

Neuralstem, Inc.
Form 10-Q
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)

Quarterly Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Quarterly Period Ended March 31, 2016

Or

Transition Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number 001-33672

NEURALSTEM, INC.

(Exact name of registrant as specified in its charter)

Delaware
State or other jurisdiction of
incorporation or organization

52-2007292
(I.R.S. Employer
Identification No.)

Neuralstem, Inc.

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PART I**FINANCIAL INFORMATION****ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****Neuralstem, Inc.****Unaudited Condensed Consolidated Balance Sheets**

	March 31, 2016	December 31, 2015
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$7,620,746	\$4,716,533
Short-term investments	-	7,517,453
Trade and other receivables	39,167	37,316
Prepaid expenses	1,077,762	1,159,782
Total current assets	8,737,675	13,431,084
Property and equipment, net	336,974	343,200
Patents, net	1,066,577	1,103,467
Other assets	57,692	71,797
Total assets	\$10,198,918	\$14,949,548
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY		
CURRENT LIABILITIES		
Accounts payable and accrued expenses	\$2,627,137	\$1,455,826
Accrued bonuses	287,046	161,362
Current portion of long term debt, net of fees and discount	4,466,081	4,634,742
Other current liabilities	241,008	173,542
Total current liabilities	7,621,272	6,425,472
Long term debt, net of fees, discount and current portion	2,546,296	3,391,808
Other long term liabilities	200,739	164,990
Total liabilities	10,368,307	9,982,270
STOCKHOLDERS' EQUITY (DEFICIT)		
Preferred stock, 7,000,000 shares authorized, zero shares issued and outstanding	-	-

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Common stock, \$0.01 par value; 300 million shares authorized, 92,044,042 and 92,005,705 shares outstanding in 2016 and 2015, respectively	920,440	920,057
Additional paid-in capital	177,473,335	176,002,832
Accumulated other comprehensive income	1,298	3,071
Accumulated deficit	(178,564,462)	(171,958,682)
Total stockholders' equity (deficit)	(169,389)	4,967,278
Total liabilities and stockholders' equity (deficit)	\$10,198,918	\$14,949,548

Neuralstem, Inc.**Unaudited Condensed Consolidated Statements of Operations and Comprehensive Loss**

	Three Months Ended March 31,	
	2016	2015
Revenues	\$ 2,500	\$ 2,917
Operating expenses:		
Research and development expenses	3,065,590	3,182,823
General and administrative expenses	3,170,522	1,433,074
Total operating expenses	6,236,112	4,615,897
Operating loss	(6,233,612)	(4,612,980)
Other income (expense):		
Interest income	11,136	13,569
Interest expense	(386,506)	(453,734)
Other income	3,199	-
Total other income (expense)	(372,171)	(440,165)
Net loss	\$ (6,605,783)	\$ (5,053,145)
Net loss per share - basic and diluted	\$ (0.07)	\$ (0.06)
Weighted average common shares outstanding - basic and diluted	92,009,782	89,654,634
Comprehensive loss:		
Net loss	\$ (6,605,783)	\$ (5,053,145)
Foreign currency translation adjustment	(1,773)	13
Comprehensive loss	\$ (6,607,556)	\$ (5,053,132)

Neuralstem, Inc.**Unaudited Condensed Consolidated Statements of Cash Flows**

	Three Months Ended March 31,	
	2016	2015
Cash flows from operating activities:		
Net loss	\$ (6,605,783)	\$ (5,053,145)
Adjustments to reconcile net loss to cash used in operating activities:		
Depreciation and amortization	85,467	83,773
Share based compensation expense	1,470,886	689,857
Amortization of deferred financing fees and debt discount	189,462	215,182
Changes in operating assets and liabilities:		
Trade and other receivables	(1,851)	217,351
Prepaid expenses	82,020	(71,207)
Other assets	14,029	(357)
Accounts payable and accrued expenses	1,170,334	(375,988)
Accrued bonuses	125,684	(421,639)
Other current liabilities	49,177	(3,648)
Other long term liabilities	(67,646)	-
Net cash used in operating activities	(3,488,221)	(4,719,821)
Cash flows from investing activities:		
Purchases of short-term investments	-	(15,032,419)
Maturity of short-term investments	7,517,453	15,007,478
Patent costs	(12,747)	(57,283)
Purchase of property and equipment	(14,598)	(16,052)
Net cash provided by (used in) investing activities	7,490,108	(98,276)
Cash flows from financing activities:		
Proceeds from issuance of common stock from warrants exercised, net	-	3,073,537
Proceeds from sale of common stock and warrants, net of issuance costs	-	2,931,925
Payment of fees for future financing	-	(42,758)
Payments of long-term debt	(1,096,951)	-
Payments of short term notes payable	-	(70,241)
Net cash provided by (used in) financing activities	(1,096,951)	5,892,463
Effects of exchange rates on cash	(723)	115
Net increase in cash and cash equivalents	2,904,213	1,074,481
Cash and cash equivalents, beginning of period	4,716,533	12,518,980

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Cash and cash equivalents, end of period	\$ 7,620,746	\$ 13,593,461
Supplemental disclosure of cash flows information:		
Cash paid for interest	\$ 205,827	\$ 238,552
Supplemental schedule of non cash investing and financing activities:		
Issuance of common stock for cashless exercise of warrants and options	\$ 38,337	\$ 201,720

NEURALSTEM, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

MARCH 31, 2016 AND 2015

Note 1. Basis of Presentation and Liquidity

In management's opinion, the accompanying condensed financial statements include all adjustments, consisting of normal recurring adjustments, which are necessary to present fairly our financial position, results of operations and cash flows. The condensed consolidated balance sheet at December 31, 2015, has been derived from audited financial statements as of that date. The interim results of operations are not necessarily indicative of the results that may occur for the full fiscal year. Certain information and footnote disclosure normally included in the financial statements prepared in accordance with generally accepted accounting principles in the United States of America (U.S. GAAP) have been condensed or omitted pursuant to instructions, rules and regulations prescribed by the U.S. Securities and Exchange Commission (SEC). We believe that the disclosures provided herein are adequate to make the information presented not misleading when these condensed financial statements are read in conjunction with the Financial Statements and Notes included in our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC, and as may be amended. Certain prior period amounts have been reclassified to conform to current year classifications. Specifically, depreciation and amortization expense is no longer shown as a separate line item; patent amortization is now included in research and development expense and fixed asset depreciation is allocated between research and development expense and general and administrative expense. Management feels that this reclassification better represents the expenses in their functional categories.

Neuralstem, Inc. is referred to as "Neuralstem," the "Company," "us," or "we" throughout this report. Our wholly-owned and controlled subsidiary located in China is consolidated in our condensed consolidated financial statements and all intercompany activity has been eliminated.

Our operations currently do not generate significant cash. Our management does not know when or if this will change. We have spent and will continue to spend substantial funds in the research, development, clinical and pre-clinical testing of our small molecule product candidates and to a lesser extent on our stem cell product candidates with the goal of ultimately obtaining approval from the United States Food and Drug Administration (the "FDA") and its international equivalents, to market and sell our products.

No assurance can be given that (i) approval will ever be granted for us to market and sell our product candidates, or (ii) that if approval is granted, that we will ever be able to sell our products or be profitable.

Liquidity

The Company has incurred losses since its inception and has not demonstrated an ability to generate revenues from sales or services and has not yet achieved profitable operations. There can be no assurance that profitable operations will ever be achieved, or if achieved, could be sustained on a continuing basis. In addition, development activities, clinical and pre-clinical testing, and commercialization of our products will require significant additional financing. These factors create substantial doubt about the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustment that might be necessary if the Company is unable to continue as a going concern.

Our cash, cash equivalents and short term investments balance at March 31, 2016 was approximately \$7.6M. Our ability to continue as a going concern is wholly dependent upon obtaining sufficient financing to fund our operations.

Our auditors' report on our December 31, 2015 financial statements expressed an opinion that our capital resources as of the date of their Audit Report were not sufficient to sustain operations or complete our planned activities for the upcoming year unless we raised additional funds. If we do not obtain additional funds by such time, we may no longer be able to continue as a going concern and will cease operation which means that our shareholders may lose their entire investment.

On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. The warrants allow the holder to purchase one share of common stock, have an exercise price of \$0.40 per share and a term of 5 years. This offering was made pursuant to our shelf registration statement that was declared effective by the SEC on June 19, 2014 (Registration No. 333-196567).

The public offering in May 2016 has provided us with sufficient funds to finance operations at least through December 31, 2016.

Note 2. Significant Accounting Policies and Recent Accounting Pronouncements

Use of Estimates

The preparation of financial statements in accordance with U.S. GAAP 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 revenues and expenses during the reporting period. The condensed financial statements include significant estimates for the expected economic life and value of our licensed technology, our net operating loss and related valuation allowance for tax purposes and our stock-based compensation related to employees and directors, consultants and investment banks, among other things. Because of the use of estimates inherent in the financial reporting process, actual results could differ significantly from those estimates.

Fair Value Measurements

The carrying amounts of our short-term financial instruments, which primarily include cash and cash equivalents, other short-term investments, accounts payable and accrued expenses, approximate their fair values due to their short maturities.

Foreign Currency Translation

The functional currency of our wholly owned foreign subsidiary is its local currency. Assets and liabilities of our foreign subsidiary are translated into United States dollars based on exchange rates at the end of the reporting period; income and expense items are translated at the weighted average exchange rates prevailing during the reporting period. Translation adjustments for subsidiaries that have not been sold, substantially liquidated or otherwise disposed of are accumulated in other comprehensive income or loss, a component of stockholders' equity. Transaction gains or losses are included in the determination of net loss.

Cash, Cash Equivalents, Short-Term Investments and Credit Risk

Cash equivalents consist of investments in low risk, highly liquid money market funds and certificates of deposit with original maturities of 90 days or less. Cash deposited with banks and other financial institutions may exceed the amount of insurance provided on such deposits. If the amount of a deposit at any time exceeds the federally insured amount at a bank, the uninsured portion of the deposit could be lost, in whole or in part, if the bank were to fail.

Short-term investments consist entirely of fixed income certificates of deposit ("CDs") with original maturities of greater than 90 days and not more than one year.

Financial instruments that potentially subject us to concentrations of credit risk consist primarily of cash equivalents and short-term investments. Our investment policy, approved by our Board of Directors, limits the amount we may invest in any one type of investment issuer, thereby reducing credit risk concentrations. In addition, our certificates of deposit are invested through the Certificate of Deposit Account Registry Service (“CDARS”) program which reduces or eliminates our risk related to concentrations of investments above FDIC insurance levels. We limit our credit and liquidity risks through our investment policy and through regular reviews of our portfolio against our policy. To date, we have not experienced any loss or lack of access to cash in our operating accounts or to our cash equivalents and short-term investments.

Research and Development

Research and development costs are expensed as they are incurred. Research and development expenses consist primarily of costs associated with the pre-clinical development and clinical trials of our product candidates.

Income (Loss) per Common Share

Basic income (loss) per common share is computed by dividing total net income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period.

For periods of net income when the effects are dilutive, diluted earnings per share is computed by dividing net income available to common shareholders by the weighted average number of shares outstanding and the dilutive impact of all dilutive potential common shares. Dilutive potential common shares consist primarily of stock options, restricted stock units and common stock purchase warrants. The dilutive impact of potential common shares resulting from common stock equivalents is determined by applying the treasury stock method. Our unvested restricted shares contain non-forfeitable rights to dividends, and therefore are considered to be participating securities; the calculation of basic and diluted income per share excludes net income attributable to the unvested restricted shares from the numerator and excludes the impact of the shares from the denominator.

For all periods of net loss, diluted loss per share is calculated similarly to basic loss per share because the impact of all dilutive potential common shares is anti-dilutive due to the net losses; accordingly, diluted loss per share is the same as basic loss per share for the three-month periods ended March 31, 2016 and 2015. A total of approximately 40.5 million and 39.1 million potential dilutive shares have been excluded in the calculation of diluted net income per share for the three-month periods ended March 31, 2016 and 2015, respectively, as their inclusion would be anti-dilutive.

Share-Based Compensation

We account for share-based compensation at fair value. Share-based compensation cost for stock options and warrants granted to employees and board members is generally determined at the grant date while awards granted to non-employee consultants are generally valued at the vesting date using an option pricing model that uses level 3 unobservable inputs; share-based compensation cost for restricted stock and restricted stock units is determined at the grant date based on the closing price of our common stock on that date. The value of the award that is ultimately expected to vest is recognized as expense on a straight-line basis over the requisite service period.

Intangible and Long-Lived Assets

We evaluate our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. We assess this recoverability by comparing the carrying amount of the asset to the estimated undiscounted future cash flows to be generated by the asset. If an asset is deemed to be impaired, we estimate the impairment loss by determining the excess of the asset's carrying amount over the estimated fair value. During the three months ended March 31 2016 and 2015, no significant impairment losses were recognized.

Income Taxes

We account for income taxes using the asset and liability approach, which requires the recognition of future tax benefits or liabilities on the temporary differences between the financial reporting and tax bases of our assets and liabilities. A valuation allowance is established when necessary to reduce deferred tax assets to the amounts expected to be realized. We also recognize a tax benefit from uncertain tax positions only if it is "more likely than not" that the position is sustainable based on its technical merits. Our policy is to recognize interest and penalties on uncertain tax positions as a component of income tax expense.

Significant New Accounting Pronouncements

In April 2015, the FASB issued *ASU 2015-03 – Interest-Imputation of Interest, Simplifying the Presentation of Debt Issuance Costs*. This Change in Accounting Principle requires that deferred debt issuance costs related to a recognized debt liability be presented in the balance sheet as a deduction of the carrying amount of the debt liability (similar to debt discounts). This change is effective for fiscal years beginning after December 15, 2015 and early adoption is permitted. This change has been applied retrospectively. This new pronouncement results in our reclassifying amounts previously reflected as current and long-term assets to a contra-liability, which reduces the carrying value of the associated debt instruments. To conform to this standard, \$89,562 was reclassified on our December 31, 2015 balance sheet from current assets to current portion of long term debt and \$9,154 was reclassified from non-current assets to long term debt.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements – Going Concern. This ASU requires entities to evaluate for each annual and interim reporting period, whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity’s ability to continue as a going concern within one year after the date that the financial statements are issued (or within one year after the date that the financial statements are available to be issued when applicable). The ASU will become effective for annual reporting periods after December 15, 2016. The Company is currently evaluating the impact of the adoption of this ASU on its consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, Leases. This ASU requires the recognition of lease assets and lease liabilities on the balance sheet and disclosure of key information about leasing arrangements. This ASU will become effective for annual periods beginning after December 15, 2018. The Company is currently evaluating the impact of the adoption of this ASU on its consolidated financial statements.

In March 2016, the FASB issued ASU 2016-09, Improvements to Employee Share Based Payment Accounting. This ASU address areas for simplification in several aspects of accounting for share-based payment including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The ASU will become effective for annual reporting periods after December 15, 2016. The Company is currently evaluating the impact of the adoption of this ASU on its consolidated financial statements.

The Company has reviewed other recent accounting pronouncements released during the quarter and concluded that they are either not applicable to the business, or that no material effect is expected on the consolidated financial statements as a result of future adoption.

Note 3. Fair Value Measurements

Fair value is the price that would be received from the sale of an asset or paid to transfer a liability assuming an orderly transaction in the most advantageous market at the measurement date. U.S. GAAP establishes a hierarchical disclosure framework which prioritizes and ranks the level of observability of inputs used in measuring fair value. These levels are:

- *Level 1* – inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.

Level 2 – inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques (e.g. the Black-Scholes model) for which all significant inputs are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, foreign exchange rates, and forward and spot prices for currencies and commodities.

Level 3 – inputs are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques, including option pricing models and discounted cash flow models. Our Level 3 non-derivative assets primarily comprise investments in certain corporate bonds and goodwill when it is recorded at fair value due to an impairment charge.

Note 4. Debt

In March 2013, we entered into a loan and security agreement for an initial \$8 million term loan with an additional \$2 million of borrowing capacity if certain conditions involving new partnerships were met. The loan is collateralized by substantially all of our assets, including our intellectual property.

The loan provided for interest at a variable rate based on prime with a floor of 11% and matured in June 2016. The variable rate was 11% and did not change during the period through the loan amendment. The loan provided for interest only payments through December 2013 at which time monthly principal and interest payments of approximately \$300,000 were due through maturity. The loan resulted in net proceeds of approximately \$7,551,000 after origination and other cash fees and expenses related to the closing of the loan.

In conjunction with the loan agreement, we issued the lender a five-year common stock purchase warrant to purchase 648,809 shares of common stock at an exercise price of \$1.0789 per share. This warrant contained non-standard anti-dilution protection and, consequently, was being accounted for as a derivative instrument, recorded at fair market value each period (see Note 3). The allocation of proceeds to this warrant resulted in a debt discount which was amortized as interest expense over the term of the debt using the effective interest method. The warrant was exercised in the first quarter of 2014.

We also incurred expenses with various third parties in connection with the debt issuance, consisting of approximately \$449,000 in cash, 350,650 shares of common stock valued at approximately \$396,000, and a five-year common stock purchase warrant to purchase 648,798 shares at an exercise price of \$1.07892 per share. The warrant is classified as equity. Fees related to the debt offering are recorded as deferred financing fees and are being amortized as interest expense over the term of the debt using the effective interest method.

The loan agreement provided for a conversion feature whereby the lender or the Company could each convert up to a maximum of \$1 million in principal payments into common stock of the Company. In 2014, the lender elected to convert the maximum principal payments of \$1 million into 805,972 shares of our common stock in accordance with the terms of the loan and security agreement.

In October 2014, we entered into an agreement with the existing lender to refinance and amend the terms of our loan and security agreement. The amended loan provided for refinancing of approximately \$5.6 million of outstanding balance of the initial loan along with approximately \$4.4 million of new principal for a total of \$10 million in principal. The amended loan provides for a variable interest rate based on prime with a floor of 10% and matures in April 2017. The loan provides for interest only payments through September 2015; payments of principal and interest of approximately \$461,000 from October 2015 through December 2016, and principal and interest of approximately \$435,000 from January, 2016 through March 2017 and a final balloon payment of approximately \$2.8 million in April 2017. The loan amendment generated approximately \$4.3 million in net proceeds after fees and expenses. The loan amendment is accounted for as a debt extinguishment in accordance with guidance provided for in ASC 470, Debt resulting in a loss on extinguishment of approximately \$446,000. In conjunction with the loan amendment we recorded a debt discount relating to the beneficial conversion feature. Such discount is being amortized as interest expense over the term of the debt using the effective interest method.

In conjunction with the loan amendment, we issued the lender a five-year common stock purchase warrant to purchase 75,188 shares of common stock at an exercise price of \$2.66 per share. The warrant contains standard anti-dilution protection but does not contain any anti-dilution price protection for subsequent offerings. The value of the warrant was accounted for in calculating the loss on extinguishment.

We also incurred expenses with various third parties in connection with the loan amendment, consisting of approximately \$86,000 in cash, 28,119 shares of common stock valued at approximately \$80,000, and a three-year common stock purchase warrant to purchase 58,141 shares at an exercise price of \$2.66 per share. The warrant is classified as equity and has terms substantially similar to the lender warrant. These fees related to the loan amendment are recorded as deferred financing fees and are being amortized as interest expense over the term of the debt using the effective interest method.

At March 31, 2016, remaining principal payments due under this loan are approximately \$3,470,000 and \$3,766,000 payable in, 2016 and 2017, respectively.

Note 5. Stockholders' Equity

We have granted share-based compensation awards to employees, board members and service providers. Awards may consist of common stock, restricted common stock, restricted common stock units, warrants, or stock options. Our stock options and warrants have lives of up to ten years from the grant date. The stock options and warrants vest either upon the grant date or over varying periods of time. The stock options we grant provide for option exercise prices equal to or greater than the fair market value of the common stock at the date of the grant. Restricted stock units grant the holder the right to receive fully paid common shares with various restrictions on the holder's ability to transfer the shares. Vesting of the restricted stock units is similar to that of stock options. As of March 31, 2016, we have approximately 45.4 million shares of common stock reserved for issuance upon the exercise of such awards.

Share-based compensation expense included in the statements of operations for the three months ended March 31, 2016 and 2015 was as follows:

	Three Months Ended March 31,	
	2016	2015
Research and development expenses	\$709,416	\$278,180
General and administrative expenses	761,470	411,677
Total	\$1,470,886	\$689,857

Included in the general and administrative expense for the three months ended March 31, 2016 is approximately \$407,000 related to the acceleration of the vesting of options for the previous CEO who left during the quarter.

No income tax benefit was recognized in the consolidated statements of operations for stock-based compensation for the years presented due to the Company's net loss position.

Stock Options A summary of stock option activity during the three months ended March 31, 2016 and related information is included in the table below:

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	Number of Options	Weighted-Average Exercise Price	Weighted-Average Contractual Life (in years)	Aggregate Intrinsic Value
Outstanding at January 1, 2016	17,102,947	\$ 2.08	5.0	\$ 550,000
Granted	3,712,898	\$ 0.77	-	
Exercised	-			\$ 0
Forfeited	(102,010)	\$ 1.63		
Outstanding at March 31, 2016	20,713,835	\$ 1.85	5.7	\$ 165,000
Exercisable at March 31, 2016	14,998,577	\$ 2.16	4.5	\$ 0
Vested and expected to vest	20,428,072	\$ 1.86	5.7	\$ 156,750

Range of Exercise Prices	Outstanding		Weighted-Average Contractual Life (in years)	Aggregate Intrinsic Value
	Number of Options	Weighted-Average Exercise Price		
\$0.50 - \$1.00	7,829,776	\$ 0.84	7.6	165,000
\$1.01 - \$2.00	5,057,096	\$ 1.17	6.6	-
\$2.01 - \$3.00	2,122,669	\$ 2.50	3.5	-
\$3.01 - \$5.00	5,704,294	\$ 3.60	3.1	-
	20,713,835	\$ 1.85	5.7	\$ 165,000

The Company uses the Black-Scholes option pricing model for “plain vanilla” options and other pricing models as appropriate to calculate the fair value of options. Significant assumptions used in these models include:

	Three months ended March 31,	
	2016	2015
Annual dividend	-	-
Expected life (in years)	6.0-7.0	6.0
Risk free interest rate	1.35%-1.75%	1.70%-1.78%
Expected volatility	69.0%-80.2%	69.3%-69.4%

The options granted in the three months ended March 31, 2016 and 2015 had a weighted average grant date fair value of \$0.77 and \$2.38, respectively.

Unrecognized compensation cost for unvested stock option awards outstanding at March 31, 2016 was approximately \$4,620,000 to be recognized over approximately 2.0 years.

RSUs We have granted restricted stock units (RSUs) to certain employees that entitle the holders to receive shares of our common stock upon vesting and subject to certain restrictions regarding the exercise of the RSUs. The fair value of RSUs granted is based upon the market price of the underlying common stock as if they were vested and issued on the date of grant.

A summary of our restricted stock unit activity for the three months ended March 31, 2016 is as follows:

	Number of RSU's	Weighted- Average Grant Date Fair Value
Outstanding at January 1, 2016	150,906	\$ 2.13
Granted	-	\$ -
Vested and converted to common shares	(38,337)	\$ 2.02
Forfeited	(6,465)	\$ 2.02
Outstanding at March 31, 2016	106,104	\$ 2.17
Exercisable at March 31, 2016	106,104	\$ 2.17

Unrecognized compensation cost for unvested RSUs outstanding at March 31, 2016 was approximately \$0.

Stock Purchase Warrants. In the past, we have issued Warrants to purchase common stock to certain officers, directors, stockholders and service providers as well as in conjunction with debt and equity offerings and at various times replacement warrants were issued as an inducement for warrant exercises.

A summary of warrant activity for the three months ended March 31, 2016 follows:

	Number of Warrants	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Outstanding at January 1, 2016	19,652,096	\$ 2.34	3.1	\$ 309,724
Granted	-			
Exercised	-		-	
Forfeited	-		-	
Outstanding at March 31, 2016	19,652,096	\$ 2.34	2.9	\$ 117,189
Exercisable at March 31, 2016	19,614,596	\$ 2.34	2.9	\$ 117,189

There were no stock purchase warrants granted in the three months ended March 31, 2016.

Restricted Stock

We have granted restricted stock to certain board members based on revised board of director year and compensation policy.

A summary of our restricted stock activity for the year ended March 31, 2016 is as follows:

	Number of Restricted Stock Shares	Weighted-Average Grant Date Fair Value
Outstanding at January 1, 2016	213,904	\$ 1.87
Granted	-	
Vested	(106,952)	\$ 1.87
Forfeited	-	
Outstanding at March 31, 2016	106,952	\$ 1.87

The total intrinsic value of the outstanding units at March 31, 2016 was approximately \$80,000.

Common Stock

During the three months ended March 31, 2015, we issued 812,423 shares of common stock as a result of sales under our At the Market Offering Agreement. The shares were sold at an average price of \$3.77 per share and we received approximately \$2,932,000 in net proceeds.

During the three months ended March 31, 2015, we issued 1,705,400 shares of common stock upon the exercise of outstanding common stock purchase warrants. The warrants were exercised at an average exercise price of \$1.94. We received approximately \$3,074,000 of net proceeds from the exercises.

During the three months ended March 31, 2015, we issued 29,141 shares of our common stock upon the cashless exercise of 89,000 outstanding common stock purchase warrants and stock options. The warrants and options were exercised at an average price of \$2.27. We received no proceeds from the exercises.

During the three months ended March 31, 2016, no warrants were exercised.

During the three months ended March 31, 2016, we issued 38,337 shares of our common stock upon the cashless conversion of 44,802 outstanding restricted stock units. The restricted stock units were converted at an average price of 2.02. We received no proceeds from the conversions.

On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. The warrants allow the holder to purchase one share of common stock, have an exercise price of \$0.40 per share and a term of 5 years. This offering was made pursuant to our shelf registration statement that was declared effective by the SEC on June 19, 2014 (Registration No. 333-196567).

Note 6. Commitments and Contingencies

We currently operate two facilities located in the United States and one facility located in China. Our corporate offices and primary research facilities are located in Germantown, Maryland, where we license approximately 3,100 square feet. This license provides for monthly payments of approximately \$10,200 per month with the term expiring on December 31, 2016.

In 2015, we entered into a lease consisting of approximately 3,100 square feet of research space in San Diego, California. This lease provides for current monthly payments of approximately \$11,000 and expires on August 31, 2018.

We also lease a research facility in People's Republic of China. This lease expires on September 30, 2018 with lease payments of approximately \$3,200 per month.

From time to time, we are parties to legal proceedings that we believe to be ordinary, routine litigation incidental to the business of present or former operations. We are currently not a party to any litigation or legal proceeding.

The Company is currently obligated under three written employment agreements and a general release agreement. The employment agreements are with our: (i) Chief Executive Officer, (ii) Chief Scientific Officer (“CSO”) and (iii) Chief Financial Officer (“CFO”): Pursuant to the terms of the agreements, our CEO, CSO and CFO receive annual salaries of \$440,000, \$750,000 and \$315,000, respectively. The agreements also provide for the payment of severance in the event one of the executives is terminated and in certain circumstances, the agreements also provide for the acceleration of vesting with regard to options.

On March 1, 2016, we entered into a general release and waiver of claims with I. Richard Garr in connection with his resignation as our chief executive officer. Pursuant to the release, timing of the required severance payment to Mr. Garr was amended as consideration for Mr. Garr’s voluntary resignation and release. Pursuant to the release, Mr. Garr will: (i) continue to receive his monthly salary of \$36,667 until March 1, 2017, (ii) receive a lump of \$177,000 to be paid on June 1, 2016, January 1, 2017 and March 1, 2017, (iii) receive healthcare benefits until January 1, 2017, and (iv) be entitled to the immediate vesting of any previously outstanding but unvested equity awards.

Note 7. Subsequent Events

On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. The warrants allow the holder to purchase one share of common stock, have an exercise price of \$0.40 per share and a term of 5 years. This offering was made pursuant to our shelf registration statement that was declared effective by the SEC on June 19, 2014 (Registration No. 333-196567).

On April 20, 2016, we received a written notice from the Nasdaq Stock Market LLC that we are not in compliance with Nasdaq Listing Rule 5550(a)(2), as the minimum bid price of our common stock has been below \$1.00 per share for 30 consecutive business days. In accordance with Nasdaq Listing Rule 5810(c)(3)(A), we have a period of 180 calendar days, or until October 17, 2016, to regain compliance with the minimum bid price requirement. To regain compliance, the closing bid price of our common stock must meet or exceed \$1.00 per share for at least ten consecutive business days during this 180 calendar day period. In the event we do not regain compliance by October 17, 2016, we may be eligible for an additional 180 calendar day grace period if we meet the initial listing standards, with the exception of bid price, for the Nasdaq Capital Market, and provide written notice to Nasdaq of our intention to cure the deficiency during the second compliance period, by effecting a reverse stock split, if necessary. If we do not regain compliance within the allotted compliance period(s), including any extensions that may be granted by Nasdaq, Nasdaq will provide notice that our common stock will be subject to delisting. We will then be entitled to appeal the determination to a Nasdaq Listing Qualifications Panel and request a hearing. We cannot be sure that our share price will comply with the requirements for continued listing of our shares on the Nasdaq Capital Market in the future or that we will comply with the other continued listing requirements. If our shares lose their status on the Nasdaq Capital Market, we believe that our shares would likely be eligible to be quoted on the inter-dealer electronic quotation and trading system operated by Pink OTC Markets Inc., commonly referred to as the Pink Sheets and now

known as the OTCQB market. These markets are generally considered not to be as efficient as, and not as broad as, the Nasdaq Capital Market. If our common stock is delisted, this would, among other things, substantially impair our ability to raise additional funds and could result in a loss of institutional investor interest and fewer development opportunities for us.

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

Statements in this Quarterly Report that are not strictly historical are forward-looking statements and include statements about products in development, results and analyses of pre-clinical studies, clinical trials and studies, research and development expenses, cash expenditures, and alliances and partnerships, among other matters. You can identify these forward-looking statements because they involve our expectations, intentions, beliefs, plans, projections, anticipations, or other characterizations of future events or circumstances. These forward-looking statements are not guarantees of future performance and are subject to risks and uncertainties that may cause actual results to differ materially from those in the forward-looking statements as a result of any number of factors. These factors include, but are not limited to, risks relating to our ability to conduct and obtain successful results from ongoing clinical trials, commercialize our technology, obtain regulatory approval for our product candidates, contract with third parties to adequately test and manufacture our proposed therapeutic products, protect our intellectual property rights and obtain additional financing to continue our development efforts. Some of these factors are more fully discussed, as are other factors, in our Annual Report on Form 10-K for the fiscal year ended December 31, 2015, filed with the SEC, as well as in the section of this Quarterly Report entitled "Risk Factors" and elsewhere herein. We do not undertake to update any of these forward-looking statements or to announce the results of any revisions to these forward-looking statements except as required by law.

We urge you to read this entire Quarterly Report on Form 10-Q, including the “Risk Factors” section, the financial statements, and related notes. As used in this Quarterly Report, unless the context otherwise requires, the words “we,” “us,” “our,” “the Company,” “Neuralstem” and “Registrant” refers to Neuralstem, Inc. and its subsidiaries. Also, any reference “common shares,” “common stock,” or “shares” refers to our \$.01 par value common stock. The information contained herein is current as of the date of this Quarterly Report (March 31, 2016), unless another date is specified. We prepare our interim financial statements in accordance with U.S. GAAP. Our financials and results of operations for the three-month period ended March 31, 2016 are not necessarily indicative of our prospective financial condition and results of operations for the pending full fiscal year ending December 31, 2016. The interim financial statements presented in this Quarterly Report as well as other information relating to our company contained in this Quarterly Report should be read in conjunction and together with the reports, statements and information filed by us with the United States Securities and Exchange Commission or SEC.

Our Management’s Discussion and Analysis of Financial Condition and Results of Operations or MD&A, is provided in addition to the accompanying financial statements and notes to assist readers in understanding our results of operations, financial condition and cash flows. Our MD&A is organized as follows:

Executive Overview — Discussion of our business and overall analysis of financial and other highlights affecting the Company in order to provide context for the remainder of MD&A.

Trends & Outlook — Discussion of what we view as the overall trends affecting our business and overall strategy.

Critical Accounting Policies— Accounting policies that we believe are important to understanding the assumptions and judgments incorporated in our reported financial results and forecasts.

Results of Operations— Analysis of our financial results comparing the three-month periods ended March 31, 2016 to the comparable period of 2015.

Liquidity and Capital Resources— An analysis of cash flows and discussion of our financial condition and future liquidity needs.

Executive Overview

We are focused on the research, development and commercialization of central nervous system therapies based on our proprietary human neuronal stem cells and our stem-cell derived small molecule compounds. We are headquartered in Germantown, Maryland and have a wholly-owned subsidiary in China, Suzhou Neuralstem Biopharmaceutical Co. Ltd., or Neuralstem China.

Our technology base has produced three primary assets: Our NSI-189 small molecule program, our NSI-566 stem cell therapy program and our novel and proprietary new chemical entity screening platform.

Our patented technology enables the commercial-scale production of multiple types of central nervous system stem cells, which are under development for the potential treatment of central nervous system diseases and conditions. In addition, this ability to generate human neural stem cell lines provides a platform for chemical screening and discovery of novel compounds that we believe may stimulate the brain's capacity to generate neurons, potentially reversing pathologies associated with certain central nervous system (CNS) conditions. This proprietary screening platform led to our discovery of NSI-189.

We have developed and maintain what we believe is a strong portfolio of patents and patent applications that form the proprietary base for our research and development efforts. We own or exclusively license over 110 U.S. and foreign issued patents and over 40 U.S. and foreign patent applications in the field of regenerative medicine, related to our stem cell technologies as well as our small molecule compounds.

We believe our technology base, in combination with our expertise, and collaborative projects with major research institutions, could facilitate the development and commercialization of products for use in the treatment of a wide array of central nervous system disorders including neurodegenerative conditions and regenerative repair of acute disease.

There can be no assurances that we will ultimately produce any viable products or processes or that our screen platform will lead to the discovery of any additional product candidates. Even if we are able to produce a commercially viable product, there are strong competitors in this field and our products may not be able to successfully compete against them.

All of our research efforts to date are at the pre-clinical or clinical stage of development. We are focused on leveraging our key assets, including our intellectual property, proprietary technology, scientific team and facilities, to advance our technologies and clinical programs. In addition, we are pursuing strategic collaborations with members of academia and industry to further advance and discover additional product candidates.

Recent Developments

Business Highlights

In January 2016, we announced an initiative to pursue collaborations for our stem cell therapy programs in order to utilize additional expertise, expedite clinical and regulatory pathways and secure alternative funding.

In February 2016, we strengthened our management team with the appointment of Richard Daly as our President and Chief Executive Officer.

In May 2016, we completed a public offering of our securities which resulted in gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000.

Clinical Highlights

In March 2016, we commenced our NSI-189 Phase 2 clinical trial for the treatment of Major Depressive Disorder (MDD).

Small Molecule Pharmaceutical Compounds Clinical Development

Lead asset, NSI-189 Phase 2 clinical trial for the treatment of MDD.

In March 2016, we commenced our NSI-189 Phase 2 clinical trial for the treatment of MDD. The double-blind, randomized, placebo-controlled, 220 subject study is expected to enroll the first subject in the second quarter of 2016.

Stem Cells

Cell Therapy Platform Clinical Development

In January 2016, Dr. Karl Johe, Founder and Chief Scientific Officer, presented at the Facilitate Cell & Gene Therapy World Conference. He concluded that the collective trial data analysis showed the cells consistently demonstrated biological activity in all three program indications: Amyotrophic Lateral Sclerosis or ALS, chronic spinal cord injury (cSCI), and motor deficits due to ischemic stroke.

NSI-566 Phase 1 safety trial for the treatment of cSCI

In January 2016, we reported preliminary six-month follow-up Phase 1 safety data on all four subjects. The stem cell treatment demonstrated feasibility and safety. A self-reported ability to contract some muscles below the level of injury was confirmed via clinical and electrophysiological follow-up examinations in one of the four patients treated. This study was completed with the collaboration of the UCSD School of Medicine, supported by the UCSD Sanford Stem Cell Clinical Center.

NSI-566 Phase 1 and 2 safety trials for the treatment of ALS

In September 2015, nine-month Phase 2 and combined Phase 1 and Phase 2 data on the NSI-566 trial in ALS were presented at the American Neurological Association Annual Meeting by the principal investigator, Eva Feldman, MD, PhD, Director of the A. Alfred Taubman Medical Research Institute and Director of Research of the ALS Clinic at the University of Michigan Health. The data showed that the intraspinal transplantation of the cells was safe and well tolerated. In January 2016, we announced that we are in discussions with various governmental, State and non-profit organizations regarding funding grants for the next trial; the initiation of the trial will be dependent upon significant funding from such sources.

NSI-566 Phase 1 safety trial for the treatment of motor deficits in stroke

We completed dosing the third planned cohort in a Phase 1 clinical trial at BaYi Brain Hospital in Beijing. The trial is being conducted by Neuralstem China, at BaYi Brain Hospital in Beijing, China.

Financial Condition

Our Cash and Cash Equivalent balances of approximately \$7.6 million as of March 31, 2016 are only sufficient to fund operations through June 2016. We will require additional capital to continue to develop our pre-clinical and clinical development operations. We cannot assure you that we will be able to secure additional financing or that the expected income will materialize. Several factors will affect our ability to raise additional funding, including, but not limited to market conditions, interest rates and, more specifically, our progress in our exploratory, preclinical and future clinical development programs.

On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. The warrants allow the holder to purchase one share of common stock, have an exercise price of \$0.40 per share and a term of 5 years. This offering was made pursuant to our shelf registration statement that was declared effective by the SEC on June 19, 2014 (Registration No. 333-196567).

The public offering in May 2016 has provided us with sufficient funds to finance operations at least through December 31, 2016.

Pre-Clinical and Clinical Programs and Development

In January 2016, we announced a strategic refocusing to concentrate our resources on the NSI-189 small molecule program. As part of this refocusing, we announced that we will seek external funding to defray all, or substantially all, of the costs associated with the NSI-566 stem cell therapy program. We cannot say when, if ever, we will be able to achieve this goal.

We have devoted substantially all our efforts to the pre-clinical and clinical development of our small molecule compounds and our stem cell therapeutics. Below is a description of our most advanced clinical programs, their intended indication, current stage of development and our expected future development plans:

Status*

- (1) Phase 2 MDD clinical trial results are expected to be provided during 2H17
- (2) Second Indication to be determined in 2Q16 at which time we will provide an update.
- (3) Ongoing preclinical studies in NSI-189 and other undisclosed compounds. Multiple NSI-189 proof of principal studies and publications to be submitted in 2016.
- (4) Active efforts to pursue partnerships or alternative funding such as through grants for NSI-566 (stem cell).

NSI – 189 (small molecule)

Major Depressive Disorder (MDD)

Major depressive disorder, or MDD (also known as recurrent depressive disorder, clinical depression, major depression, unipolar depression, or unipolar disorder), is a mental disorder characterized by episodes of all-encompassing low mood accompanied by low self-esteem and loss of interest or pleasure in normally enjoyable activities. MDD affects approximately 14.8 million American adults, or about 6.7 percent of the U.S. population age 18 and older in a given year. Additionally, the incidence of first line therapy failure creates a robust market for branded molecules in second/third line therapy. These factors combine to create a significant opportunity for a differentiated therapeutic agent.

NSI-189 is being developed for the treatment of major depressive disorder and other psychiatric and/or cognitive impairment indications associated with hippocampal atrophy. NSI-189 is the lead compound in our neurogenic small molecule drug platform. We believe that NSI-189 may provide an effective treatment for patients suffering from MDD by promoting neurogenesis.

Pre-Clinical Development

The inhibition of adult hippocampal neurogenesis has been implicated in a number of diseases that affect cognition and/or emotion such as major depressive disorder. As part of our research, we focused on compounds that were shown to enhance the baseline level of neurogenesis in normal healthy young mice. We believe that by enhancing baseline neurogenesis and accordingly, increasing hippocampal neurogenesis, we can decrease the effects of central nervous system or CNS diseases. Additionally, we believe that a compound that stimulates in vitro neurogenesis, enhances in vivo neurogenesis, increases hippocampal volume, and exerts anti-depressive effects on animals will be

well suited for treating major depressive disorder. During our pre-clinical research, we identified NSI-189 as seeming to stimulate all four activities. Pre-clinical testing of this compound at multiple doses showed antidepressant activity at 10, 30, and 100mg/kg doses with rapid bioavailability in the brain. Histology analysis of the mouse brains suggested a bell-shaped dose-response curve, 10mg/kg and 30mg/kg being optimal for pharmacologically active concentrations and with higher doses not necessarily yielding larger biological effects.

Clinical Development — MDD

Phase 1a

In February 2011, we commenced a Phase 1 clinical trial (Phase 1a portion), NSI-189, at California Clinical Trials, LLC, in Glendale, California. The purpose of the Phase 1a portion of the trial was to evaluate the safety of the drug in healthy volunteers. The Phase 1a portion tested a single oral administration of NSI-189 in 24 healthy volunteers and was completed in October of 2011. The Phase 1a study showed that NSI-189 had demonstrated no gender difference in exposure profiles and no difference in drug exposure (Area Under the Curve (AUC) and half-life ($t_{1/2}$)) between fasted and fed states. It also showed attractive pharmaceutical properties such as good solubility, high permeability, single crystalline polymorph with optimized salt form.

Phase 1b

In December of 2011, we received authorization from the FDA to commence the Phase 1b randomized, dose-escalating, placebo controlled clinical trial for the treatment of MDD. The purpose of the Phase 1b portion of the clinical trial was to determine the drug safety and tolerability in three dosages in diagnosed MDD patients. The Phase 1b portion consisted of subjects with MDD receiving daily doses for 28 consecutive days with an eight-week observation period. The trial was completed in November 2013 and met its primary endpoints of safety and tolerability and showed a promising reduction in depressive and cognitive symptoms across the secondary, exploratory endpoints.

In our Phase 1b study, tolerability and efficacy of NSI-189, a benzylpiperizine-aminopyridine neurogenic compound for treating MDD were examined. This was a double-blind, randomized, placebo-controlled, multiple-dose study with three cohorts. The first cohort received 40 mg QD (n=6) or placebo (n=2), the second cohort 40 mg BID (n=6) or placebo (n=2), and the third cohort 40 mg TID (n=6) or placebo (n=2). Twenty-four subjects with MDD were recruited, with the diagnosis and severity confirmed through remote interviews. Eligible patients received NSI-189 or placebo for 28 days in an inpatient setting with assessments for safety, pharmacokinetics (PK), pharmacodynamics (PD), and efficacy. Outpatient follow-up visits were conducted until Day 84 (± 3). In this study, NSI-189 was relatively well tolerated at all doses, and no serious adverse effects. NSI-189 AUC increased in a dose-related and nearly proportional manner across the 3 cohorts with a half-life of 17-20 hours. In the Phase 1b study, the exploratory clinical efficacy measurements, including Symptoms of Depression Questionnaire (SDQ), Montgomery-Asberg Depression Scale (MADRS), Clinical Global Impressions - Improvement (CGI-I), and The Massachusetts General Hospital (MGH) Cognitive and Physical Functioning Questionnaire (CPFQ), showed a promising reduction in depressive and cognitive symptoms across all measures for NSI-189, with significant improvement in the SDQ and CPFQ, and a medium to large effect size for all measures. These improvements persisted during the follow-up phase. NSI-189 showed potential as a treatment for MDD despite the small sample size of each cohort.

Phase 2

In March 2016, we commenced our NSI-189 Phase 2 clinical trial for the treatment of MDD. This study is a double-blind, placebo-controlled study of NSI-189 among out-patients with major depressive disorder and will consist of a screening period of 14-28 days and a randomized treatment. Approximately 220 subjects who meet eligibility during the screening period will be randomized to initiate a 12-week, double-blind treatment with NSI-189 80mg/day (provided as 40 mg BID), NSI-189 40 mg/day QD, or placebo. We have contracted with 12 sites within the US who have the track record of enrolling high quality MDD subjects. The primary endpoint will be Montgomery-Asberg Depression Rating Scale (MADRS). The secondary endpoints will consist of: Symptoms of Depression Questionnaire (SDQ), The Massachusetts General Hospital Cognitive and Physical Functioning Questionnaire (MGH CPFQ), 17-item Hamilton Rating Scale for Depression (HAM-D17), Clinical Global Impressions - Severity and Improvement (CGI-S, CGI-I), Cogstate Brief Battery, and Cogscreen Battery. Other pre-specified outcome measures will include Blood Diagnostics Panel of major depressive disorder as a biomarker and Massachusetts General Hospital Sexual Functioning Inventory (MGH SFI) as a safety endpoint. This study is powered to achieve 80% confidence level with two-sided statistical significance value (p) of 0.05 or less while assuming Cohen's effect size (d) of 0.5. We believe this study could serve as one of the two registration studies required for marketing approval by the US FDA. The results are expected in the second half of 2017. The study Principal Investigator will be Maurizio Fava, M.D. Slater Family Professor of Psychiatry at Harvard Medical School, Massachusetts General Hospital. For information on the trial please visit <https://clinicaltrials.gov/show/NCT02695472>.

NSI - 566 (Stem Cells)

Amyotrophic Lateral Sclerosis (ALS)

Amyotrophic lateral sclerosis, or ALS, is a disease of the nerve cells in the brain and spinal cord that control voluntary muscle movement. Approximately 6,400 people in the U.S. are diagnosed with ALS each year. The incidence of ALS is two per 100,000 people, and it is estimated that more than 20,000 Americans may be living with ALS at any given time. In ALS, nerve cells (neurons) waste away or die, and can no longer send messages to muscles. This eventually leads to muscle weakening, twitching, and an inability to move the arms, legs, and body. The condition slowly gets worse. When the muscles in the chest area stop working, it becomes hard or impossible to breathe. NSI-566 is under development as a potential treatment for ALS by providing cells designed to nurture and protect the patients' remaining motor neurons; and possibly repair some motor neurons which have not yet died but which are diseased. We have received orphan designation by the FDA for NSI-566 in ALS.

Clinical Development — ALS

Phase 1

In January 2010, we commenced the Phase 1 trial of NSI-566 in ALS at Emory University in Atlanta Georgia. The purpose of the Phase 1 trial was to evaluate the safety and transplantation technique of our proposed treatment and procedure. The dosing of patients in the Phase 1 trial, as designed, was completed in August of 2012.

Phase 2

We commenced our Phase 2 clinical trial for ALS in September of 2013. The transplantation portion of the trial was completed in August of 2014 and the observation period of six months after the last surgery concluded in January 2015. The Phase 2 ALS clinical trial met the primary safety endpoints and established what we believe to be the maximum safe tolerated dose of 16 million cells delivered in 40 injections. In September 2015, nine-month Phase 2 and combined Phase 1 and Phase 2 data on the NSI-566 trial in amyotrophic lateral sclerosis was presented at the American Neurological Association Meeting by principal investigator Eva Feldman, MD, PhD, Director of the A. Alfred Taubman Medical Research Institute and Director of Research of the ALS Clinic at the University of Michigan Health. We are in discussions with the FDA regarding a larger registration directed, controlled trial.

In January 2016, we announced that we were in discussions with various governmental, state and non-profit organizations regarding funding grants for a registration directed, controlled trial and that initiation of such a trial would, in part, be dependent upon significant funding from such sources. To date, substantially all of the clinical costs of our ALS studies have been funded by such grants.

Chronic Spinal Cord Injury

A spinal cord injury, or SCI, generally refers to any injury to the spinal cord that is caused by trauma instead of disease although in some cases, it can be the result of diseases. It is estimated that there are 12,500 new cases of SCI per year and that at any given time, it is estimated around 276,000 US spinal cord patients in 2014. People in the United States that are living with SCI. Chronic spinal cord injury refers to the time after the initial hospitalization. SCI's are most often traumatic, caused by lateral bending, dislocation, rotation, axial loading, and hyperflexion or hyperextension of the cord or cauda equina. Motor vehicle accidents are the most common cause of SCI's, while other causes include falls, work-related accidents, sports injuries, and penetrations such as stab or gunshot wounds. In

certain instances, SCIs can also be of a non-traumatic origin, as in the case of cancer, infection, intervertebral disc disease, vertebral injury and spinal cord vascular disease. We believe that NSI-566 may provide an effective treatment for chronic spinal cord injury by “bridging the gap” in the spinal cord circuitry created in traumatic spinal cord injury and providing new cells to help transmit the signal from the brain to points at or below the point of injury.

Clinical Development – Chronic Spinal Cord Injury

Phase 1

During the first quarter of 2013, we received authorization from the FDA to commence our proposed Phase 1 clinical trial to treat chronic spinal cord injury. The entire trial took place at The University of California, San Diego. The trial commenced during the third quarter of 2014 and the first subject was treated in October 2014. The study enrolled four AIS A thoracic-spinal cord injury subjects (motor and sensory complete), one-to-two years post-injury at the time of stem cell treatment. In January 2016 at the Facilitate Cell & Gene Therapy World Conference, we reported six-month follow-up data on all four subjects. The stem cell treatment demonstrated feasibility and safety; there were no serious adverse events. A self-reported ability to contract some muscles below the level of injury was confirmed via clinical and electrophysiological follow-up examinations in one of the four subjects treated. All patients will be followed for five years. To date, substantially all of the clinical costs of this study have been funded by grants arranged through the University of California, San Diego.

Motor Deficits Due to Ischemic Stroke

Ischemic strokes, the most common type of stroke, occur as a result of an obstruction within a blood vessel supplying blood to the brain. Approximately 15 million people worldwide suffer from stroke of which it is estimated that 87% are ischemic stroke. Post-stroke motor deficits include paralysis in arms and legs and can be permanent. We believe that NSI-566 may provide an effective treatment for restoring motor deficits resulting from ischemic stroke by both creating new circuitry in the area of injury and through repairing and nurturing diseased cells to improve function in patients.

Clinical Development – Motor Deficit Due to Ischemic Stroke

Phase 1

In the fourth quarter of 2013 we commenced a human clinical trial for treatment of motor deficits due to ischemic stroke. The trial is being conducted by Neuralstem China, at BaYi Brain Hospital in Beijing, China utilizing NSI-566. The trial authorization encompasses a Phase 1 clinical trial design and will test the safety of direct injections of NSI-566 into the brain. The Phase 1 trial is a safety trial designed to evaluate the maximum safe tolerated dose. We have completed dosing all three planned cohorts for a total of nine subjects, three subjects in each cohort. To date, we have funded substantially all of the costs associated with the Ischemic Stroke program.

Our Technologies

Stem Cells

Our technology enables the isolation and large-scale expansion of regionally specific, human neural stem cells from all areas of the developing human brain and spinal cord, thus enabling the generation of physiologically relevant human neurons of all types. We believe that our stem cell technology will assist the body in producing new cells to replace malfunctioning or dead cells as a way to treat disease and injury. Many significant and currently untreatable human diseases arise from the loss or malfunction of specific cell types in the body. Our focus is the development of effective methods to generate replacement cells from neural stem cells. We believe that replacing damaged, malfunctioning or dead neural cells with fully functional ones may be a useful therapeutic strategy in treating many diseases and conditions of the central nervous system. We own or exclusively license over 50 U.S. and foreign issued patents and over 30 U.S. and foreign patent applications related to our stem cell technologies.

Small Molecule Pharmaceutical Compounds

Utilizing our proprietary stem cell derived, screening capability, we have developed and patented a series of small molecule compounds. We believe the low molecular weight organic compounds can efficiently cross the blood/brain barrier. In mice, research indicated that the small molecule compounds both stimulate neurogenesis of the hippocampus and increase its volume. Our collaborators at Massachusetts General Hospital have presented the human data from the MDD trial which showed clinically meaningful and statistically significant improvement in depressive and cognitive scales. We believe the small molecule compounds may assist promoting synaptogenesis or neurogenesis

in the human hippocampus documented in indications such as MDD.

Our small molecule compounds are covered by over 60 exclusively owned U.S. and foreign issued patents and over 10 exclusively owned U.S. and foreign patent applications related to our small molecule compounds.

Intellectual Property

Our research and development is supported by our intellectual property. We own or exclusively license over 110 U.S. and foreign issued patents and over 40 U.S. and foreign patent applications in the field of regenerative medicine, related to our stem cell technologies as well as our small molecule compounds. Our issued patents have expiration dates ranging from 2016 through 2034, based on appropriate Patent Expansions. In our opinion the patents expiring in 2016 and in the near term are not critical to our business.

Operating Strategy

We generally employ an outsourcing strategy where we outsource our Good Laboratory Practices, or GLP, preclinical development activities and Good Manufacturing Practices, or GMP, Good Tissue Practices, or GTP, if applicable, and clinical development activities to contract research organizations or CROs and contract manufacturing organizations or CMOs as well as all non-critical corporate functions. Manufacturing is also outsourced to organizations with approved facilities and manufacturing practices. This outsource model allows us to better manage cash on hand and minimize non-vital expenditures. It also allows for us to operate with relatively fewer employees and lower fixed costs than that required by other companies conducting similar business.

Employees

As of March 31, 2016, we had 32 full-time employees. Of these full-time employees, 24 work on research and development and clinical operations 8 in administration. We also use the services of numerous outside consultants in business and scientific matters.

Our Corporate Information

We were incorporated in Delaware in 2001. Our principal executive offices are located at 20271 Goldenrod Lane, Germantown, Maryland 20876, and our telephone number is (301) 366-4841. Our website is located at www.neuralstem.com.

In addition to announcing material financial information through our investor relations website, press releases, SEC filings and public conference calls and webcasts, we also intend to use the following social media channels as a means of disclosing information about the company, its services and other matters and for complying with our disclosure obligations under Regulation FD:

· Neuralstem's Twitter Account (https://twitter.com/Neuralstem_Inc)

· Neuralstem's LinkedIn Company Page (<http://www.linkedin.com/company/neuralstem-inc->)

The information we post through these social media channels may be deemed material. Accordingly, investors should monitor these accounts and the blog, in addition to following the company's press releases, SEC filings and public conference calls and webcasts. This list may be updated from time to time.

We have not incorporated by reference into this report the information in, or that can be accessed through, our website or social media channels, and you should not consider it to be a part of this report.

Trends & Outlook

Revenue

We generated no revenues from the sale of our proposed therapies for any of the periods presented. We are mainly focused on successfully managing our current clinical trials related to our small molecule compounds and seeking potential partnerships for our stem cell product candidates. We are also pursuing pre-clinical studies on other central nervous system indications in preparation for potential future clinical trials.

In the first quarter of 2013 and the third quarter of 2012, we licensed the use of certain of our intellectual property to third parties. During the three-months ended March 31, 2016 and 2015, we recognized approximately \$3,000 and

\$3,000 of revenue, respectively, related to up-front payments and ongoing fees under these licenses.

On a long-term basis, we anticipate that our revenue will be derived primarily from licensing fees and sales of our small molecule compounds and licensing fees and royalties from our cell based therapies. Because we are at such an early stage in the clinical trials process, we are not yet able to accurately predict when we will have a product ready for commercialization, if ever.

Research and Development Expenses

Our research and development expenses consist primarily of contractor and personnel expenses associated with clinical trials and regulatory submissions; costs associated with preclinical activities such as proof of principle for new indications; toxicology studies; costs associated with cell processing and process development; facilities-related costs and supplies. Clinical trial expenses include payments to research organizations, contract manufacturers, clinical trial sites, consultants and laboratories for testing clinical samples.

We focus on the development of treatment candidates with potential uses in multiple indications, and use employee and infrastructure resources across several projects. Accordingly, many of our costs are not attributable to a specifically identified product and we do not account for internal research and development costs on a project-by-project basis.

For a further description of these clinical trials, see the section of this report entitled “Pre-Clinical and Clinical Programs and Development” contained in Item 2.

We expect that research and development expenses, which include expenses related to our ongoing clinical trials, will increase in the future, as funding allows and we proceed into our anticipated Phase 2 trial in major depressive disorder. To the extent that it is practical, we will continue to outsource much of our efforts, including product manufacture, proof of principle and pre-clinical testing, toxicology, tumorigenicity, dosing rationale, and development of clinical protocol and IND applications. This approach allows us to use the best expertise available for each task and permits staging new research projects to fit available cash resources.

We have formed a wholly owned subsidiary in the People’s Republic of China. We anticipate that this subsidiary will primarily: (i) conduct pre-clinical research with regard to proposed stem cells therapies, and (ii) oversee our approved future clinical trials in China, including the current trial to treat motor deficits due to ischemic stroke.

General and Administrative Expenses

General and administrative expenses are primarily comprised of salaries, benefits and other costs associated with our operations including, finance, human resources, information technology, public relations, legal fees, facilities and other external general and administrative services.

Critical Accounting Policies

Our consolidated financial statements have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Note 2 of the Notes to Condensed Consolidated Financial Statements included elsewhere herein describes the significant accounting policies used in the preparation of the financial statements. Certain of these significant accounting policies are considered to be critical accounting policies, as defined below.

A critical accounting policy is defined as one that is both material to the presentation of our financial statements and requires management to make difficult, subjective or complex judgments that could have a material effect on our financial condition and results of operations. Specifically, critical accounting estimates have the following attributes: (1) we are required to make assumptions about matters that are highly uncertain at the time of the estimate; and (2) different estimates we could reasonably have used, or changes in the estimate that are reasonably likely to occur, would have a material effect on our financial condition or results of operations.

Estimates and assumptions about future events and their effects cannot be determined with certainty. We base our estimates on historical experience and on various other assumptions believed to be applicable and reasonable under the circumstances. These estimates may change as new events occur, as additional information is obtained and as our operating environment changes. These changes have historically been minor and have been included in the financial statements as soon as they became known. Based on a critical assessment of our accounting policies and the underlying judgments and uncertainties affecting the application of those policies, management believes that our financial statements are fairly stated in accordance with U.S. GAAP, and present a meaningful presentation of our financial condition and results of operations. We believe the following critical accounting policies reflect our more significant estimates and assumptions used in the preparation of our consolidated financial statements:

Use of Estimates - Our financial statements prepared in accordance with U.S. GAAP require us to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Specifically, we have estimated the expected

economic life and value of our patent technology, our net operating loss carryforward and related valuation allowance for tax purposes and our stock -based compensation expenses related to employees, directors, consultants and investment banks. Actual results could differ from those estimates.

Long Lived Intangible Assets - Our long lived intangible assets consist of our intellectual property patents including primarily legal fees associated with the filings and in defense of our patents. The assets are amortized on a straight-line basis over the expected useful life which we define as ending on the expiration of the patent group. These assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. We assess this recoverability by comparing the carrying amount of the asset to the estimated undiscounted future cash flows to be generated by the asset. If an asset is deemed to be impaired, we estimate the impairment loss by determining the excess of the asset's carrying amount over the estimated fair value. These determinations use assumptions that are highly subjective and include a high degree of uncertainty. During the three months ended March 31, 2016 and 2015, no significant impairment losses were recognized.

Fair Value Measurements - The carrying amounts of our short-term financial instruments, which primarily include cash and cash equivalents, other short-term investments, accounts payable and accrued expenses, approximate their fair values due to their short maturities. The fair value of our long-term indebtedness is estimated based on the quoted prices for the same or similar issues or on the current rates offered to the Company for debt of the same remaining maturities. The fair values of our derivative instruments were estimated using Level 3 unobservable inputs.

Share-Based Compensation - We account for share-based compensation at fair value; accordingly we expense the estimated fair value of share-based awards over the requisite service period. Share-based compensation cost for stock options and warrants issued to employees and board members is determined at the grant date while awards granted to non-employee consultants are generally valued at the vesting date using an option pricing model. Option pricing models require us to make assumptions, including expected volatility and expected term of the options. If any of the assumptions we use in the model were to significantly change, stock based compensation expense may be materially different. Share-based compensation cost for restricted stock and restricted stock units issued to employees and board members is determined at the grant date based on the closing price of our common stock on that date. The value of the award that is ultimately expected to vest is recognized as expense on a straight-line basis over the requisite service period.

RESULTS OF OPERATIONS

Comparison of Three Months Ended March 31, 2016 and 2015

Revenue

We did not generate any revenues from the sale of our products in any of the periods presented. For the three months ended March 31, 2016 and 2015, we recognized approximately \$3,000 and \$3,000, respectively related to the

licensing of certain intellectual properties to third parties.

Operating Expenses

Operating expenses for the three months ended March 31, 2016 and 2015 were as follows:

	Three Months Ended March 31,		Increase (Decrease)	
	2016	2015	\$	%
Operating Expenses				
Research and development expenses	\$ 3,065,590	\$ 3,182,823	\$ (117,233)	(4)%
General and administrative expenses	3,170,522	1,433,074	1,737,448	121 %
Total operating expenses	\$ 6,236,112	\$ 4,615,897	\$ 1,620,215	35 %

Research and Development Expenses

The decrease of approximately \$117,000 or 4% in research and development expenses for the period ended March 31, 2016 compared to the comparable period of 2015 was primarily attributable to a decrease in pre-clinical and clinical cost partially offset by an increase in headcount and stock based compensation.

General and Administrative Expenses

The increase of approximately \$1,737,000 or 121% in general and administrative expenses for the period ended March 31, 2016 compared to the comparable period of 2015 was primarily due to a severance accrual and increased stock based compensation resulting from the accelerated vesting of options, both related to the termination of our former Chief Executive Officer.

Other expense

Other expenses, net totaled approximately \$372,000 and \$440,000 for the three months ended March 31, 2016 and 2015, respectively. Other expense in 2016 consisted of approximately \$387,000 of interest expense principally related to our long-term debt partially offset by approximately \$11,000 of interest income.

Other expenses, net in 2015 consisted primarily of approximately \$454,000 of interest expense principally related to our long-term debt partially offset by approximately \$14,000 in interest income.

Liquidity and Capital Resources

Since our inception, we have financed our operations through the sales of our securities, issuance of long term debt, the exercise of investor warrants, and to a lesser degree from grants and research contracts.

We will require additional capital to conduct research and development, establish and conduct clinical and pre-clinical trials, enter into commercial-scale manufacturing arrangements and to provide for marketing and distribution of our products. We cannot assure you that we will be able to secure such additional financing or that the expected income will materialize. Several factors will affect our ability to raise additional funding, including, but not limited to market conditions, interest rates and, more specifically, our progress in our exploratory, preclinical and future clinical development programs.

	Three Months Ended March 31,		Increase (Decrease)	
	2016	2015	\$	%
Net cash used in operating activities	\$ (3,488,221)	\$ (4,719,821)	\$ 1,231,600	26 %
Net cash provided by/(used in) investing activities	\$ 7,490,108	\$ (98,276)	\$ 7,588,384	7722 %
Net cash provided by/(used in) financing activities	\$ (1,096,951)	\$ 5,892,463	\$ (6,989,414)	(119)%

Our Cash and Cash Equivalent balances of approximately \$7.6 million as at March 31, 2016.

On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. The warrants allow the holder to purchase one share of common stock, have an exercise price of \$0.40 per share and a term of 5 years. This offering was made pursuant to our shelf registration statement that was declared effective by the SEC on June 19, 2014 (Registration No. 333-196567).

The public offering in May 2016 has provided us with sufficient funds to finance operations at least through December 31, 2016, however, we will require additional capital to conduct research and development, establish and conduct clinical and pre-clinical trials, enter into commercial-scale manufacturing arrangements and to provide for marketing and distribution of our products. We cannot assure you that we will be able to secure such additional financing or that the expected income will materialize. Several factors will affect our ability to raise additional funding, including, but not limited to market conditions, interest rates and, more specifically, our progress in our exploratory, preclinical and future clinical development programs.

Net Cash Used in Operating Activities

We used approximately \$3,488,000 and \$4,720,000 of cash in our operating activities for the three months ended March 31, 2016 and 2015, respectively. The decrease in our use of cash of approximately \$1,232,000 was primarily due to the net loss coupled with changes in our operating assets and liabilities.

Net Cash Provided by (used in) Investing Activities

We received approximately \$7,490,000 and used approximately \$98,000 of cash in connection with investment activities for the three months ended March 31, 2016 and 2015 respectively.

Net Cash Provided by (used in) Financing Activities

Use of cash from financing activities were approximately \$(1,097,000) and cash provided by financing activities were \$5,892,000 in the three months ended March 31, 2016 and 2015, respectively. Cash outflow from financing activities in the first quarter of 2016 is the result of principal payments on debt. Cash inflow from financing activities in the first quarter of 2015 is the result of proceeds from equity transactions.

Future Liquidity and Needs

We have incurred significant operating losses and negative cash flows since inception. We have not achieved profitability and may not be able to realize sufficient revenue to achieve or sustain profitability in the future. We do not expect to be profitable in the next several years, but rather expect to incur additional operating losses. We have limited liquidity and capital resources and must obtain significant additional capital resources in order to sustain our product development efforts, for acquisition of technologies and intellectual property rights, for preclinical and clinical testing of our anticipated products, pursuit of regulatory approvals, acquisition of capital equipment, laboratory and office facilities, establishment of production capabilities, for general and administrative expenses and other working capital requirements. We rely on cash balances and the proceeds from the offering of our securities, exercise of outstanding warrants and grants to fund our operations.

We intend to pursue opportunities to obtain additional financing in the future through the sale of our securities and additional research grants. We currently have two shelf registration statements that are effective. On September 13, 2013, our shelf registration statement (Registration No. 333-190936) registering the sale of up to \$50 million of our securities was declared effective by the SEC. To date, through March 31, 2016 we have sold or reserved for sale upon the exercise of outstanding warrants approximately \$48.2 million of securities under this shelf registration statement. On June 19, 2014, our shelf registration statement registering the sale of up to \$100 million of our securities was declared effective by the SEC (Registration No. 333-196567).

On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. The warrants allow the holder to purchase one share of common stock, have an exercise price of \$0.40 per share and a term of 5 years. This offering was made pursuant to our shelf registration statement that was declared effective by the SEC on June 19, 2014.

We anticipate conducting financing in the future based on our shelf registration statement when and if financing opportunities arise.

The source, timing and availability of any future financing will depend principally upon market conditions, interest rates and, more specifically, our progress in our exploratory, preclinical and future clinical development programs. Funding may not be available when needed, at all, or on terms acceptable to us. Lack of necessary funds may require us, among other things, to delay, scale back or eliminate some or all of our research and product development programs, planned clinical trials, and/or our capital expenditures or to license our potential products or technologies to third parties.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Financial instruments that potentially subject us to concentrations of credit risk consist of cash and cash equivalents which are held at highly rated United States financial institutions and at times maintain the balances of our deposits in excess of federally insured limits. We invest our cash in instruments with short-term maturities with the objective of preserving capital. Because of the short-term maturities, we do not believe that a one-half percentage point increase or decrease in interest rates would have had a material effect on our interest income.

We are subject to interest rate risk for our long-term debt which contains a floating interest rate based on Wall Street Journal published prime rate. For the full year ended December 31, 2016 a one percentage point increase in the prime rate would increase our interest expense by approximately \$61,000.

Our foreign operations in China subject us to changes in foreign exchange rates. Changes in exchange rates for the year ended December 31, 2016 are not expected to have a material effect as the operations are expected to be limited. Future changes to foreign exchange rates could have a material effect on us as our clinical trial activity increases.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Based on an evaluation under the supervision and with the participation of the Company's management, the Company's principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act were effective as of March 31, 2016,

to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and (ii) accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal control over financial reporting during the first quarter of 2016, which were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Inherent Limitations Over Internal Controls

The Company's internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles ("GAAP"). The Company's internal control over financial reporting includes those policies and procedures that:

- (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the Company's assets;
- (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that the Company's receipts and expenditures are being made only in accordance with authorizations of the Company's management and directors; and
- (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the Company's assets that could have a material effect on the financial statements.

Management, including the Company's principal executive officer and principal financial officer, does not expect that the Company's internal controls will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of internal controls can provide absolute assurance that all control issues and instances of

fraud, if any, have been detected. Also, any evaluation of the effectiveness of controls in future periods are subject to the risk that those internal controls may become inadequate because of changes in business conditions, or that the degree of compliance with the policies or procedures may deteriorate.

PART II

OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are parties to legal proceedings that we believe to be ordinary, routine litigation incidental to the business of present or former operations. It is management's opinion, based on the advice of counsel, that the ultimate resolution of such litigation will not have a material adverse effect on our financial condition, results of operations or cash flows.

ITEM 1A. RISK FACTORS

Investing in our common stock involves a high degree of risk. We have described below a number of uncertainties and risks which, in addition to uncertainties and risks presented elsewhere in this Quarterly Report, may adversely affect our business, operating results and financial condition. The uncertainties and risks enumerated below as well as those presented elsewhere in this Quarterly Report, and those included in our Annual Report on Form 10-K for the year ended December 31, 2015, filed with the SEC should be considered carefully in evaluating our company and our business and the value of our securities.

Risks Relating to Our Stage of Development and Capital Structure

We may not be able to continue as a going concern if we do not obtain additional financing by December, 2016.

We have incurred losses since our inception and have not demonstrated the ability to generate revenues from the sales of our products or services. These factors create substantial doubt about our ability to continue as a going concern. The consolidated financial statements do not include any adjustment that might be necessary if we are unable to continue as a going concern.

Our ability to continue as a going concern is dependent on us generating cash from the sales of our securities and/or obtaining debt financing.

Our cash and cash equivalents balance at March 31, 2016 was approximately \$7.6 million. On May 06, 2016, we closed a public offering of 20,000,000 shares of common stock and 20,000,000 common stock purchase warrants at a public offering price of \$0.40 per each share and common stock purchase warrant. We received aggregate gross proceeds of \$8.0 million and net proceeds of approximately \$7,420,000 from the offering. Based upon our cash at March 31, 2016, and the proceeds from our May public offering, we expect to be able to fund our operations through December 31, 2016. Our ability to continue as a going concern is wholly dependent upon obtaining sufficient financing to fund our operations. Accordingly, despite our ability to secure capital in the past, there is no assurance that additional equity or debt financing will be available to us when needed. In the event that we are not able to secure financing, we may be forced to curtail operations, delay or stop ongoing clinical trials, cease operations altogether or file for bankruptcy.

Our auditors have expressed substantial doubt about our ability to continue as a going concern.

Our auditors' report on our December 31, 2015 financial statements expressed an opinion that our capital resources as of the date of their audit report were not sufficient to sustain operations or complete our planned activities for the upcoming year unless we raised additional funds. Accordingly, our current cash level raises substantial doubt about our ability to continue as a going concern. If we do not obtain additional funds by such time, we may no longer be able to continue as a going concern and will cease operation which means that our shareholders may lose their entire investment .

We have a history of losses.

Since inception in 1996 and through March 31, 2016, we have accumulated losses totaling approximately \$178,564,000. On March 31, 2016, we had a working capital surplus of approximately \$1,116,000 and stockholders' deficit of approximately \$(169,000). Our net losses for the two most recent fiscal years have been approximately \$20,904,000 and \$22,629,000, for 2015 and 2014, respectively, while our loss for the three months ended March 31, 2016 was approximately \$6,606,000. Although we recognized revenue in 2016 and 2015 as a result of us providing subcontractor services and the licensing of our intellectual property, we have generated no significant revenue from the sales of our proposed products.

Our ability to generate revenues and achieve profitability will depend upon our ability to complete the development of our proposed products, obtain the required regulatory approvals, manufacture and market and sell our proposed products. To date, we have not generated any revenue from the commercial sale of our proposed products. No assurances can be given as to exactly when, if at all, we will be able to fully develop, commercialize, market, sell and/or derive any, let alone material, revenues from our proposed products.

We will need to raise additional capital to continue operations.

Since our inception, we have funded our operations through the sale of our securities, credit facilities, the exercise of options and warrants, and to a lesser degree, from grants and research contracts and other revenue generating activities such as licensing. As of March 31, 2016, we had cash, cash equivalents and short-term investments on hand of approximately \$7,621,000. We cannot assure you that we will be able to secure additional capital through financing transactions, including issuance of debt, licensing agreements or grants. Our inability to license our intellectual property, obtain grants or secure additional financing will materially impact our ability to fund our current and planned operations.

We have spent and expect to continue spending substantial cash in the research, development, clinical and pre-clinical testing of our proposed products with the goal of ultimately obtaining FDA approval and equivalent international approvals to market such products. We will require additional capital to conduct research and development, establish and conduct clinical and pre-clinical trials, enter into commercial-scale manufacturing arrangements and to provide for marketing and distribution of our products. We cannot assure you that financing will be available if needed. If additional financing is not available, we may not be able to fund our operations, develop or enhance our technologies, take advantage of business opportunities or respond to competitive market pressures. If we exhaust our cash reserves and are unable to secure adequate additional financing, we may be unable to meet operating obligations which could result in us initiating bankruptcy proceedings or delaying, or eliminating some or all of our research and product development programs.

We will need to raise additional capital to pay our indebtedness as it comes due.

We have a substantial level of debt. As of March 31, 2016, we had approximately \$7,235,000 in aggregate principal amount long-term indebtedness outstanding. Under our amended loan and security agreement, we were required to make monthly interest only payments through September 2015; and are required to make monthly interest and principal payments of approximately \$435,000 per month from January 2016 through March 2017 and make a balloon payment for the remaining principal in April 2017. As security for such indebtedness, we have pledged substantially all of our assets, including our intellectual property. If we are unable to make the required payments, or if we fail to comply with the various requirements and covenants of our indebtedness, we would be in default, which would permit the holders of our indebtedness to accelerate the maturity and require immediate repayment and lead to potential foreclosure on the assets securing the debt. Any default under our indebtedness would have a material adverse effect on our business, operating results and financial condition. Additionally, our amended loan and security agreement governing this loan also contains a number of affirmative and restrictive covenants, including reporting requirements and other collateral limitations, certain limitations on liens and indebtedness, dispositions, mergers and acquisitions, restricted payments and investments, corporate changes and limitations on waivers and amendments to certain agreements, our organizational documents, and documents relating to debt that is subordinate to our obligations under the credit facility. Our failure to comply with the covenants in the amended loan and security agreement could result in an event of default that, if not cured or waived, could result in the acceleration of all or a substantial portion of our

debt and potential foreclosure on the assets securing the debt. If we are unable to refinance or repay our indebtedness as it becomes due, including upon an event of default, we may become insolvent and be unable to continue operations.

If we are unable to meet the continued listing requirements for the Nasdaq Capital Market, our securities will be subject to delisting.

On April 20, 2016, we received a written notice from the Nasdaq Stock Market LLC that we are not in compliance with Nasdaq Listing Rule 5550(a)(2), as the minimum bid price of our common stock has been below \$1.00 per share for 30 consecutive business days. In accordance with Nasdaq Listing Rule 5810(c)(3)(A), we have a period of 180 calendar days, or until October 17, 2016, to regain compliance with the minimum bid price requirement. To regain compliance, the closing bid price of our common stock must meet or exceed \$1.00 per share for at least ten consecutive business days during this 180 calendar day period. In the event we do not regain compliance by October 17, 2016, we may be eligible for an additional 180 calendar day grace period if we meet the initial listing standards, with the exception of bid price, for the Nasdaq Capital Market, and provide written notice to Nasdaq of our intention to cure the deficiency during the second compliance period, by effecting a reverse stock split, if necessary. If we do not regain compliance within the allotted compliance period(s), including any extensions that may be granted by Nasdaq, Nasdaq will provide notice that our common stock will be subject to delisting. We will then be entitled to appeal the determination to a Nasdaq Listing Qualifications Panel and request a hearing. We cannot be sure that our share price will comply with the requirements for continued listing of our shares on the Nasdaq Capital Market in the future or that we will comply with the other continued listing requirements. If our shares lose their status on the Nasdaq Capital Market, we believe that our shares would likely be eligible to be quoted on the inter-dealer electronic quotation and trading system operated by Pink OTC Markets Inc., commonly referred to as the Pink Sheets and now known as the OTCQB market. These markets are generally considered not to be as efficient as, and not as broad as, the Nasdaq Capital Market. If our common stock is delisted, this would, among other things, substantially impair our ability to raise additional funds and could result in a loss of institutional investor interest and fewer development opportunities for us.

Risks Relating to Our Business

Our business is dependent on the successful development of our product candidates and our ability to raise additional capital.

Our business is significantly dependent on our product candidates which are currently at different phases of pre-clinical and clinical development. The process to approve our product candidates is time-consuming, involves substantial expenditures of resources, and depends upon a number of factors, including the availability of alternative treatments, and the risks and benefits demonstrated in our clinical trials. Our success will depend on our ability to achieve scientific and technological advances and to translate such advances into FDA-approvable, commercially competitive products on a timely basis. Failure can occur at any stage of the process. If we are not successful in developing our product candidates, we will have invested substantial amounts of time and money without developing revenue-producing products. As we enter a more extensive clinical program for our product candidates, the data generated in these studies may not be as compelling as the earlier results. This, in turn, could adversely impact our ability to raise additional capital and pursue our business plan and planned research and development efforts.

Our proposed products are not likely to be commercially available for at least several years, if at all. Our development schedules for our proposed products may be affected by a variety of factors, including technological difficulties, clinical trial failures, regulatory hurdles, competitive products, intellectual property challenges and/or changes in governmental regulation, many of which will not be within our control. Any delay in the development, introduction or marketing of our product candidates could result either in such products being marketed at a time when their cost and performance characteristics would not be competitive in the marketplace or in the shortening of their commercial lives. In light of the long-term nature of our projects, the unproven technology involved and the other factors described elsewhere in this section, there can be no assurance that we will be able to successfully complete the development or marketing of any of our proposed product candidates.

Our business relies on technologies that we may not be able to commercially develop and we are unable to predict when or if we will be able to earn revenues.

We have allocated the majority of our resources to the development of our stem cell and small molecule technologies. Our ability to generate revenue and operate profitably will depend on being able to develop these technologies for human applications. These are emerging technologies that may have limited human application. We cannot guarantee that we will be able to develop our technologies or that if developed, our technologies will result in commercially viable products or have any commercial utility or value. We anticipate that the commercial sale of our proposed products and/or royalty/licensing fees related to our technologies, will be our primary sources of revenue. We recognized revenue of approximately \$10,000 and \$19,000 for the years ended December 31, 2015 and 2014, respectively, and \$3,000 for the three months ended March 31, 2016, related to the licensing of certain intellectual

property to third parties and certain subcontractor services that we provided. If we are unable to develop our technologies, we may never realize any significant revenue. Additionally, given the uncertainty of our technologies, product candidates and the need for government regulatory approval, we cannot predict when, or if ever, we will be able to realize revenues related to our products. As a result, we will be primarily dependent on our ability to raise capital through the sale of our securities for the foreseeable future.

Our product development programs are based on novel technologies in an emerging field and are inherently risky.

We are subject to the risks inherent in the development of products based on new technologies. The novel nature of therapies in the field of regenerative medicine creates significant challenges in regard to product development and optimization, manufacturing, government regulation, third party reimbursement, and market acceptance. For example, the pathway to regulatory approval for cell-based therapies, including our product candidates, may be more complex and lengthy than the pathway for conventional drugs. These challenges may prevent us from developing and commercializing products on a timely or profitable basis or at all. Regenerative medicine is still an emerging field. There can be no assurances that we will ultimately produce any viable commercialized products and processes. Even if we are able to produce a commercially viable product, there may be strong competitors in this field and our products may not be able to successfully compete against them.

Our stem cell therapy programs rely on experimental surgical devices and experimental and highly invasive surgical procedures.

We are subject to the risks inherent in the use and development of experimental surgical devices and procedures. We have limited experience with medical devices and must rely on outside consultants and manufacturers to develop and seek any required approvals for the device we use in connection with our stem cell therapy program. Additionally, the surgical procedures required to administer our stem cell therapy is experimental, highly invasive and is required to be performed by highly experienced neurosurgeons who have received special training. We cannot guarantee consistent and safe performance of the device or the surgical procedure. A surgery related adverse event may result in a clinical hold and may have long-term and damaging effects on our ability to complete development of the stem cell therapy programs, including the completion of any ongoing or planned clinical trials. Even if one or more of our programs is successful and receives marketing approval from a regulatory authority, due to the specialized nature of the device and surgical procedure, there may not be sufficient train surgeons to administer our therapy.

We are unable to predict when or if we will be able to earn revenues.

Given the uncertainty of our technologies and the need for government regulatory approval, we cannot predict when, or if ever, we will be able to realize revenues related to our products.

Our proposed products are not likely to be commercially available for at least several or more years, if ever. Accordingly, we do not foresee generating any significant revenue during such time. As a result, we will be primarily dependent on our ability to raise capital through the sale of our securities to fund our operations for the foreseeable future.

Our inability to manufacture and store our stem cells in-house that are used in our products could adversely impact our business.

We currently outsource most of the manufacturing of our stem cells and small molecule pharmaceutical compounds to third party contractors and as such have limited ability to adequately control the manufacturing process and the safe storage thereof. Any manufacturing or storage irregularity, error, or failure to comply with applicable regulatory procedure would require us to find new third parties to outsource our manufacturing and storage responsibilities or our business would be impacted. Additionally, as part of our business plan, we are developing in-house manufacturing capabilities but there can be no assurance that such capabilities will be successfully developed or if developed, be sufficient to meet our demands. And delays in the development of such in-house manufacturing capabilities could adversely affect our plans.

If we are unable to complete pre-clinical and clinical testing and trials or if clinical trials of our product candidates are prolonged, delayed, suspended or terminated, our business and results of operations could be materially harmed.

We are currently in clinical trials for NSI-566 and NSI-189, two of our proposed products, with regard to multiple indications. Although we have commenced a number of trials, the ultimate outcome of the trials is uncertain. If we are unable to satisfactorily complete such trials, or if such trials yield unsatisfactory results, we may be unable to obtain regulatory approval for and commercialize our proposed products. No assurances can be given that our clinical trials will be completed or result in successful outcomes. A number of events, including any of the following, could delay the completion of our planned clinical trials and negatively impact our ability to obtain regulatory approval for, and to market and sell, a particular product candidate:

- conditions imposed on us by the FDA or any foreign regulatory authority regarding the scope or design of our clinical trials;
- delays in obtaining, or our inability to obtain, required approvals from institutional review boards, or IRBs, or other reviewing entities at clinical sites selected for participation in our clinical trials;
- insufficient supply or deficient quality of our product candidates or other materials necessary to conduct our clinical trials;
- delays in obtaining regulatory agency agreement for the conduct of our clinical trials;
- lower than anticipated enrollment and retention rate of subjects in clinical trials;
- serious and unexpected side effects experienced by patients in our clinical trials which are related to the use of our product candidates; or
- failure of our third-party contractors to meet their contractual obligations to us in a timely manner.

Clinical trials may also be delayed or terminated as a result of ambiguous or negative interim results. In addition, a clinical trial may be suspended or terminated by us, the FDA, the IRBs at the sites where the IRBs are overseeing a trial, or a data safety monitoring board, or DSMB, overseeing the clinical trial at issue, or other regulatory authorities due to a number of factors. Additionally, changes in regulatory requirements and guidance may occur and we may need to amend clinical trial protocols to reflect these changes. Amendments may require us to resubmit our clinical trial protocols to IRBs for reexamination, which may impact the cost, timing or successful completion of a clinical trial. We do not know whether our clinical trials will be conducted as planned, will need to be restructured or will be completed on schedule, if at all. Delays in our clinical trials will result in increased development costs for our drug candidates. In addition, if we experience delays in the completion of, or if we terminate, any of our clinical trials, the commercial prospects for our drug candidates may be harmed and our ability to generate product revenues will be jeopardized. Furthermore, many of the factors that cause, or lead to, a delay in the commencement or completion of clinical trials may also ultimately lead to the denial of regulatory approval of a drug candidate. If regulatory authorities do not approve our products or if we fail to maintain regulatory compliance, we would be unable to commercialize our proposed products, and our business and results of operations could be materially harmed.

The results of pre-clinical studies and clinical trials may not be predictive of the results of our later-stage clinical trials and our proposed products may not have favorable results in later-stage clinical trials or receive regulatory approval.

Positive results from pre-clinical studies or our Phase 1 and Phase 2 trials should not be relied upon as evidence that our clinical trials will succeed. Even if our product candidates achieve positive results in pre-clinical studies or during our Phase 1 and Phase 2 studies, we will be required to demonstrate through further clinical trials that our product candidates are safe and effective for use in a diverse population before we can seek regulatory approvals for their commercial sale. There is typically an extremely high rate of attrition from the failure of product candidates as they proceed through clinical trials. If any product candidate fails to demonstrate sufficient safety and efficacy in any clinical trial, then we may experience potentially significant delays in, or be required to abandon, development of that product candidate. Additionally, failure to demonstrate safety and efficacy results acceptable to the FDA in later stage trials could impair our development prospects and even prevent regulatory approval of our current and future product candidates. Any such delays or abandonment in our development efforts of any of our product candidates would materially impair our ability to generate revenues.

Our research and development expenses are subject to uncertainty.

Factors affecting our research and development expenses include, but are not limited to:

- competition from companies that have substantially greater assets and financial resources than we have;
- need for acceptance of our proposed products;
- ability to anticipate and adapt to a competitive market and rapid technological developments;
- amount and timing of operating costs and capital expenditures relating to outsourcing of manufacturing and management of pre-clinical and clinical trials;
- need to rely on multiple levels of outside funding due to the length of drug development cycles and governmental approved protocols associated with the pharmaceutical industry; and
- dependence upon key personnel including key independent consultants and advisors.

There can be no guarantee that our research and development expenses will be consistent from period to period. We may be required to accelerate or delay incurring certain expenses depending on the results of our studies and the availability of adequate funding.

We are subject to numerous risks inherent in conducting clinical trials.

We outsource the management of our clinical trials to third parties. Agreements with clinical investigators and medical institutions for clinical testing and with other third parties for data management services, place substantial responsibilities on these parties that, if unmet, could result in delays in, or termination of, our clinical trials. For example, if any of our clinical trial sites fail to comply with FDA-approved good clinical practices, we may be unable to use the data gathered at those sites. If these clinical investigators, medical institutions or other third parties do not carry out their contractual duties or obligations or fail to meet expected deadlines, or if the quality or accuracy of the clinical data they obtain is compromised due to their failure to adhere to our clinical protocols or for other reasons, our clinical trials may be extended, delayed or terminated, and we may be unable to obtain regulatory approval for, or successfully commercialize, our proposed products. Delays in recruitment, lack of clinical benefit or unacceptable side effects would delay or prevent the completion of our clinical trials.

We or our regulators may suspend or terminate our clinical trials for a number of reasons. We may voluntarily suspend or terminate our clinical trials if at any time we believe they present an unacceptable risk to the patients enrolled in our clinical trials or do not demonstrate clinical benefit. In addition, regulatory agencies may order the temporary or permanent discontinuation of our clinical trials at any time if they believe that the clinical trials are not being conducted in accordance with applicable regulatory requirements or that they present an unacceptable safety risk to the patients enrolled in our clinical trials.

Our clinical trial operations are subject to regulatory inspections at any time. If regulatory inspectors conclude that we or our clinical trial sites are not in compliance with applicable regulatory requirements for conducting clinical trials, we may receive reports of observations or warning letters detailing deficiencies, and we will be required to implement corrective actions. If regulatory agencies deem our responses to be inadequate, or are dissatisfied with the corrective actions we or our clinical trial sites have implemented, our clinical trials may be temporarily or permanently discontinued, we may be fined, we or our investigators may be precluded from conducting any ongoing or any future clinical trials, the government may refuse to approve our marketing applications or allow us to manufacture or market our products, and we may be criminally prosecuted.

The lengthy approval process as well as the unpredictability of future clinical trial results may result in our failing to obtain regulatory approval for our proposed products, which would materially harm our business, results of operations and prospects.

There are no assurances that we will be able to submit a pre-market application or obtain FDA approval in order to market and sell our products.

There can be no assurance that even if the clinical trial of any potential product candidate is successfully initiated and completed, that we will be able to submit a Biologics License Application (“BLA”) or New Drug Application (“NDA”) to the FDA, or that any BLA or NDA that we submit will be approved in a timely manner, if at all. If we are unable to submit a BLA or NDA with respect to any future product, or if such application is not approved by the FDA, we will be unable to commercialize that product. The FDA can and does reject BLAs and NDAs and may require additional clinical trials, even when product candidates performed well or achieved favorable results during initial clinical trials. If we fail to commercialize our product candidates and are unable to generate sufficient revenues to attain profitability our business will be adversely effected.

The manufacturing of stem cell-based therapeutic products is novel and dependent upon specialized key materials.

The manufacturing of stem cell-based therapeutic products is a complicated and difficult process, dependent upon substantial know-how and subject to the need for continual process improvements. We depend almost exclusively on third party manufacturers to supply our cells. In addition, our suppliers' ability to scale-up manufacturing to satisfy the various requirements of our planned clinical trials is uncertain. Manufacturing irregularities or lapses in quality control could have a material adverse effect on our business. Additionally, many of the materials that we use to prepare our cell-based products are highly specialized, complex and available from only a limited number of suppliers. The loss of one or more of these sources would likely delay our ability to conduct planned clinical trials and otherwise adversely affect our business.

We may be subject to litigation that will be costly to defend or pursue and uncertain in its outcome.

Our business may bring us into conflict with licensees, licensors, or others with whom we have contractual or other business relationships or with our competitors or others whose interests differs from ours. If we are unable to resolve these conflicts on terms that are satisfactory to all parties, we may become involved in litigation brought by or against such parties. Any litigation is likely to be expensive and may require a significant amount of management's time and attention, at the expense of other aspects of our business. The outcome of litigation is always uncertain, and in some cases could include judgments against us which could have a materially adverse effect on our business.

We may not be able to obtain necessary licenses to third-party patents and other rights.

A number of companies, universities and research institutions have filed patent applications or have received patents relating to technologies in our field. We cannot predict which, if any, of these applications will issue as patents or how many of these issued patents will be found valid and enforceable. There may also be existing issued patents on which we would infringe by the commercialization of our product candidates. If so, we may be prevented from commercializing these products unless the third party is willing to grant a license to us. We may be unable to obtain licenses to the relevant patents at a reasonable cost, if at all, and may also be unable to develop or obtain alternative non-infringing technology. If we are unable to obtain such licenses or develop non-infringing technology at a reasonable cost, our business could be significantly harmed. Also, any infringement lawsuits commenced against us may result in significant costs, divert our management's attention and result in an award against us for substantial damages, or potentially prevent us from continuing certain operations.

We may not be able to obtain government or third-party payor coverage and reimbursement.

Our ability to successfully commercialize our product candidates, if approved, depends to a significant degree on the ability of patients to be reimbursed for the costs of such products and related treatments. We cannot assure you that reimbursement in the U.S. or in foreign countries will be available for any products developed, or, if available, will not decrease in the future, or that reimbursement amounts will not reduce the demand for, or the price of, our products. There is considerable pressure to reduce the cost of therapeutic products. Government and other third party payors are increasingly attempting to contain health care costs by limiting both coverage and the level of reimbursement for new therapeutic products and by refusing, in some cases, to provide any coverage for uses of approved products for disease indications for which the FDA or other relevant authority has not granted marketing approval. Moreover, in some cases, government and other third party payors have refused to provide reimbursement for uses of approved products for disease indications for which the FDA or other relevant authority has granted marketing approval. Significant uncertainty exists as to the reimbursement status of newly approved health-care products or novel therapies such as ours. We cannot predict what additional regulation or legislation relating to the health care industry or third-party coverage and reimbursement may be enacted in the future or what effect such regulation or legislation may have on our business. If additional regulations are overly onerous or expensive or if healthcare related legislation makes our business more expensive or burdensome than originally anticipated, we may be forced to significantly downsize our business plans or completely abandon the current business model.

Our products may not be profitable due to manufacturing costs and our inability to receive favorable pricing.

Our products may be significantly more expensive to manufacture than other drugs or therapies currently on the market today due to a fewer number of potential manufacturers, greater level of needed expertise and other general market conditions affecting manufacturers of our proposed products. Even if we are able to receive approval for the reimbursement of our proposed products the amount of reimbursement may be significantly less than the manufacturing costs of our products. Additionally, other market factors may limit the price which we can charge for our proposed products while still being competitive. Accordingly, even if we are successful in developing our proposed products, we may not be able to charge a high enough price for us to earn a profit.

We are dependent on the acceptance of our products by the healthcare community.

Our product candidates, if approved for marketing, may not achieve market acceptance since hospitals, physicians, patients or the medical community, in general, may decide not to accept and utilize these products. The products that we are attempting to develop represent substantial departures from established treatment methods and will compete with a number of more conventional therapies marketed by major pharmaceutical companies. If the healthcare community does not accept our products for any reason, our business will be materially harmed.

We depend on key employees and consultants for our continued operations and future success.

We are highly dependent on our chief executive officer, chief scientific officer and outside consultants. Although we have entered into employment and consulting agreements with these parties, these agreements can be terminated at any time. The loss of any of these key employees or consultants could adversely affect our opportunities and materially harm our future prospects. In addition, we anticipate growth and expansion into areas and activities requiring additional expertise, such as clinical testing, regulatory compliance, manufacturing and marketing. We anticipate the need for additional management personnel as well as the development of additional expertise by existing management personnel. There is intense competition for qualified personnel in the areas of our present and planned activities, and there can be no assurance that we will be able to attract and retain the qualified personnel necessary for the development our business.

The employment contracts of certain key employees contain significant anti-termination provisions which could make changes in management difficult or expensive.

We have entered into employment agreements with Messrs. Daly and Lloyd Jones and Dr. Johe. Each of these employment agreements require the payment of severance, in the event certain conditions are met, if these individuals are terminated. These provisions will make the replacement of these employees very costly and could cause difficulty in effecting a change in control.

If we are unable to successfully execute our new refocused business strategy or integrate our new management team, our business could be harmed.

During 2016, the strategic direction of our company and executive management team have undergone significant change. In January 2016, we announced a new strategic refocusing to concentrate our resources on the NSI-189 small molecule program. As part of this refocusing, we announced that we will seek external funding to defray all, or

substantially all, of the costs associated with the NSI-566 stem cell therapy program. During 2016, we also received the resignation of our former President and Chief Executive Officer and founder. In addition, in February 2016, Richard Daly joined our company as our new President and Chief Executive Officer and was appointed to the board and, in May 2015, Jonathan Lloyd joined our company as our new Chief Financial Officer. Our success depends largely on the development and execution of our refocused business strategy by our senior management team as well as the acceptance of such refocused strategy and team by our stakeholders. The recent transitions in our executive team may be disruptive to our business, and if we are unable to manage orderly transitions, our business may be adversely affected. Additionally, since our management team consists of a limited number of individuals, the loss of these members of our senior management team or key personnel would likely harm our ability to implement our business strategy and respond to the rapidly changing market conditions in which we operate. There may be a limited number of persons with the requisite skills to serve in these positions, and we cannot assure you that we would be able to identify or employ such qualified personnel on acceptable terms, if at all. We cannot assure you that we will be able to successfully execute our refocused business strategy or that management will succeed in working together as a team. In the event we are unsuccessful, our business and prospects could be harmed.

Our competition has significantly greater experience and financial resources.

The biotechnology industry is characterized by rapid technological developments and a high degree of competition. We compete against numerous companies, many of which have substantially greater resources. Several such enterprises have initiated cell therapy research programs and/or efforts to treat the same diseases which we target. Given our current stage of development and resources, it may be extremely difficult for us to compete against more developed companies.

As a result, our proposed products could become obsolete before we recoup any portion of our related research and development and commercialization expenses. Competition in the biopharmaceutical industry is based significantly on scientific and technological factors. These factors include the availability of patent and other protection for technology and products, the ability to commercialize technological developments and the ability to obtain governmental approval for testing, manufacturing and marketing. We compete with specialized biopharmaceutical firms in the United States, Europe and elsewhere, as well as a growing number of large pharmaceutical companies