2017 were nominal.

Litigation, Claims and Assessments

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

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

On April 4, 2018, the court approved the parties’ stipulation and proposed order to withdraw the motion for preliminary injunction and dismiss the action and the case was closed. The court retained jurisdiction of the action solely for determining any potential fee application if the parties are unable to reach agreement and a fee application becomes necessary.

9.Stockholders' Equity

Stock-Based Compensation

On May 7, 2018, in connection with the closing of the sale under the APA of substantially all of the Company's assets to Cellularity, which triggered certain change in control provisions of the Company's equity plans, all unvested and outstanding options and restricted stock awards under the 2011 Plan and 2014 Plan became vested and exercisable.

A summary of the stock option activity for the nine months ended September 30, 2018 is presented below (in thousands, except years and per option data):

	Number of Options	Weighted Average Exercise Price per Option	Weighted Average Remaining Life in Years	Intrinsic Value
Outstanding, December 31, 2017	810	$ 52.90		
Granted	-	-		
Exercised	-	-		
Forfeited	(466)	34.68		
Outstanding, September 30, 2018	344	$ 46.54	4.8	$ -
Exerciseable, September 30, 2018	344	$ 46.54	4.8	$ -

As a result, a summary of the Company's outstanding and exercisable options as of September 30, 2018 was as follows (in thousands, except per share data):

	Options Outstanding		Options Exercisable		
Range of Exercise Price	Weighted Average Exercise Price	Outstanding Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Life in Years	Exercisable Number of Options
$2.00 - $4.00	$ 3.63	54	3.63	8.4	54
$4.10 - $9.90	8.72	23	8.72	7.6	23
$10.00 - $19.90	10.77	11	10.77	5.8	11
$20.00 - $39.90	33.47	40	33.47	4.6	40
$40.00 - $49.90	44.71	27	44.71	4.0	27
$50.00 - $59.90	53.87	26	53.87	1.5	26
$60.00 - $69.90	66.23	135	66.23	4.2	135
$70.00 - $79.90	79.40	1	79.40	5.6	1
$80.00 - $89.90	87.50	11	87.50	2.9	11
$90.00 - $99.90	90.00	11	90.00	3.0	11
$100.00 - $266.90	109.40	5	109.40	1.6	5
	46.54	344	46.54	4.8	344

For the three months ended September 30, 2018 and 2017, the Company recognized $0.023 million and $0.7 million of stock-based compensation expense, of which, $0.009 million and ($0.001) million is included in cost of revenues and $0.014 million and $0.7 million is included in selling, general and administrative expenses in the condensed consolidated statements of operations, respectively. For the nine months ended September 30, 2018 and 2017, the Company recognized $1.0 million and $1.6 million of stock-based compensation expense, of which, $0.030 million and $0.025 million is included in cost of revenues and $0.97 million and $1.6 million is included in selling, general and administrative expenses in the condensed consolidated statements of operations, respectively. As of September 30, 2018, there was no unrecognized stock-based compensation expense remaining.

Reverse Stock Split

The Company effected a 1-for-10 reverse stock split of its outstanding common stock on October 5, 2017. The accompanying consolidated financial statements and accompanying notes to the consolidated financial statements give retroactive effect to the reverse stock split for all periods presented. The shares of common stock retained a par value of $0.001 per share.

10. Related Party

In November 2015, the Company entered into a manufacturing supply agreement with a company where a Company director was then a member of the Board of Directors. During the three months ended September 30, 2018 and 2017, the Company incurred costs of approximately $0 and $0.028 million, respectively, from this vendor. During the nine months ended September 30, 2018 and 2017, the Company incurred costs of approximately $0.26 million and $0.3 million, respectively. Approximately $0 and $0.039 million is included in accounts payable related to this related party as of September 30, 2018 and December 31, 2017, respectively.

11. Fair Value Measurement

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

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

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

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

Warrant Liabilities

On September 30, 2018, the Company recomputed the fair value of its warrant liability of outstanding warrants to purchase an aggregate of 210,000 shares of common stock as $186,000 using the Binomial option pricing model (Level 3 inputs) using the following assumptions: expected volatility of 80.17% risk-free rate of 2.88%, expected term of 3.33 years, and expected dividends of 0.00%. The Company recorded a loss on the change in fair value of these warrant liabilities of $22,000 and $56,000 during the three and nine months ended September 30, 2018, respectively. During the three and nine months ended September 30, 2017, the Company recorded a gain on the change in fair value of its warrant liabilities of $35,000 and $403,000, respectively.

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

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

	Nine Months Ended September 30,	
	2018	2017
Warrant Liabilities		
Beginning balance as of January 1,	$ 130	$ 20
Change in fair value of warrant liability	56	(403)
Warrant modification expense	-	803
Ending balance as of September 30,	$ 186	$ 420

	Nine Months Ended September 30,	
	2018	2017
Contingent Consideration		
Beginning balance as of January 1,	$ -	$ 1,816
Payments of contingent consideration	-	(1,851)
Change in fair value of contingent consideration	-	35

Ending balance as of September 30,	$ -	$ -

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

	September 30, 2018		
	Level 1	Level 2	Level 3
Liabilities:			
Warrant liabilities	$-	$ -	$186
Total liabilities	$-	$ -	$186

	December 31, 2017		
	Level 1	Level 2	Level 3
Liabilities:			
Warrant liabilities	$-	$ -	$130
Total liabilities	$-	$ -	$130

12. Income Taxes

In accordance with ASC 740-270, *Income Taxes – Interim Reporting*, the Company is required at the end of each interim period to determine the best estimate of its annual effective tax rate and apply that rate to year-to-date ordinary income or loss. The resulting tax expense (or benefit) is adjusted for the tax effect of specific events, if any, required to be discretely recognized in the interim period as they occur. For the three months ended September 30, 2018 and 2017, the Company recorded a tax benefit of $0.026 million and immaterial tax expense, respectively. For the nine months ended September 30, 2018 and 2017, the Company recorded a tax expense of $0.488 million and immaterial tax expense, respectively. The gain on sale of assets to Celularity in the period ended June 30, 2018 resulted in current state tax expense, primarily due to limitations on the use of net operating loss carryforwards in certain state jurisdictions. The Company has not recorded net deferred tax assets as of September 30, 2018 or December 31, 2017 because it maintained a full valuation allowance against all material deferred tax assets, and management has determined that it is more likely than not that the Company will be unable to realize those future benefits. The Company's effective tax rate differs from the statutory rates of 21% and 34% as of September 30, 2018 and 2017, respectively, due to losses for which no future benefit is expected. As of September 30, 2018 and December 31, 2017, the Company had no uncertain tax positions recorded in its consolidated balance sheets.

The United States enacted the Tax Cuts and Jobs Act ("Act") on December 22, 2017, most provisions of which took effect in years beginning after December 31, 2017. The Act made substantial changes to U.S. taxation of corporations, including a reduction in the U.S. federal corporate income tax rate from 34% to 21% and changes to limitations on the deductibility of executive compensation. The effect on deferred tax assets and liabilities of a change in law or tax rates is recognized in income in the period that includes the enactment date.

After the enactment of the Act, the SEC issued Staff Accounting Bulletin No. 118 ("SAB 118") to address the application of U.S. GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Act. In our financial statements for the period ended December 31, 2017, we calculated an estimate of the impact of the Act related to the remeasurement of our net U.S. deferred tax asset due to the change in U.S. federal corporate income tax rate. The provisional amount recorded was deferred tax expense of $14.6 million, but which was fully and equally offset by a deferred tax benefit related to a corresponding reduction in our valuation allowance. In addition, due to changes in executive compensation rules pursuant to the Act, the Company determined that approximately $1.3 million of deferred tax asset for stock compensation may not be realizable. The Company had previously recorded a valuation allowance against the deferred tax asset so this adjustment had no impact on the financial statements for the period ended December 31, 2017. During the quarter ended September 30, 2018, the Company finalized its U.S. federal 2017 income tax return, which resulted in an immaterial change in the net deferred tax asset, before valuation allowance, as of the enactment date. The Company has not adjusted the provisional estimates recorded during period ended December 31, 2017 under SAB 118 and will complete the accounting for the income tax effects of the Act prior to the end of the one-year measurement period.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and related notes above.

Forward-Looking Statements

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

- the occurrence of any event, change or other circumstances that could give rise to the termination of the merger agreement with Adynxx, Inc.;
- our stockholders failing to approve the merger with Adynxx, Inc.;
- an increase in the amount of costs, fees, expenses and other charges related to the merger agreement with Adynxx, Inc.;
- risks arising from the diversion of management's attention from our ongoing business operations;
- risks associated with our ability to identify and realize business opportunities following the merger with Adynxx, Inc.;
- our ability to continue as a going concern;
- inadequate capital;

- the uncertainty regarding the adequacy of our liquidity to pursue our complete business objectives, including a return of capital to shareholders and execution of a definitive business restructure;

- our ability to comply with current good manufacturing practices ("cGMPs");

- loss or retirement of key executives;

- our plans to make significant additional outlays of working capital before we expect to generate significant revenues and the uncertainty regarding when we will begin to generate significant revenues, if we are able to do so;

- adverse economic conditions and/or intense competition;

- loss of a key customer or supplier;

- entry of new competitors;

- adverse federal, state and local government regulation;

- technological obsolescence of our manufacturing process and equipment;

- technical problems with our research and products;

- risks of mergers and acquisitions including the time and cost of implementing transactions and the potential failure to achieve expected gains, revenue growth or expense savings;

- price increases for supplies and components; and

- the inability to carry out our business plans.

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

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Overview

We manufacture a high-water content, electron beam cross-linked, aqueous polymer hydrogels, or gels, used for wound care, medical diagnostics, transdermal drug delivery and cosmetics. We believe that we are one of the leading manufacturers of high-performance gels in the United States. We specialize in custom gels by capitalizing on proprietary manufacturing technologies. We have historically served as a contract manufacturer, supplying our gels to third parties who incorporate them into their own products. Our contract manufacturing business provides custom hydrogels to the OEM market.

Recent Events

On October 11, 2018, the Company, Embark Merger Sub Inc., a Delaware corporation and a wholly-owned subsidiary of the Company ("Merger Sub"), and Adynxx, Inc., a privately-held Delaware corporation ("Adynxx"), entered into an Agreement and Plan of Merger and Reorganization (the "Merger Agreement"), pursuant to which, among other things, subject to the satisfaction or waiver of the conditions set forth in the Merger Agreement, Merger Sub will merge with and into Adynxx, with Adynxx becoming a wholly-owned subsidiary of the Company and the surviving corporation of the merger (the "Merger"). Subject to the terms and conditions of the Merger Agreement, at the effective time of the Merger (the "Effective Time"), (a) each outstanding share of Adynxx common stock, on an as-converted basis taking into consideration all outstanding common stock, preferred stock, restricted stock and all other securities convertible or exercisable for Adynxx common stock, will be converted into the right to receive the number of shares of Alliqua's common stock (the "Company Common Stock") equal to the exchange ratio described below; (b) each outstanding Adynxx stock option that has not previously been exercised prior to the Effective Time will be assumed by the Company; and (c) each outstanding warrant to acquire Adynxx capital stock that has not previously been exercised prior to the Effective Time will be assumed by the Company.

Under the exchange ratio formula in the Merger Agreement, as of immediately after the Merger, but excluding the effect of certain financings (as further described in the Merger Agreement), the former Adynxx securityholders are expected to own approximately 86% of the aggregate number of shares of the Company Common Stock issued and outstanding following the consummation of the Merger (the "Post-Closing Shares"), and the stockholders of the Company as of immediately prior to the Merger are expected to own approximately 14% of the aggregate number of Post-Closing Shares. This exchange ratio will be fixed immediately prior to the Effective Time to reflect the Company's and Adynxx's equity capitalization as of immediately prior to such time. In addition, to the extent Adynxx consummates a Permitted Financing, as specifically defined in the Merger Agreement, in excess of $10.0 million dollars prior to the Effective Time, the exchange ratio may be further adjusted in a manner that would reduce the percentage of the aggregate number of Post-Closing Shares held by stockholders of the Company as of immediately prior to the Merger.

Immediately following the Merger, the name of the Company will be changed from “Alliqua BioMedical, Inc.” to “Adynxx, Inc.” At the Effective Time, the Merger Agreement contemplates that the Board of Directors of the Company will consist of such directors selected by Adynxx, with Alliqua having the right to designate one member. The executive officers of the Company immediately after the Effective Time will be designated by Adynxx; the merger will be a change of control and accounted for as a reverse business combination whereby Adynxx will be deemed the accounting acquiror.

The Merger Agreement contains customary representations, warranties and covenants made by the Company and Adynxx, including covenants relating to obtaining the requisite approvals of the stockholders of the Company and Adynxx, indemnification of directors and officers, and the Company’s and Adynxx’s conduct of their respective businesses between the date of signing the Merger Agreement and the closing of the Merger. Consummation of the Merger is subject to certain closing conditions, including, among other things, approval by the stockholders of the Company and Adynxx. The Merger Agreement contains certain termination rights for both the Company and Adynxx, and further provides that, upon termination of the Merger Agreement under specified circumstances, the Company or Adynxx, as applicable, may be required to pay the other party a termination fee of $0.249 million.

The Merger Agreement contemplates that the Company will also seek approval from its stockholders to effect a reverse stock split, if applicable, with the split ratio to be mutually agreed to by the Company and Adynxx within the range approved by the Company’s stockholders immediately prior to the Effective Time. In addition, the Merger Agreement requires Alliqua to use commercially reasonable efforts to consummate a spin-off of its hydrogel contract manufacturing business prior to the closing of the Merger.

The Company’s operations contemplated under the Merger Agreement are classified as Held for Use.

Completion of the Asset Sale Transaction with Celularity

On May 7, 2018, we completed the previously announced sale of substantially all of our assets (the "AST") to Celularity, Inc. ("Celularity"), including certain assets comprising its MIST, Biovance and Interfyl product lines (the "Purchased Assets") pursuant to the terms of the Asset Purchase Agreement (the "APA"), dated January 5, 2018 with Celularity. As consideration for the Purchased Assets, Celularity paid a purchase price of $29.0 million in cash. No debt or significant liabilities were assumed by Celularity.

Under the terms of the APA, we retained certain specified assets, including, among other things, cash, accounts receivable and our hydrogel contract manufacturing business, including our SilverSeal and Hydress product lines.

In connection with the completion of the AST, we terminated our Credit Agreement and Guaranty (the "Credit Agreement"), dated as of May 29, 2015, as amended, by and among us, AquaMed Technologies, Inc., a wholly owned subsidiary of us ("Guarantor"), and Perceptive Credit Holdings LP ("Perceptive"). Additionally, we terminated the related Pledge and Security Agreement, dated as of May 29, 2015, by and among us, Guarantor and Perceptive. The Credit Agreement provided for a senior secured term loan in a single borrowing to us in the initial principal amount of approximately $15.5 million, of which approximately $12.0 million remained outstanding on the termination date. The full unpaid principal amount of the term loan and associated fees were paid off.

Liquidity and Capital Resources

The AST was completed on May 7, 2018. As consideration for the Purchased Assets, Celularity paid consideration to us of $29.0 million in cash. No debt or significant liabilities were assumed by Celularity in the AST. A portion of the proceeds, approximately $14.8 million, was used to extinguish our debt obligations and associated costs to Perceptive under the Credit Agreement. As of September 30, 2018, we had cash and cash equivalents totaling approximately $11.1 million compared to $2.2 million at December 31, 2017.

Net cash used in operating activities was $7.6 million and $9.8 million for the nine months ended September 30, 2018 and 2017, respectively.

Net cash provided in investing activities was $29.4 million and $2.9 million for the nine months ended September 30, 2018, and 2017, respectively. Cash provided by investing activities during the nine months ended September 30, 2018 was primarily due to the consideration received from Celularity in connection with the AST. Cash provided by

investing activities during the nine months ended September 30, 2017 included $3.4 million received from the sale of the rights to the TheraBond product from Argentum, offset by $0.35 million provided to Soluble Systems, LLC as a bridge loan and $0.126 million in purchases of improvements and equipment.

Net cash used in financing activities for the nine months ended September 30, 2018 consisted of $14.8 million in the payment of obligations owed to Perceptive under the Credit Agreement, offset by $1.7 million received from proceeds of a Bridge Loan Note. Net cash provided by financing activities for the nine months ended September 30, 2017 consisted of $5.9 million of net proceeds received from the issuance of our common stock offset by $0.7 million utilized to pay the cash portion of the contingent consideration related to the Celleration acquisition.

At September 30, 2018, current assets totaled $12.2 million and current liabilities totaled $3.1 million, as compared to current assets totaling $7.5 million and current liabilities totaling $17.0 million at December 31, 2017. As a result, we had working capital of $9.1 million at September 30, 2018 compared to working capital deficit of $9.5 million at December 31, 2017.

Given our current cash position and reduced cash burn, we believe substantial doubt has been mitigated and we have sufficient resources to support our planned operations for a year from the date these financial statements are issued.

Results of Operations

Three Months Ended September 30, 2018 Compared to the Three Months Ended September 30, 2017

Our MIST, Biovance and Interfyl product lines sold under the APA have been reclassified to discontinued operations.

Revenues, net. For the three months ended September 30, 2018 revenues decreased by $0.2 million, or 30%, to $0.3 million from $0.5 million for the three months ended September 30, 2017. The decrease in our overall revenue was due to a decrease in orders from contract manufacturing customers.

Gross profit. Our gross loss was $0.013 million for the three months ended September 30, 2018 compared to gross profit of $0.1 million for the three months ended September 30, 2017. The declined results for the three months ended September 30, 2018, as compared to the three months ended September 30, 2017 was primarily due to a decrease in the volume of orders fulfilled for our contract manufacturing customers, thus a lack of sales volume to adequately absorb all of the fixed overhead costs. Gross margin was approximately a negative 4% for the three months ended September 30, 2018. Gross margin was approximately 20% for the three months ended September 30, 2017.

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The components of cost of revenues are as follows for the three months ended September 30, 2018 and 2017 (in thousands):

	Three Months Ended September 30,	
	2018	2017
Cost of revenues		
Materials and finished products	$ 91	$ (40)
Stock-based compensation	10	(1)
Compensation and benefits	94	99
Depreciation and amortization	73	74
Equipment, production and other expenses	93	268
Total cost of revenues	$ 361	$ 400

Selling, general and administrative expenses. The following table highlights selling, general and administrative expenses by type for the three months ended September 30, 2018 and 2017 (in thousands):

	Three Months Ended September 30,	
	2018	2017
Selling, general and administrative expenses		
Compensation and benefits	$162	$492
Stock-based compensation	13	206
Depreciation and amortization	16	7
Other expenses and professional fees	554	817
Total selling, general and administrative expenses	$745	$1,522

Selling, general and administrative expenses decreased by $0.8 million to $0.7 million for the three months ended September 30, 2018, as compared to $1.5 million for the three months ended September 30, 2017. The decrease in selling, general and administrative expenses is attributable to our organizational restructuring post the completion of the AST and continued focus on managing operating expenditures.

Compensation and benefits decreased by $0.3 million to $0.2 million for the three months ended September 30, 2018, as compared to $0.5 million for the three months ended September 30, 2017. The decrease in compensation and benefits was primarily due to the decrease in the average number of full-time employees in 2018 compared to 2017, due to the completion of the AST.

Stock-based compensation decreased by $0.2 million, to $0.013 million for the three months ended September 30, 2018, as compared to $0.2 million for the three months ended September 30, 2017. The decrease in stock-based compensation is primarily due to the accelerated vesting of employee stock options and restricted stock awards resulting from the completion of the AST on May 7, 2018.

Other expenses and professional fees decreased by $0.2 million to $0.6 million for the three months ended September 30, 2018 from $0.8 million for the three months ended September 30, 2017. Other selling, general and administrative expenses consist of costs associated with our selling efforts and general management, including information technology, travel, training and recruiting. The decrease is due to lower legal and consulting fees.

Business development costs. During the three months ended September 30, 2018, we incurred $0.2 million in costs related to business development opportunities. These costs were mainly due to professional fees, including accounting, legal and consulting fees; in the past these were in other expenses and professional fees, however because they are not of a normal course of business, these have been carved out. During the three months ended September 30, 2017 we did not incur any business development costs.

Nine Months Ended September 30, 2018 Compared to the Nine Months Ended September 30, 2017

Our operations sold under the AST have been reclassified to discontinued operations.

Revenues, net. For the nine months ended September 30, 2018 revenues increased by $0.4 million, or 30%, to $1.8 million from $1.4 million for the nine months ended September 30, 2017. The increase in our overall revenue was due to an increase in orders fulfilled for our contract manufacturing customers.

Gross profit. Our gross profit was $0.4 million for the nine months ended September 30, 2018 compared to gross profit of $0.019 million for the nine months ended September 30, 2017. The improved results for the nine months ended September 30, 2018, as compared to the nine months ended September 30, 2017 was primarily due to the greater volume of contract manufacturing sales and a stricter emphasis on operating efficiency. Gross margin was approximately 22% for the nine months ended September 30, 2018. Gross margin was approximately 1% for the nine months ended September 30, 2017.

The components of cost of revenues are as follows for the nine months ended September 30, 2018 and 2017 (in thousands):

	Nine Months Ended September 30,	
	2018	2017
Cost of revenues		
Materials and finished products	$ 519	$ 277
Stock-based compensation	33	25
Compensation and benefits	299	384
Depreciation and amortization	217	217
Equipment, production and other expenses	303	432
Total cost of revenues	$ 1,371	$ 1,335

Selling, general and administrative expenses. The following table highlights selling, general and administrative expenses by type for the nine months ended September 30, 2018 and 2017 (in thousands):

	Nine Months Ended September 30,	
	2018	2017
Selling, general and administrative expenses		
Compensation and benefits	$1,039	$1,513
Stock-based compensation	288	86
Depreciation and amortization	36	19
Other expenses and professional fees	2,529	2,439
Total selling, general and administrative expenses	$3,892	$4,057

Selling, general and administrative expenses decreased by $0.2 million to $3.9 million for the nine months ended September 30, 2018, as compared to $4.1 million for the nine months ended September 30, 2017. The decrease in selling, general and administrative expenses is directly attributable to organizational restructure post the completion of the AST.

Compensation and benefits decreased by $0.5 million to $1.0 million for the nine months ended September 30, 2018, as compared to $1.5 million for the nine months ended September 30, 2017. The decrease in compensation and benefits was primarily due to the decrease in the average number of full-time employees in 2018 compared to 2017, due to the completion of the AST.

Stock-based compensation increased by $0.2 million, to $0.3 million for the nine months ended September 30, 2018, as compared to a $0.1 million to stock-based compensation for the nine months ended September 30, 2017. The increase in stock-based compensation is primarily due to the accelerated vesting of employee stock options and restricted stock awards resulting from the completion of the AST on May 7, 2018.

Other expenses and professional fees increased by $0.1 million to $2.5 million for the nine months ended September 30, 2018 from $2.4 million for the nine months ended September 30, 2017. Other selling, general and administrative expenses consist of costs associated with our selling efforts and general management, including information technology, travel, training and recruiting. The increase was due to higher legal expenses.

Business development costs. During the nine months ended September 30, 2018, we incurred $0.4 million in costs related to business development opportunities. These costs were mainly due to professional fees, including accounting, legal and consulting fees; in the past these were in other expenses and professional fees, however because they are not of a normal course of business, these have been carved out. During the nine months ended September 30, 2017 we incurred $0.6 million in costs related to business development opportunities.

Off Balance Sheet Arrangements

As of September 30, 2018, we had no off-balance sheet arrangements in the nature of guarantee contracts, retained or contingent interests in assets transferred to unconsolidated entities (or similar arrangements serving as credit, liquidity or market risk support to unconsolidated entities for any such assets), or obligations (including contingent obligations) arising out of variable interests in unconsolidated entities providing financing, liquidity, market risk or credit risk support to us, or that engage in leasing, hedging or research and development services with us.

Critical Accounting Policies

There have been no significant changes to our critical accounting policies and estimates from the information provided in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” included in the Annual Report on Form 10-K for the year ended December 31, 2017.

Recent Accounting Pronouncements

Recently issued accounting pronouncements are addressed in Note 1 in the Notes to Condensed Consolidated Financial Statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not required.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures.

As of September 30, 2018, we conducted an evaluation of the effectiveness of our "disclosure controls and procedures" ("Disclosure Controls"), as defined by Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The Disclosure Controls evaluation was done under the supervision and with the participation of management, including our chief executive officer and chief financial officer. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based upon this evaluation, our chief executive officer and chief financial officer have concluded that our Disclosure Controls and Procedures were effective at the reasonable assurance level as of September 30, 2018.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting during the fiscal quarter ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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

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

On April 4, 2018, the court approved the parties' stipulation and proposed order to withdraw the motion for preliminary injunction and dismiss the action and the case was closed. The court retained jurisdiction of the action solely for determining any potential fee application if the parties are unable to reach agreement and a fee application becomes necessary.

ITEM 1A. RISK FACTORS

During the three months ended September 30, 2018, there were no material changes to the risk factors previously discussed in Part I, Item 1A "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2017 and Form 10-Q for the quarter ended June 30, 2018, except that the risk factors related to the failure of the consummation of the AST are no longer applicable and as set forth below.

The issuance of shares of Company Common Stock to Adynxx stockholders in the merger will substantially dilute the voting power of current Company stockholders. Having a minority share position may reduce the influence that current stockholders have on the management of the Company.

Pursuant to the terms of the Merger Agreement, at the Effective Time of the merger, the former Adynxx security holders are expected to own approximately 86% of the aggregate number of Post-Closing Shares of the Company, and the stockholders of the Company as of immediately prior to the Merger are expected to own approximately 14% of the aggregate number of Post-Closing Shares of the Company, subject to certain adjustments as set forth in the Merger Agreement. Accordingly, the issuance of the shares of Company common stock to Adynxx equity holders in the Merger will significantly reduce the ownership stake and relative voting power of each share of Company common stock held by current Company stockholders. Consequently, following the merger, the ability of the Company's current stockholders to influence the management of the Company will be substantially reduced.

There is no assurance when or if the Merger will be completed. Any delay in completing the Merger may substantially reduce the benefits that the Company and Adynxx expect to obtain from the Merger.

Completion of the merger is subject to the satisfaction or waiver of a number of conditions as set forth in the Merger Agreement. There can be no assurance that the Company and Adynxx will be able to satisfy the closing conditions or that closing conditions beyond their control will be satisfied or waived. If the Merger and the integration of the companies' respective businesses are not completed within the expected timeframe, such delay may materially and adversely affect the synergies and other benefits that the Company and Adynxx expect to achieve as a result of the Merger and could result in additional transaction costs or other effects associated with uncertainty about the Merger.

The Company and Adynxx can agree at any time to terminate the Merger Agreement, even if Adynxx stockholders have already adopted the Merger Agreement and thereby approved the Merger and the other transactions contemplated by the Merger Agreement. The Company and Adynxx can also terminate the Merger Agreement under other specified circumstances.

The issuance of the Company's common stock in connection with the merger could decrease the market price of the Company's common stock.

In connection with the Merger and as part of the merger consideration, the Company expects to issue shares of its common stock to Adynxx equity holders. The anticipated issuance of the Company's common stock in the Merger may result in fluctuations in the market price of the Company common stock, including a stock price decrease.

Failure to complete the merger could negatively affect the value of the Company's common stock and the future business and financial results of the Company.

If the merger is not completed, the ongoing businesses of the Company could be adversely affected and the Company will be subject to a variety of risks associated with the failure to complete the mergers, including without limitation the following:

- diversion of management focus and resources from operational matters and other strategic opportunities while working to implement the merger;

- reputational harm due to the adverse perception of any failure to successfully complete the merger; and

- having to pay certain costs relating to the merger, such as legal, accounting, financial advisory, filing and printing fees.

If the Merger is not completed, these risks could materially affect the market price of the Company's common stock and the Company's business and financial results and may result in the cessation of the Company's operations.

Adynxx is a clinical development stage pharmaceutical company and has never been profitable. Adynxx expects to incur additional losses in the future and may never be profitable.

Adynxx is a clinical development stage pharmaceutical company. Adynxx has not commercialized any product candidates or recognized any revenues from product sales. All of Adynxx's product candidates are still in the preclinical or clinical development stage, and none has been approved for marketing or is being marketed or commercialized. Adynxx's product candidates will require significant additional development, clinical studies, regulatory clearances and additional investment before they can be commercialized. Adynxx cannot be certain when or if any of its product candidates will obtain the required regulatory approval.

Adynxx has never been profitable or generated positive cash flow from operation. Adynxx may incur significant additional losses as it continues to focus its resources on prioritizing, selecting and advancing its product candidates. Adynxx's ability to generate revenue and achieve profitability depends mainly upon its ability, alone or with others, to successfully develop its product candidates, obtain the required regulatory approvals in various territories and commercialize its product candidates. Adynxx may be unable to achieve any or all of these goals with regard to its product candidates. As a result, Adynxx may never be profitable or achieve significant and/or sustained revenues.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

(a) Unregistered Sales of Equity Securities

None

(b) Issuer Purchases of Equity Securities

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

ITEM 6. EXHIBITS

See “Index to Exhibits” for a description of our exhibits.

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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.

ALLIQUA BIOMEDICAL, INC.

Date: October 26, 2018 By: /s/ David Johnson
Name: David Johnson
Title: Chief Executive Officer
(Principal Executive Officer)

By: /s/ Joseph Warusz
Name: Joseph Warusz
Title: Chief Financial Officer
(Principal Financial Officer)

Index to Exhibits

Exhibit No.	Description
3.1	Certificate of Incorporation of Alliqua BioMedical, Inc. (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on June 11, 2014).
3.2	Bylaws of Alliqua BioMedical, Inc. (incorporated by reference to Exhibit 3.2 to the Current Report on Form 8-K filed on June 11, 2014).
3.3	Certificate of Amendment to Certificate of Incorporation of Alliqua BioMedical, Inc. (incorporated by reference to Exhibit 3.3 to the Current Report on Form 8-K filed on June 11, 2014).
3.4	Certificate of Amendment to Certificate of Incorporation of Alliqua BioMedical, Inc. (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on May 6, 2016).
3.5	Certificate of Amendment of Certificate of Incorporation of Alliqua BioMedical, Inc. dated October 5, 2017 (incorporated by reference in Exhibit 3.1 to the Current Report on Form 8-K filed on October 5, 2017).
31.1*	Certification of Chief Executive Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer Pursuant to Section 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer Pursuant to Section 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101*	The following materials from the Company's Quarterly Report on Form 10-Q for the fiscal quarter September 30, 2018, formatted in XBRL (eXtensible Business Reporting Language), (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations, (iii) Consolidated Statements of Stockholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to the Consolidated Financial Statements.

*Filed herewith.

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