

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

FORM 10-Q

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

For the quarterly period ended **September 30, 2019**

OR

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

For the transition period from _____ to _____

Commission file number: **001-38418**

COCRYSTAL PHARMA, INC.

(Exact name of registrant as specified in its charter)

Delaware

*(State or Other Jurisdiction of
Incorporation or Organization)*

35-2528215

*(I.R.S. Employer
Identification No.)*

19805 N. Creek Parkway Bothell, WA

(Address of Principal Executive Office)

98011

(Zip Code)

Registrant's telephone number, including area code: **(786) 459-1831**

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (Sec.232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Emerging growth company

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

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

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	COCP	The Nasdaq Stock Market LLC (The Nasdaq Capital Market)

As of November 8, 2019, the number of outstanding shares of the registrant's common stock, par value \$0.001 per share, was 35,150,058.

COCRYSTAL PHARMA, INC.

FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 30, 2019

INDEX

Part I - FINANCIAL INFORMATION	
Item 1.	
<u>Condensed Consolidated Balance Sheets</u>	F-1
<u>Condensed Consolidated Statements of Operations</u>	F-2
<u>Condensed Consolidated Statements of Stockholders' Equity</u>	F-3
<u>Condensed Consolidated Statements of Cash Flows</u>	F-4
<u>Notes to the Condensed Consolidated Financial Statements</u>	F-5
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	3
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	7
Item 4. <u>Controls and Procedures</u>	7
Part II - OTHER INFORMATION	
Item 1. <u>Legal Proceedings</u>	8
Item 1.A. <u>Risk Factors</u>	9
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	9
Item 3. <u>Defaults Upon Senior Securities</u>	9
Item 4. <u>Mine Safety Disclosures</u>	9
Item 5. <u>Other</u>	9
Item 6. <u>Exhibits</u>	9
SIGNATURES	10

Part I – FINANCIAL INFORMATION

COCRYSTAL PHARMA, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except per share data)

	September 30, 2019 (unaudited)	December 31, 2018
Assets		
Current assets:		
Cash	\$ 5,994	\$ 2,723
Restricted cash	50	29
Accounts receivable	768	-
Prepaid expenses and other current assets	201	191
Total current assets	7,013	2,943
Property and equipment, net	459	384
Deposits	50	40
Operating lease right-of-use assets, net	720	-
Goodwill	65,195	65,195
Total assets	\$ 73,437	\$ 68,562
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 1,690	\$ 1,077
Deferred rent	-	3
Current maturities of finance lease liabilities	154	214
Current maturities of operating lease liabilities	171	-
Derivative liabilities	90	263
Total current liabilities	2,105	1,557
Long-term liabilities:		
Finance lease liabilities	18	117
Operating lease liabilities	569	-
Total long-term liabilities	587	117
Total liabilities	2,692	1,674
Commitments and contingencies		
Stockholders' equity:		
Common stock, \$.001 par value; 100,000 shares authorized as of September 30, 2019 and December 31, 2018; 31,621 and 29,938 shares issued and outstanding as of September 30, 2019 and December 31, 2018, respectively	32	30
Additional paid-in capital	258,128	253,949
Accumulated deficit	(187,415)	(187,091)
Total stockholders' equity	70,745	66,888
Total liabilities and stockholders' equity	\$ 73,437	\$ 68,562

See accompanying notes to condensed consolidated financial statements.

COCRYSTAL PHARMA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

(in thousands, except per share data)

	Three months ended September 30,		Nine months ended September 30,	
	2019	2018	2019	2018
Revenues:				
Collaboration revenue	\$ 492	\$ -	\$ 6,162	\$ -
Total Revenues	492	-	6,162	-
Operating expenses:				
Research and development	1,077	1,467	3,046	3,464
General and administrative	1,223	952	3,597	3,157
Total operating expenses	2,300	2,419	6,643	6,621
Loss from operations	(1,808)	(2,419)	(481)	(6,621)
Other (expense) income:				
Interest expense, net	(5)	-	(16)	(55)
Gain on settlement of mortgage note receivable	-	-	-	106
Loss on disposal of property and equipment	-	(61)	-	(61)
Change in fair value of derivative liabilities	33	129	173	410
Total other income, net	28	68	157	400
Loss before income taxes	(1,780)	(2,351)	(324)	(6,221)
Income tax benefit	-	483	-	1,459
Net loss	\$ (1,780)	\$ (1,868)	\$ (324)	\$ (4,762)
Net loss per common share:				
Loss per share, basic and diluted	\$ (0.06)	\$ (0.06)	\$ (0.01)	\$ (0.17)
Weighted average number of common shares outstanding, basic and diluted	31,621	29,923	31,201	27,360

See accompanying notes to condensed consolidated financial statements.

COCRYSTAL PHARMA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(unaudited)
(in thousands)

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount			
Balance as of December 31, 2018	29,938	\$ 30	\$ 253,949	\$ (187,091)	\$ 66,888
Stock-based compensation	-	-	33	-	33
Sale of common stock, net of transaction costs	1,683	2	3,926	-	3,928
Net income	-	-	-	2,971	2,971
Balance as of March 31, 2019	31,621	\$ 32	\$ 257,908	\$ (184,120)	\$ 73,820
Stock-based compensation	-	-	113	-	113
Net loss	-	-	-	(1,515)	(1,515)
Balance as of June 30, 2019	31,621	\$ 32	\$ 258,021	\$ (185,635)	\$ 72,418
Stock-based compensation	-	-	107	-	107
Net loss	-	-	-	(1,780)	(1,780)
Balance as of September 30, 2019	31,621	\$ 32	\$ 258,128	\$ (187,415)	\$ 70,745

	Common Stock		Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Equity
	Shares	Amount			
Balance as of December 31, 2017	24,275	\$ 24	\$ 243,419	\$ (138,043)	\$ 105,400
Stock-based compensation	-	-	105	-	105
Exercise of common stock options	127	-	184	-	184
Net loss	-	-	-	(1,551)	(1,551)
Balance as of March 31, 2018	24,402	\$ 24	\$ 243,708	\$ (139,594)	\$ 104,138
Stock-based compensation	-	-	107	-	107
Exercise of common stock options	1	-	1	-	1
Convertible debt instruments	1,085	1	2,061	-	2,062
Sale of common stock, net of transaction costs	4,435	5	7,679	-	7,684
Net loss	-	-	-	(1,343)	(1,343)
Balance as of June 30, 2018	29,923	\$ 30	\$ 253,556	\$ (140,937)	\$ 112,649
Stock-based compensation	-	-	120	-	120
Net loss	-	-	-	(1,868)	(1,868)
Balance as of September 30, 2018	29,923	\$ 30	\$ 253,676	\$ (142,805)	\$ 110,901

See accompanying notes to condensed consolidated financial statements.

COCRYSTAL PHARMA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)
(in thousands)

	Nine months ended September 30,	
	2019	2018
Operating activities:		
Net income (loss)	\$ (324)	\$ (4,762)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization expense	69	40
Amortization of right of use assets	114	-
Stock-based compensation	253	332
Interest expense, net	-	55
Loss on disposal of property and equipment	-	61
Payments on operating lease liabilities	(94)	-
Gain on mortgage note receivable	-	(106)
Change in deferred income tax	-	(1,459)
Change in fair value of derivative liabilities	(173)	(410)
Changes in operating assets and liabilities:		
Accounts receivable	(768)	-
Prepaid expenses and other current assets	(10)	(173)
Deposits	(10)	(18)
Accounts payable and accrued expenses	613	141
Deferred rent	(3)	(21)
Net cash provided by (used in) operating activities	(333)	(6,320)
Investing activities:		
Purchases of property and equipment	(144)	(13)
Long-term deposits	-	-
Proceeds from settlement of mortgage note receivable	-	1,400
Net cash (used in) provided by investing activities	(144)	1,387
Financing activities:		
Proceeds from issuance of common stock and warrants	3,928	7,684
Payments on finance lease liabilities	(159)	-
Proceeds from issuance of convertible notes	-	1,000
Proceeds from exercise of stock options	-	185
Net cash provided by financing activities	3,769	8,869
Net increase in cash and restricted cash	3,292	3,936
Cash and restricted cash at beginning of period	2,752	777
Cash and restricted cash at end of period	\$ 6,044	\$ 4,713
SUPPLEMENTAL DISCLOSURE OF NON-CASH FINANCING ACTIVITIES:		
Recognition of operating lease right-of-use assets and operating lease liabilities upon adoption of ASC Topic 842 <i>Leases</i>	\$ 833	\$ -
Issuance of commons stock upon conversion of notes payable	\$ -	\$ 2,062

See accompanying notes to condensed consolidated financial statements.

COCRYSTAL PHARMA, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Business

Cocrystal Pharma, Inc. (“we”, the “Company” or “Cocrystal”), a clinical stage biopharmaceutical company, has been developing novel technologies and approaches to create first-in-class and best-in-class antiviral drug candidates since its initial funding in 2008. Our focus is to pursue the development and commercialization of broad-spectrum antiviral drug candidates that will transform the treatment and prophylaxis of viral diseases in humans. By concentrating our research and development efforts on viral replication inhibitors, we plan to leverage our infrastructure and expertise in these areas.

On January 18, 2018, the Company’s Board of Directors (the “Board”) filed an amendment (the “Amendment”) with the Delaware Secretary of State to affect a one-for-thirty reverse split (the “Reverse Stock Split”) of the Company’s class of common stock. The Amendment took effect on January 24, 2018. The Reverse Stock Split did not change the authorized number of shares of common stock. Pursuant to the terms of the Company’s then outstanding convertible notes (see Note 7 – Convertible Notes Payable), its options and warrants have been proportionately adjusted to reflect the Reverse Stock Split. A proportionate adjustment was made to the per share exercise price, number of shares issued, and shares reserved for issuance under all of the Company’s equity compensation plans.

All per share amounts and number of shares in the condensed consolidated financial statements and related notes presented have been retroactively restated to reflect the Reverse Stock Split.

The Company’s activities since inception have principally consisted of acquiring potential product and technology rights, raising capital, and performing research and development. Successful completion of the Company’s development programs, obtaining regulatory approvals of its products and, ultimately, the attainment of profitable operations is dependent on future events, including, among other things, its ability to access potential markets, secure financing, develop a customer base, attract, retain and motivate qualified personnel, and develop and maintain strategic alliances. Through December 31, 2018, the Company has primarily funded its operations through equity offerings.

On January 31, 2019, the Company received an upfront non-refundable payment of \$4,000,000 and anticipates future payments for employees and research expense reimbursements over the term of our collaboration with Merck Sharp & Dohme Corp. (“Merck”), effective January 2, 2019 (refer to Note 10 – Licenses and Collaborations).

The Company’s historical operating results indicate substantial doubt exists related to the Company’s ability to continue as a going concern. The Company has no pharmaceutical products approved for sale, has not generated any revenues to date from pharmaceutical product sales, and has incurred significant operating losses since inception. The Company has incurred losses from operations of \$481,000 and \$6,621,000 in the nine months ended September 30, 2019 and 2018, respectively, and incurred losses from operations of \$1,808,000 and \$2,419,000 in the three months ended September 30, 2019 and 2018, respectively.

The Company will need to continue obtaining adequate capital to fund its operations until it becomes profitable on a consistent basis. The Company can give no assurances that the additional capital it is able to raise, if any, will be sufficient to meet its needs, or that any such financing will be obtainable on acceptable terms. If the Company is unable to obtain adequate capital, it could be forced to cease operations or substantially curtail its drug development activities. The Company expects to continue incurring substantial operating losses and negative cash flows from operations over the next several years during its pre-clinical and clinical development phases. The accompanying financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and the classification of liabilities should the Company be unable to continue as a going concern.

2. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles (“U.S. GAAP”) for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X set forth by the Securities and Exchange Commission (“SEC”). They do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The results of operations for the interim periods presented are not necessarily indicative of the results of operations for the entire fiscal year. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company’s annual report on Form 10-K for the year ended December 31, 2018 filed on April 1, 2019 (“Annual Report”).

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Cocrystal Pharma, Inc. and its wholly owned subsidiaries: RFS Pharma, LLC, Cocrystal Discovery, Inc., Cocrystal Merger Sub, Inc., Baker Cummins Corp. and Biozone Laboratories, Inc. Intercompany transactions and balances have been eliminated.

Segments

The Company operates in only one segment. Management uses cash flows as the primary measure to manage its business and does not segment its business for internal reporting or decision-making.

Use of Estimates

Preparation of the Company’s condensed consolidated financial statements in conformance with U.S. GAAP requires the Company’s management to make estimates and assumptions that impact the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities in the Company’s condensed consolidated financial statements and accompanying notes. The significant estimates in the Company’s condensed consolidated financial statements relate to the valuation of equity awards and derivative liabilities, recoverability of deferred tax assets, estimated useful lives of fixed assets, and forecast assumptions used in the valuation of intangible assets and goodwill. The Company bases estimates and assumptions on historical experience, when available, and on various factors that it believes to be reasonable under the circumstances. The Company evaluates its estimates and assumptions on an ongoing basis, and its actual results may differ from estimates made under different assumptions or conditions.

Concentrations of Credit Risk

Financial instruments that potentially subject the Company to significant concentrations of credit risk consist primarily of cash deposited in accounts held at two United States financial institutions, which may, at times, exceed federally insured limits of \$250,000 for each institution where accounts are held. At September 30, 2019 and December 31, 2018, our primary operating account held approximately \$5,994,000 and \$2,723,000 and our collateral account balance held at a different institution was \$50,000 and \$29,000, respectively. The Company has not experienced any losses in such accounts and believes it is not exposed to significant risks thereof.

Cash and Restricted Cash

The Company considers all highly liquid investments with an original maturity from the date of purchase of three months or less to be cash equivalents, and the Company held no cash equivalents as of September 30, 2019 and 2018, nor as of December 31, 2018.

The following table provides a reconciliation of cash and restricted cash reported within the condensed consolidated balance sheets that sum to the total of the same such amounts shown in the condensed consolidated statements of cash flows (in thousands):

	September 30, 2019	September 30, 2018
Cash	\$ 5,994	\$ 4,684
Restricted cash	50	29
Total cash and restricted cash shown in the statements of cash flows	<u>\$ 6,044</u>	<u>\$ 4,713</u>

Restricted cash represents amounts pledged as collateral for financing arrangements that are currently limited to the issuance of business credit cards. The restriction will end upon the conclusion of these financing arrangements.

Leases

Prior to January 1, 2019, the Company accounted for leases under Accounting Standards Codification (“ASC”) 840, Accounting for Leases. Effective from January 1, 2019, the Company adopted the guidance of ASC 842, *Leases*, which requires an entity to recognize a right-of-use asset and a lease liability for virtually all leases. The Company adopted ASC 842 using a modified retrospective approach. As a result, the comparative financial information has not been updated and the required disclosures prior to the date of adoption have not been updated and continue to be reported under the accounting standards in effect for those periods. The adoption of ASC 842 on January 1, 2019 resulted in the recognition of operating lease right-of-use assets and lease liabilities of approximately \$833,000 and did not result in a cumulative-effect adjustment to accumulated deficit.

Fair Value Measurements

FASB Accounting Standards Codification 820 (“ASC 820”) defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosures about fair value measurements. Fair value is defined under ASC 820 as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value under ASC 820 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

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

Level 2 — other significant observable inputs for the assets or liabilities through corroboration with market data at the measurement date.

Level 3 — significant unobservable inputs that reflect management’s best estimate of what market participants would use to price the assets or liabilities at the measurement date.

The Company categorizes its cash as Level 1 fair value measurements. The Company categorizes its warrants potentially settleable in cash as Level 3 fair value measurements. The warrants potentially settleable in cash are measured at fair value on a recurring basis and are being marked to fair value at each reporting date until they are completely settled or meet the requirements to be accounted for as component of stockholders’ equity. The warrants are valued using the Black-Scholes option pricing model as discussed in Note 9 – Warrants.

The following tables present a summary of fair values of assets and liabilities that are re-measured at fair value at each balance sheet date presented as of September 30, 2019 and December 31, 2018, and their placement within the fair value hierarchy as discussed above (in thousands):

Description	September 30, 2019	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Assets:				
Cash and restricted cash	\$ 6,044	\$ 6,044	\$ -	\$ -
Total assets	\$ 6,044	\$ 6,044	\$ -	\$ -
Liabilities:				
Warrants potentially settleable in cash (Note 9)	\$ 90	\$ -	\$ -	\$ 90
Total liabilities	\$ 90	\$ -	\$ -	\$ 90

Description	December 31, 2018	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)
Assets:				
Cash and restricted cash	\$ 2,752	\$ 2,752	\$ -	\$ -
Total assets	\$ 2,752	\$ 2,752	\$ -	\$ -
Liabilities:				
Warrants potentially settleable in cash (Note 9)	\$ 263	\$ -	\$ -	\$ 263
Total liabilities	\$ 263	\$ -	\$ -	\$ 263

The Company has not transferred any financial instruments into or out of Level 3 classification during the nine months ended September 30, 2019 and 2018. A reconciliation of the beginning and ending Level 3 liabilities is as follows (in thousands):

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)	
	September 30, 2019	September 30, 2018
Balance, January 1,	\$ 263	\$ 569
Change in fair value of warrants potentially settleable in cash (Note 9)	(173)	(410)
Balance at September 30,	\$ 90	\$ 159

Goodwill and In-Process Research and Development

We account for business combinations using the acquisition method, recording the acquisition-date fair value of total consideration over the acquisition-date fair value of net assets acquired as goodwill. Acquisition-related costs, including banking, legal, accounting, valuation, and other similar costs, are expensed in the periods in which the costs are incurred and included in loss from operations in the condensed consolidated financial statements. The results of operations of the acquired business are included in the condensed consolidated financial statements from the acquisition date.

In November 2014, goodwill and intangible assets for in-process research and development were recorded in connection with the acquisition of RFS Pharma, and have represented a series of awarded patents, filed patent applications and an in-process research programs acquired related to Hepatitis C compound development.

We evaluate indefinite-lived intangible assets and goodwill for impairment annually, as of November 30, or more frequently when events or circumstances indicate that impairment may have occurred. As part of the impairment evaluation, we may elect to perform an assessment of qualitative factors. If this qualitative assessment indicates that it is more likely than not that the fair value of the indefinite-lived intangible asset or the reporting unit (for goodwill) is less than its carrying value, we then would proceed with the quantitative impairment test to compare the fair value to the carrying value and record an impairment charge if the carrying value exceeds the fair value.

Fair value is typically estimated using an income approach based on the present value of future discounted cash flows. The significant estimates in the discounted cash flow model primarily include the discount rate, and rates of future revenue and expense growth and/or profitability of the acquired assets. In performing the impairment test, the Company considered, among other factors, the Company's intention for future use of acquired assets, analyses of historical financial performance and estimates of future performance of Cocrystal's product candidates.

In-process research and development assets are accounted for as indefinite-lived intangible assets and maintained on the balance sheet until either the underlying project is completed, or the asset becomes impaired. If the project is completed, the carrying value of the related intangible assets are amortized to cost of sales over the remaining estimated life of the asset(s), beginning in the period in which the project is completed. If the intangible asset becomes impaired or the related project is abandoned, the carrying value of the underlying intangible asset is written down to its fair value and an impairment charge is recorded in the period in which the impairment occurs and included in operating expenses under research and development within the relative condensed consolidated statement of operations.

The Company has a lead compound, CC-31244, for its Hepatitis C program, which was created at the Company's labs in Bothell, Washington, and was not part of the acquisition from RFS Pharma. In 2016, the Company initiated and completed a Phase 1A trial with compound CC-31244 and began a Phase 1B trial with CC-31244 that was completed in 2017.

In 2018, the Company began a Phase 2A clinical trial with CC-31244 and released interim results in January 2019. In late 2018, the Company concluded that given the success of CC-31244 in clinical trials, the Hepatitis C program would move forward solely with CC-31244 without any of the compounds acquired from RFS Pharma. As part of this decision, the Company abandoned all remaining in process research and development intangible assets recognized by the Company and thereafter, terminated its license with Emory University on December 6, 2018. This resulted in a \$53,905,000 impairment in the fourth quarter of 2018. At September 30, 2019 and December 31, 2018, there was no in-process research and development on the Company's condensed consolidated balance sheets.

At September 30, 2019 and December 31, 2018, the Company had goodwill of \$65,195,000 respectively included on the Company's condensed consolidated balance sheets. The Company has experienced a decrease in the stock price that has resulted in a possible goodwill impairment indicator. Since the Company stock has a history of volatility and low trading volume management will continue to monitor the goodwill for impairment and perform procedures on November 30, 2019.

Revenue Recognition

The Company recognizes revenue from research and development arrangements. In accordance with Accounting Standards Codification ("ASC") Topic 606-*Revenue from Contracts with Customers* ("Topic 606"), revenue is recognized when a customer obtains control of promised goods or services. The amount of revenue recognized reflects the consideration to which the Company expects to be entitled to receive in exchange for these goods and services.

On January 2, 2019, the Company entered into an Exclusive License and Research Collaboration Agreement (the “Collaboration Agreement”) with Merck Sharp & Dohme Corp. (“Merck”) to discover and develop certain proprietary influenza A/B antiviral agents. Under the terms of the Collaboration Agreement, Merck will fund research and development for the program, including clinical development, and will be responsible for worldwide commercialization of any products derived from the collaboration. As a result of this agreement, the Company recognized \$4,368,000 in revenues as consideration in exchange for conveyance of intellectual property rights at the signing of the agreement and also receives revenues for reimbursement of research and development activities related to its influenza A/B program. Research and development expenses reimbursed by Merck and recognized as revenue for the three and nine months ended September 30, 2019 were \$492,000 and \$1,794,000, respectively.

Income Taxes

The Company accounts for income taxes under the asset and liability method. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and tax bases of assets and liabilities and are measured using enacted tax rates and laws that are expected to be in effect when the differences are expected to be recovered or settled. Realization of deferred tax assets is dependent upon future taxable income. A valuation allowance is recognized if it is more likely than not that some portion or all of a deferred tax asset will not be realized based on the weight of available evidence, including expected future earnings. The Company recognizes an uncertain tax position in its financial statements when it concludes that a tax position is more likely than not to be sustained upon examination based solely on its technical merits. Only after a tax position passes the first step of recognition will measurement be required. Under the measurement step, the tax benefit is measured as the largest amount of benefit that is more likely than not to be realized upon effective settlement. This is determined on a cumulative probability basis. The full impact of any change in recognition or measurement is reflected in the period in which such change occurs. The Company elects to accrue any interest or penalties related to income taxes as part of its income tax expense.

As of September 30, 2019, the Company assessed its income tax expense based on its projected future taxable income for the year ended December 31, 2019 and therefore recorded no amount for income tax expense for the nine months ended September 30, 2019. In addition, the Company has significant deferred tax assets available to offset income tax expense due to net operating loss carry forwards which are currently subject to a full valuation allowance based on the Company’s assessment of future taxable income. Refer to our Annual Report on Form 10-K for the year ended December 31, 2018 for more information.

Stock-Based Compensation

The Company recognizes compensation expense using a fair value-based method for costs related to stock-based payments, including stock options in accordance with ASC 718. The fair value of options awarded to employees is measured on the date of grant using the Black-Scholes option pricing model and is recognized as expense over the requisite service period on a straight-line basis.

Use of the Black-Scholes option pricing model requires the input of subjective assumptions including expected volatility, expected term, and a risk-free interest rate. The Company estimates volatility using a blend of its own historical stock price volatility as well as that of market comparable entities since the Company’s common stock has limited trading history and limited observable volatility of its own. The expected term of the options is estimated by using the Securities and Exchange Commission Staff Bulletin No. 107’s *Simplified Method for Estimate Expected Term*. The risk-free interest rate is estimated using comparable published federal funds rates.

Common Stock Purchase Warrants and Other Derivative Financial Instruments

We classify as equity any contracts that require physical settlement or net-share settlement or provide us a choice of net-cash settlement or settlement in our own shares (physical settlement or net-share settlement) provided that such contracts are indexed to our own stock as defined in ASC 815-40, *Contracts in Entity’s Own Equity*. We classify as assets or liabilities any contracts that require net-cash settlement (including a requirement to net cash settle the contract if an event occurs and if that event is outside our control) or give the counterparty a choice of net-cash settlement or settlement in shares (physical settlement or net-share settlement). We assess classification of our common stock purchase warrants and other freestanding derivatives at each reporting date to determine whether a change in classification between assets and liabilities is required.

Recent Accounting Pronouncements

The following are new FASB Accounting Standards Updates (“ASUs”) that have been adopted by the Company as of September 30, 2019:

In 2018, the Company adopted ASC Topic 606, *Revenue from Contracts with Customers* (“Topic 606”), which had no impact on our consolidated financial statements and related footnote disclosures as of and for the year ended December 31, 2018 included in our Annual Report on Form 10-K. In January 2019, the Company recognized collaboration revenue in accordance with Topic 606 as presented in the condensed consolidated statement of operations for the nine months ended September 30, 2019.

In November 2018, the FASB issued ASU 2018-18, *Collaborative Arrangements (Topic 808): Clarifying the Interaction between Topic 808 and Topic 606*. This ASU provides guidance on whether certain transactions between collaborative arrangement participants should be accounted for as revenue under Topic 606 when the collaborative arrangement participant is a customer in the context of a unit of account. Accordingly, this amendment added unit of account guidance in Topic 606 when an entity is assessing whether the collaborative arrangement, or a part of the arrangement, is within the scope of Topic 606. In addition, the amendment provides certain guidance on presenting the collaborative arrangement transaction together with Topic 606. ASU 2018-18 is effective for fiscal years beginning after December 15, 2019 and interim periods within those fiscal years and early adoption is permitted. This ASU is to be applied retrospectively to the date of initial application of Topic 606. The Company adopted ASU 2018-18, in the fourth quarter of 2018, which had no impact on our consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2018, nor in the Company’s condensed consolidated financial statements as reported on this Form 10-Q for the nine months ended September 30, 2019.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, subsequently amended by ASU No. 2018-01, ASU No. 2018-10 and ASU No. 2018-11 (collectively, “ASC 842”), which requires lessees to recognize most leases on their balance sheets as a right-of-use (“ROU”) asset with a corresponding lease liability. Additional qualitative and quantitative disclosures are also required. The Company adopted the standard effective January 1, 2019 using the cumulative-effect adjustment transition method, which applies the provisions of the standard at the effective date without adjusting the comparative periods presented. The Company adopted the following practical expedients and elected the following accounting policies related to this standard update, a.) the option to not reassess prior conclusions related to the identification, classification and accounting for initial direct costs for leases that commenced prior to January 1, 2019, b.) short-term lease accounting policy election allowing lessees to not recognize ROU assets and liabilities for leases with a term of 12 months or less, and c.) the option to not separate lease and non-lease components for certain equipment lease asset categories. Adoption of ASC 842 resulted in the initial recognition of operating lease right-of-use assets and corresponding lease liabilities of approximately \$833,000 on the Company’s consolidated balance sheet. The Company’s accounting for finance leases (previously referred to as capital leases under ASC 840) remained substantially unchanged. The standard did not materially impact operating results or liquidity. Disclosures related to the amount, timing and uncertainty of cash flows arising from leases are included in Note 12 – Commitments and Contingencies.

The following are new FASB Accounting Standards Updates that have not been adopted by the Company as of September 30, 2019, and contain detail regarding the effective dates:

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*. This ASU eliminates, adds and modifies certain disclosure requirements for fair value measurements as part of its disclosure framework project. The standard is effective for all entities for financial statements issued for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently assessing this ASU and has not yet determined the impact ASU 2018-13 may have on its condensed consolidated financial statements.

Other recent authoritative guidance issued by the FASB (including technical corrections to the ASC), the American Institute of Certified Public Accountants, and the Securities and Exchange Commission (“SEC”) did not, or are not expected to, have a material impact on the Company’s condensed consolidated financial statements and related disclosures.

3. Property and Equipment

Property and equipment are recorded at cost and depreciated over the estimated useful lives of the underlying assets (three to five years) using the straight-line method. As of September 30, 2019, and December 31, 2018, property and equipment consists of (in thousands):

	September 30, 2019	December 31, 2018
Lab equipment (excluding equipment under finance leases)	\$ 1,073	\$ 945
Finance lease right-of-use lab equipment obtained in exchange for finance lease liabilities	347	347
Computer and office equipment	92	75
Total property and equipment	1,512	1,367
Less: accumulated depreciation and amortization	1,053	(983)
Property and equipment, net	\$ 459	\$ 384

Total depreciation and amortization expense were \$24,000 and \$69,000 for the three and nine months ended September 30, 2019, which includes amortization expense of \$17,000 and \$52,000 related to finance lease right-of-use lab equipment, respectively. Total depreciation and amortization expense were \$11,000 and \$40,000 for the three and nine months ended September 30, 2018, respectively, and included no amortization expense for finance lease right-of-use assets. For additional finance leases information, refer to Note 12 – Commitments and Contingencies.

4. Mortgage Note Receivable

In June 2014, the Company acquired a mortgage note from a bank for approximately \$2,626,000 which was collateralized by, among other things, the underlying real estate and related improvements. The property subject to the mortgage was owned by an entity managed by Daniel Fisher and his affiliate, 580 Garcia Properties LLC (the primary obligor of the note). The mortgage note had an original maturity date of August 1, 2032 and bore an interest rate of 7.24%.

Shortly thereafter in 2014, Daniel Fisher and his affiliate, 580 Garcia Properties LLC (the primary obligor of the note), brought multiple lawsuits against the Company involving its predecessors and subsidiaries. The lawsuits were later settled, and the complaints dismissed, without the Company making any payments to either Mr. Fisher or 580 Garcia Properties LLC. At the time of the note's acquisition, 580 Garcia Properties LLC was delinquent in its obligation to make monthly payments. In December 2015, the Company proceeded in accordance with rights of a secured real estate creditor under California law, to initiate private foreclosure proceedings. During 2017, the court enjoined the Company from proceeding with the foreclosure sale pending further developments in the litigation.

In February 2018, the Company, Daniel Fisher, and 580 Garcia Properties LLC resolved all outstanding claims and disputes. As part of this settlement, the Company received a payment of \$1,400,000 in exchange for the release of the mortgage note and deed of trust, resulting in a net gain of \$106,000 for disposal of the mortgage note receivable reflected in the condensed consolidated statement of operations for the nine months ended September 30, 2018.

5. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of the following (in thousands) as of:

	September 30, 2019	December 31, 2018
Accounts payable	\$ 1092	\$ 616
Accrued compensation	138	78
Accrued other expenses	460	383
Total accounts payable and accrued expenses	\$ 1,690	\$ 1,077

Accounts payable and accrued other expenses contain unpaid general and administrative expenses and costs related to research and development that have been billed and estimated unbilled, respectively, as of period-end.

6. Common Stock

As of September 30, 2019, the Company has authorized 100,000,000 shares of common stock, \$.001 par value per share. The Company had 31,620,646 and 29,938,363 shares issued and outstanding as of September 30, 2019 and December 31, 2018, respectively. The holders of common stock are entitled to one vote for each share of common stock held.

On January 18, 2018, the Company effected the Reverse Stock Split. See Note 1.

On May 3, 2018, the Company closed a public offering for gross proceeds and net proceeds of approximately \$8,428,000 and \$7,684,000, respectively. The Company sold 4,210,527 shares of common stock to the underwriter at approximately \$1.77 per share which the underwriter sold to the public at \$1.90 per share and issued the underwriter a warrant to purchase 84,211 shares of common stock at \$2.09 per share over a four year period beginning October 27, 2018. On May 14, 2018 the underwriter exercised the option to purchase an additional 225,000 shares of common stock solely to cover overallotments. As of September 30, 2019, the underwriter has no further option to purchase additional shares.

On March 13, 2019, the Company closed a private placement of 1,602,283 shares of its common stock and received gross proceeds of \$4,182,000, before deducting offering expenses and commissions, resulting in net proceeds of approximately \$3,584,000.

On March 20, 2019, the Company by written notice suspended at-the-market sales of its common stock pursuant to the Distribution Agreement, dated July 19, 2018 by and among the Company, Ladenburg, Barrington, and AGP. In December 2018, Ladenburg terminated its role as a party. The Company also terminated the engagement of Barrington as a sales agent under the Distribution Agreement effective March 21, 2019. The Distribution Agreement remains in place with respect to AGP, subject to the suspension of sales discussed above until further notice is provided by the Company to AGP. In January 2019, we sold 80,000 shares of common stock under the Distribution Agreement and received net proceeds of approximately \$344,000.

7. Convertible Notes Payable

The Company accounts for convertible notes payable (when it has determined that the embedded conversion options should not be bifurcated from their host instruments) in accordance with ASC 470-20, *Debt with Conversion and Other Options*.

On November 24, 2017 and January 31, 2018, the Company entered into securities purchase agreements with two investors, including the Company's former Chairman of the Board, pursuant to which the company sold an aggregate principal of \$1,000,000, and OPKO Health Inc., a related party, (collectively, the "Purchasers"), pursuant to which the Company sold an additional \$1,000,000, of its 8% convertible notes (collectively, "Convertible Notes") due on November 24, 2019 and January 31, 2020, respectively.

The Convertible Notes, with accrued interest, were convertible into common stock for \$8.10 per share at the option of the Purchasers. In the event the Company completed a financing in which the Company received at least \$10,000,000 in gross proceeds and issued common stock or common stock equivalents to the investor (a "Financing") or there is a change of control of the Company (or sale of substantially all of the Company's assets), the outstanding principal amount of the Convertible Notes would automatically convert. Upon the closing of a Financing, the conversion price of the Convertible Notes shall be the lesser of (i) \$8.10 per share or (ii) the price per share of the securities sold in the Financing.

The Company evaluated the embedded conversion features within the Convertible Notes under ASC 815-15 and ASC 815-40 to determine if they required bifurcation as a derivative instrument. The Company determined the embedded conversion features do not meet the definition of a derivative liability, and therefore, do not require bifurcation from the host instrument. In addition, the down-round provision under which the conversion price could be affected by future equity offerings, qualified for a scope exception from derivative accounting with the Company's early adoption of ASU 2017-11, *Simplifying Accounting for Certain Financial Instruments with Characteristics of Liabilities and Equity*, during the year ended December 31, 2017. Since the embedded conversion features were not considered derivatives, the convertible notes were accounted for in accordance with ASC 470-20, *Debt with Conversion and Other Options*.

In May 2018, the Company completed a financing and issued a total of 4,435,527 shares of common stock at \$1.90 per share, for gross proceeds and net proceeds of \$8,428,000 and \$7,680,000, respectively. Although the total gross financing amount did not contractually effectuate the conversion feature of the Convertible Notes' securities purchase agreements, the Company allowed Purchasers to convert the Convertible Notes to common stock at the \$1.90 per share price of the May 2018 financing. All outstanding 8% convertible notes were converted to shares of common stock in May 2018 at the aggregate amount of the principal and accrued interest of for approximately \$2,062,000 as of the date of conversion, for a total of 1,085,105 common shares issued. The conversion was approved by disinterested members of the Company's Board of Directors.

8. Stock Based Awards

Equity Incentive Plans

The Company adopted an equity incentive plan in 2007 (the "2007 Plan") under which 1,786,635 shares of common stock had been reserved for issuance to employees and nonemployee directors and consultants of the Company. The Company no longer issues any awards under the 2007 Plan. Holders of outstanding incentive stock options granted under the 2007 Plan are eligible to purchase shares of the Company's common stock at an exercise price equal to no less than the fair market value of such stock on the date of grant. The maximum term of options granted under the 2007 Plan was ten years.

The Company adopted a second equity incentive plan in 2015 (the "2015 Plan") under which, as amended, 5,000,000 (including 1,038,570 initially transferred from the 2007 Plan) shares of common stock have been reserved for issuance to employees, and nonemployee directors and consultants of the Company. Recipients of incentive stock options granted under the 2015 Plan shall be eligible to purchase shares of the Company's common stock at an exercise price equal to no less than the estimated fair market value of such stock on the date of grant. The maximum term of options granted under the 2015 Plan is ten years. As of September 30, 2019, 3,588,377 options remain available for future grants under the 2015 Plan.

The following table summarizes stock option transactions for the 2007 Plan and 2015 Plan, collectively, for the nine months ended September 30, 2019 (in thousands, except per share amounts):

	Number of Shares Available for Grant	Total Options Outstanding	Weighted Average Exercise Price	Aggregate Intrinsic Value
Balance at December 31, 2018	873	1,351	\$ 5.73	\$ 788
Exercised	-	-	-	-
Granted	2,295	-	-	-
Cancelled	420	(420)	9.24	-
Balance at September 30, 2019	<u>3,588</u>	<u>931</u>	<u>\$ 4.14</u>	<u>\$ -</u>

On June 21, 2019, the Company held its annual shareholder meeting and voted to increase the number of shares reserved and available for grant under the amended 2015 Plan by 2,294,762 shares of common stock. No options were granted during the nine months ended September 30, 2019, nor the nine months ended September 30, 2018.

The Company accounts for share-based awards to employees and nonemployees directors and consultants in accordance with the provisions of ASC 718, *Compensation—Stock Compensation*, and under the recently issued guidance following FASB's pronouncement, ASU 2018-07, *Compensation—Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting*. Under ASC 718, and applicable updates adopted, share-based awards are valued at fair value on the date of grant and that fair value is recognized over the requisite service, or vesting, period. The Company values its equity awards using the Black-Scholes option pricing model, and accounts for forfeitures when they occur. For the three and nine months ended September 30, 2019 and 2018, equity-based compensation expense recorded was \$108,000 and \$120,000, and \$253,000 and \$332,000, respectively.

As of September 30, 2019, there was approximately \$1,277,000 of total unrecognized compensation expense related to non-vested stock options that is expected to be recognized over a weighted average period of 1.6 years. For options granted and outstanding, there were 930,708 options outstanding which were fully vested or expected to vest, with an aggregate intrinsic value of \$0, a weighted average exercise price of \$4.14, and weighted average remaining contractual term of 8.3 years at September 30, 2019. Of those outstanding, vested and exercisable options totaled 319,458 options, with an aggregate intrinsic value of \$0. These options had a weighted average exercise price of \$6.75 per share and a weighted-average remaining contractual term of 6.9 years at September 30, 2019.

The aggregate intrinsic value of outstanding and exercisable options at September 30, 2019 was calculated based on the closing price of the Company's common stock as reported on The Nasdaq Capital Market on June 28, 2019 of \$2.35 per share less the exercise price of the options. The aggregate intrinsic value is calculated based on the positive difference between the closing fair market value of the Company's common stock and the exercise price of the underlying options.

Common Stock Reserved for Future Issuance

The following table presents information concerning common stock available for future issuance (in thousands) as of:

	September 30, 2019	September 30, 2018
Stock options issued and outstanding	931	426
Shares authorized for future option grants	3,588	1,813
Warrants outstanding	243	243
Total	<u>4,762</u>	<u>2,482</u>

9. Warrants

The following is a summary of activity in the number of warrants outstanding to purchase the Company's common stock for the nine months ended September 30, 2019 (in thousands):

	Warrants Accounted for as: Equity		Warrants Accounted for as: Liabilities		Total
	May 2018 Warrants		October 2013 Warrants	January 2014 Warrants	
Outstanding, December 31, 2018	84		26	133	243
Exercised	-		-	-	-
Granted	-		-	-	-
Expired	-		-	-	-
Outstanding, September 30, 2019	<u>84</u>		<u>26</u>	<u>133</u>	<u>243</u>
Expiration date:	October 27, 2022		October 24, 2023	January 16, 2024	

The following is a summary of activity in the number of warrants outstanding to purchase the Company's common stock for the nine months ended September 30, 2018 (in thousands):

	Warrants accounted for as: Equity		Warrants accounted for as: Liabilities		Total
	May 2018 warrants	April 2013 warrants	October 2013 Series A warrants	January 2014 warrants	
Outstanding, December 31, 2017	-	50	26	133	209
Warrants Issued	84	-	-	-	84
Warrants Expired	-	(50)	-	-	(50)
Warrants exercised	-	-	-	-	-
Outstanding, September 30, 2018	<u>84</u>	<u>-</u>	<u>26</u>	<u>133</u>	<u>243</u>
Expiration date	October 27, 2022	April 25, 2018	October 24, 2023	January 16, 2024	

Warrants consist of equity-classified warrants and warrants with the potential to be settled in cash, which are liability-classified warrants. As of September 30, 2019, and 2018, 159,164 warrants are accounted for as liabilities and 84,211 warrants are accounted for as equity.

Warrants Classified as Equity

Equity-classified warrants consist of stand-alone warrants with rights to buy shares of the Company at a pre-designated price on or before the date of expiration, irrespective of the market price. These purchase warrants are not attached to any debt or equity instruments, thus considered freestanding, and there are no circumstances under ASC 815 that require the warrants to be classified as liabilities or as derivatives. Thus, our May 2018 warrants will be classified as equity, and their value will be carried in the additional paid-in capital account in the stockholders' equity section of the balance sheet.

These warrants were granted to the underwriters and investment brokers for services provided related to the Company's May 2018 equity financing, and collectively grant the right to buy 84,211 shares of our stock at \$2.09 per share for up to four years until expiration from the commencement date of October 27, 2018.

Warrants Classified as Liabilities

Liability-classified warrants consist of warrants issued by Biozone in connection with equity financings in October 2013 and January 2014, which were assumed by the Company in connection with its merger with Biozone in January 2014. Warrants accounted for as liabilities have the potential to be settled in cash or are not indexed to the Company's own stock.

The estimated fair value of outstanding warrants accounted for as liabilities is determined at each balance sheet date. Any decrease or increase in the estimated fair value of the warrant liability since the most recent balance sheet date is recorded in the condensed consolidated statement of operations as changes in fair value of derivative liabilities.

The fair value of the warrants classified as liabilities is estimated using the Black-Scholes option-pricing model with the following inputs as of September 30, 2019:

	October 2013 Warrants	January 2014 Warrants
Strike price	\$ 15.00	\$ 15.00
Expected dividend yield	0.00%	0.00%
Contractual term (years)	4.10	4.30
Cumulative volatility	89.59%	88.08%
Risk-free rate	1.58%	1.74%

The fair value of the warrants classified as liabilities is estimated using the Black-Scholes option-pricing model with the following inputs as of September 30, 2018:

	October 2013 warrants	January 2014 warrants
Strike price	\$ 15.00	\$ 15.00
Expected dividend yield	0.00%	0.00%
Expected term (years)	5.07	5.30
Cumulative volatility %	87.95%	87.99%
Risk-free rate %	2.73%	2.74%

As of the third quarter in 2019, the Company's available historical market prices and price volatility exceeded the remaining contractual terms of outstanding warrants accounted for as liabilities. Therefore, as of September 30, 2019, the Company calculated the cumulative volatility percentage used in the Black-Scholes option-pricing model based on its own historical price volatility. In prior periods, including as of September 30, 2018, the Company estimated volatility using a blend of its own historical stock price volatility as well as that of market comparable entities since the Company's common stock had limited trading history and limited observable volatility of its own. The expected life assumption is based on the remaining contractual terms of the warrants. The risk-free rate is based on the zero-coupon rates in effect at the balance sheet date. The dividend yield used in the pricing model is zero, because the Company has no present intention to pay cash dividends.

10. Licenses and Collaborations

Merck Sharp & Dohme Corp.

On January 2, 2019, the Company entered into an Exclusive License and Research Collaboration Agreement (the "Collaboration Agreement") with Merck Sharp & Dohme Corp. ("Merck") to discover and develop certain proprietary influenza A/B antiviral agents. Under the terms of the Collaboration Agreement, Merck will fund research and development for the program, including clinical development, and will be responsible for worldwide commercialization of any products derived from the collaboration. Cocystal received an upfront payment of \$4,000,000 and is eligible to receive payments related to designated development, regulatory and sales milestones with the potential to earn up to \$156,000,000, as well as royalties on product sales. Merck can terminate the Collaboration Agreement at any time prior to the first commercial sale of the first product developed under the Collaboration Agreement, in its sole discretion, without cause.

As a result of this agreement, the Company recognized revenue of \$4,368,000 as consideration in exchange for conveyance of intellectual property rights at the time of the agreement signing in accordance with ASC Topic 606, *Revenue from Contracts with Customers*, which included the \$4,000,000 milestone upfront payment, since received and recognized as collaboration revenues during the first quarter of 2019.

Research and development expenses related to our influenza A/B program which are reimbursable by Merck within 45 days of period-end under the terms of the Collaboration Agreement and recognized as collaboration revenue were \$492,000 and \$1,794,000 for the three and nine months ended September 30, 2019, respectively. Total revenue of \$6,162,000 included in the condensed consolidated statement of operations for the nine months ended September 30, 2019 is related to this Collaboration Agreement. As of September 30, 2019, \$768,000 is due from Merck under these agreements.

National Institute of Health

Cocystal has two Public Health Biological Materials License Agreements with the National Institute of Health. The original License Agreements were dated August 31, 2010 and amended on November 6, 2013. The materials licensed are being used in Norovirus assays to screen potential antiviral agents in our library.

11. Net Income (Loss) per Share

The Company accounts for and discloses net income (loss) per common share in accordance with FASB ASC Topic 260, *Earnings Per Share*. Basic income (loss) per common share is computed by dividing income (loss) attributable to common stockholders by the weighted average number of common shares outstanding. Diluted net income (loss) per common share is computed by dividing net income (loss) attributable to common stockholders by the weighted average number of common shares that would have been outstanding during the period assuming the issuance of common stock for all potential dilutive common shares outstanding. Potential common shares consist of shares issuable upon the exercise of stock options and warrants and the conversion of convertible notes payable.

12. Commitments and Contingencies

Commitments

In the ordinary course of business, the Company enters into non-cancelable leases to purchase equipment and for its facilities, including related party leases (see Note 13 – Transactions with Related Parties). As per Note 2, leases are accounted for as operating leases or finance leases, in accordance with ASC 842, *Leases*.

Operating Leases

The Company leases office space in Miami, Florida and laboratory space in Bothell, Washington under operating leases that expire on August 31, 2021 and January 31, 2024, respectively. The Company recently signed an amendment to the Bothell, Washington lease agreement by extending the lease term for a period of sixty months from February 2019 through January 2024. For operating leases, the weighted average discount rate is 8.0% and the weighted average remaining lease term is 4.2 years.

The following table summarizes the Company's maturities of operating lease liabilities, by year and in aggregate, as of September 30, 2019 (in thousands):

2019 (excluding the nine months ended September 30, 2019)	\$	55
2020		226
2021		213
2022		178
2023		183
Thereafter		15
Total operating lease payments		870
Less: present value discount		(130)
Total operating lease liabilities	\$	740

The operating lease liabilities summarized above do not include variable common area maintenance (CAM) charges, which are contractual liabilities under the Company's Bothell, Washington lease. CAM charges for the Bothell, Washington facility are calculated annually based on actual common expenses for the building incurred by the lessor and proportionately billed to tenants based on leased square footage. For the nine months ended September 30, 2019 and 2018, approximately \$60,000 and \$49,000 of variable lease expense (CAM) was included in general and administrative operating expenses on the condensed consolidated statements of operations, respectively.

The minimum lease payments above include the amounts that would be paid if the Company maintains its Bothell lease for the five-year term, starting February 2019. The Company has the right to terminate this lease after three years on January 31, 2022, by giving prior notice at least nine months before the early termination date and by paying a termination fee equal to the sum of unamortized leasing commissions and reimbursement for tenant improvements provided by the landlord amortized at 8.0% over the extended term.

On September 1, 2018, the Company entered into a lease agreement with a limited liability company controlled by Dr. Phillip Frost, a director and a principal shareholder of the Company (see Note 13 – Transactions with Related Parties). The lease term is three years with an optional three-year extension. On an annualized basis, straight-line rent expense is approximately \$58,000, including fixed and estimable fees and taxes.

The offices and laboratory spaces in Tucker, Georgia were leased from a limited liability company owned by one of Cocrystal's former directors, Dr. Raymond Schinazi and previously leased on a month to month basis (see Note 13 – Transactions with Related Parties). The Company closed its offices and laboratory in Tucker, Georgia, and the final lease-related payment was made in October 2018.

As of September 30, 2019, right-of-use assets obtained in exchange for operating lease liabilities and amortization expense recognized for operating leases was \$833,000 and \$114,000 respectively. For the nine months ended September 30, 2019 and 2018, operating lease expense, excluding short-term leases, finance leases and CAM charges, totaled approximately \$169,000 and \$129,000, respectively. Additionally, the Company recognized short-term operating lease expense of \$9,000 during the nine months ended September 30, 2019, and cash paid for amounts included in the measurement of lease liabilities for operating leases as operating cash out flows in the same period.

Finance Leases

In November 2018, the Company entered into two lease agreements to acquire lab equipment with 18 monthly payments of \$18,000 payable through May 27, 2020 and 36 monthly payments of \$1,000 payable through November 21, 2021, respectively. For finance leases, the weighted average discount rate is 8.0% and the weighted average remaining lease term is 1.1 years.

The following table summarizes the Company's maturities of finance lease liabilities, by year and in aggregate, as of September 30, 2019 (in thousands):

2019 (excluding the nine months ended September 30, 2019)	\$	58
2020		106
2021		15
Total finance lease payments		179
Less: present value discount		(7)
Total finance lease liabilities	\$	<u>172</u>

The leased lab equipment is depreciable over five years and is presented net of accumulated depreciation on the condensed consolidated balance sheets under property and equipment. As of September 30, 2019, total right-of-use lab equipment and accumulated depreciation recognized under finance leases is \$347,000 and \$58,000, respectively, and depreciation expense for the nine months ended September 30, 2019 was \$52,000. As of December 31, 2018, total right-of-use assets exchanged for finance lease liabilities was \$347,000 and accumulated depreciation for lab equipment under finance leases was \$6,000.

At September 30, 2019, the aggregate outstanding balance of finance lease liabilities, current and long-term, is \$172,000 and the Company expects to pay future interest charges of \$7,000 over the remaining finance lease terms. For the nine months ended September 30, 2019, the Company paid \$159,000 and \$16,000 in principal and interest, respectively, totaling financing cash out flows of \$175,000 for amounts included in the measurement of lease liabilities for finance leases and added back to net income the \$16,000 of interest expense under cash flows from operating activities. The Company had no leases considered to be finance leases as of September 30, 2018.

Contingencies

From time to time, the Company is a party to, or otherwise involved in, legal proceedings arising in the normal course of business. As of the date of this report, except as described below, the Company is not aware of any proceedings, threatened or pending, against it which, if determined adversely, would have a material effect on its business, results of operations, cash flows or financial position.

On September 20, 2018, a class action lawsuit was filed with the United States District Court for the District of New Jersey as a complaint against the Company, certain current and former executive officers and directors of the Company and the other defendants named therein for violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. Additionally, the complaint alleges that certain current and former executive officers of the Company violated Section 20(a) of the Exchange Act. The class consists of the persons and entities who purchased the Company's common stock during the period from September 23, 2013 through September 7, 2018. The plaintiff seeks damages, pre-judgment and post-judgment interest, reasonable attorneys' fees, expert fees and other costs. On June 25, 2019, the plaintiffs in the class action lawsuit filed an amended class action complaint.

On January 16, 2019, Ms. Susan Church, a stockholder of the Company, filed with the United States District Court for the Western District of Washington a derivative suit against certain current and former executive officers and directors of the Company alleging breach of fiduciary duties, unjust enrichment, waste of corporate assets, and violations of the rules governing proxy solicitation. Church seeks, among other things, money damages, disgorgement of profits from alleged wrongful conduct, including cash bonuses, pre-judgment and post-judgment interest, reasonable attorneys' fees, expert fees and other costs. The attorneys have agreed to a stay of the derivative suit pending resolution of the class action.

On September 7, 2018, the SEC filed with the United States District Court for the Southern District of New York a complaint against Dr. Philip Frost, a director and principal stockholder of the Company, a trust Dr. Frost controls and OPKO Health, Inc., a stockholder of the Company, of which Dr. Frost is the Chief Executive Officer, as well as other defendants named therein. On January 10, 2019, the District Court entered final judgments against these defendants on their consent without admitting or denying the allegations set forth in the complaint. Dr. Frost was permanently enjoined from violating a certain anti-fraud provision of the Securities Act of 1933, future violations of Section 13(d) of the Exchange Act and Rule 13d-1(a) thereunder and participating in penny stock offerings subject to certain exceptions.

In November 2017, Lee Pederson, a former Biozone lawyer, filed a lawsuit in Minnesota against co-defendants the Company, Dr. Phillip Frost, OPKO Health, Inc. and Brian Keller for various allegations. On September 13, 2018, the United States District Court granted the Company and its co-defendants' motion to dismiss Pederson's amended complaint. On October 11, 2018, Pederson filed a notice of appeal with the United States Court of Appeals for the Eighth Circuit.

On July 8, 2019, Mr. Pederson filed a lawsuit in the U.S. District Court in Minnesota against the Company, Dr. Frost and Mr. Daniel Fisher. See Note 4 for information on Mr. Fisher. While the Company, to its knowledge, has not been served, it has obtained a copy of the complaint. In his complaint, Pederson alleges tortious interference by the Company and Dr. Frost with the collaboration agreement between Mr. Pederson and Mr. Fisher. Mr. Pederson seeks damages in the amount of \$800,000 or such other amount as may be determined at trial.

While the Company intends to defend itself vigorously from the claims in the aforementioned disputes, it is unable to predict the outcome of these legal proceedings. Any potential loss as a result of these legal proceedings cannot be reasonably estimated. As a result, the Company has not recorded a loss contingency for any of the aforementioned claims.

We were recently notified that our insurance company has initially declined to cover the class action and related derivative action described above. The insurance company had previously delayed reimbursing our legal fees related to the SEC subpoena we received in 2015 requesting information, but ultimately paid us that sum and never declined coverage. We have retained specialized insurance legal counsel to analyze and strategize our options. While we cannot quantify the amount of litigation costs, they are likely to be material as would be any adverse judgment or settlement amount.

13. Transactions with Related Parties

Beginning November 2014 to October 2018, the Company leased its Tucker, Georgia facility from a limited liability company owned by one of Cocrystal's former directors and principal shareholder, Dr. Raymond Schinazi. As of October 2018, the Company cancelled the leasing arrangement and closed its office and research lab in Tucker, Georgia. Total rent and other expenses paid in connection with this lease were \$0 and \$33,000 for the nine months ended September 30, 2019 and 2018, respectively.

In September 2018, the Company leased administrative offices from a limited liability company owned by one of the Company's directors and principal shareholder, Dr. Phillip Frost. The operating lease term is three years with an optional three-year extension. On an annualized basis, straight-line lease expense, including taxes and fees, for this location is approximately \$58,000. In September 2018, the Company paid a lease deposit of \$4,000 and total amounts paid in connection with this operating lease were \$42,000 and \$5,000 for the nine months ended September 30, 2019 and 2018, respectively.

As further explained in Note 7 – Convertible Notes Payable, on November 24, 2017, the Company entered into a securities purchase agreement with a company significantly owned by the Company's former Chairman of the Board and principal shareholder, Dr. Schinazi, pursuant to which the Company sold a principal amount of \$500,000 of 8% convertible notes due November 24, 2019. On January 31, 2018, the Company entered into a securities purchase agreement with OPKO Health, Inc. (the "Purchaser"), a Company affiliated with Dr. Frost, pursuant to which the Company borrowed \$1,000,000 from the Purchaser in exchange for issuing the Purchaser an 8% convertible note due January 31, 2020.

All 8% convertible notes, including accrued interest, were converted to common stock shares in May 2018 at \$1.90 per share. Dr. Schinazi's affiliated Company received 273,367 shares for its 8% convertible notes balance of approximately \$519,000, and OPKO Health, Inc., affiliated with Dr. Frost, received 538,544 shares for its 8% convertible notes balance of approximately \$1,023,000 upon conversion. In the condensed consolidated balance sheets, as of September 30, 2019 and December 31, 2018, no amounts remain in convertible notes payable due to related parties.

14. Subsequent Events

On November 4, 2019, we closed a public offering receiving gross proceeds of approximately \$3 million and net proceeds of \$2.6 million. We sold 3,529,412 shares of common stock to the underwriter at approximately \$0.79 per share which the underwriter sold to the public at \$0.85 per share. The underwriter has a 45 day option to purchase an additional 529,411 shares of common stock solely to cover overallotments.

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

Overview

Cocrystal Pharma, Inc. (the "Company" or "Cocrystal") is a clinical stage biotechnology company seeking to discover and develop novel antiviral therapeutics as treatments for serious and/or chronic viral diseases. We employ unique structure-based technologies and Nobel Prize winning expertise to create first- and best-in-class antiviral drugs. These technologies are designed to efficiently deliver small molecule therapeutics that are safe, effective and convenient to administer. We have identified promising preclinical and early clinical stage antiviral compounds for unmet medical needs including influenza virus, Hepatitis C virus ("HCV"), and norovirus infections.

Cocrystal Pharma, Inc. (the "Company" or "Cocrystal") is a biotechnology company seeking to discover and develop novel antiviral therapeutics as treatments for serious and/or chronic viral diseases. We employ unique structure-based technologies and Nobel Prize winning expertise to create first- and best-in-class antiviral drugs. These technologies are designed to efficiently deliver small molecule therapeutics that are safe, effective and convenient to administer. We have identified promising preclinical and early clinical stage antiviral compounds for unmet medical needs including influenza, Hepatitis C virus ("HCV"), and norovirus infections.

The Company operates in one segment. Management uses cash flows as the primary measure to manage its business and does not segment its business for internal reporting or decision-making.

Research and Development Update

During the nine months ended September 30, 2019, the Company focused its research and development efforts primarily in three areas: (i) Hepatitis C, (ii) Influenza and (iii) Norovirus Infections.

Hepatitis C

CC-31244, our HCV Non-Nucleoside Polymerase Inhibitor ("NNI"), is a potential best-in-class pan-genotypic inhibitor of NS5B polymerase for the treatment of HCV infection. It has the potential to be an important component in an all-oral ultra-short HCV combination therapy. The Company filed an Investigational New Drug ("IND") application with the U.S. Food and Drug Administration ("FDA") on February 28, 2018 and received notice from the FDA on March 29, 2018 that its IND was now open and the Company was cleared to initiate its Phase 2a clinical study evaluating CC-31244 for the treatment of HCV infected individuals.

In June 2018, the Company began enrollment in and initiation of patient dosing in its Phase 2a clinical study evaluating CC-31244 for the treatment of HCV infected individuals and completed the enrollment in September 2018. The Phase 2a open-label study was designed to evaluate the safety, tolerability and preliminary efficacy of CC-31244 in combination with Epclusa, an approved HCV drug. Patients are treated with CC-31244 and Epclusa for two weeks and then Epclusa alone for an additional four weeks.

On January 22, 2019, the Company announced safety and preliminary efficacy data for the Phase 2a clinical study evaluating CC-31244 for the treatment of HCV infected individuals. All subjects had completed the six-week treatment regimen. The treatment was well tolerated with no study discontinuations due to adverse events. Eight of 12 subjects achieved the primary efficacy endpoint of sustained virologic response at 12 weeks after completion of treatment (SVR12). SVR12 is defined as undetectable virus in blood 12 weeks after completion of treatment and is considered a virologic cure. The trial was conducted at the Institute of Human Virology, University of Maryland School of Medicine and the final study report is expected during the second half of 2019. New data indicates patients that achieved sustained virologic response had significantly higher frequencies of terminally differentiated effector memory CD8+ T cells compared with those who relapsed, allowing identification of patients more likely to respond to ultrashort treatment.

The trial was conducted at the Institute of Human Virology, University of Maryland School of Medicine and the final study report is expected during first quarter of 2020.

In addition, in October 2018, the Company signed a Clinical Trial Agreement for an investigator-initiated study with the Humanity & Health Research Centre in Hong Kong, China. The Phase 2a study of CC-31244 for the treatment of HCV, which commenced in May 2019, is being sponsored and conducted by the Humanity & Health Research Centre in Hong Kong under the guidance of Dr. George Lau, MBBS (HKU), M.D. (HKU), FRCP (Edin, Lond), FHKAM (Med), FHKCP, FAASLD, Chairman of Humanity and Health Medical Centre, Hong Kong. The Company has provided CC-31244 for use in the Phase 2a study. The Phase 2a open-label study will evaluate the safety, tolerability and preliminary efficacy of Cocrystal's CC-31244 in combination with Sofosbuvir and Daclatasvir with or without a protease inhibitor, for the treatment of HCV.

In December 2018, the Company voluntarily terminated a license agreement with Emory University covering the patents and patent applications for HCV inhibitors, which are not essential to our HCV program.

The Company is in partnership discussions for further clinical development of CC-31244.

Influenza A

We have several preclinical candidates under development for the treatment of influenza infection. CC-42344, a novel PB2 inhibitor, has been selected as a preclinical lead. This candidate binds to a highly conserved PB2 site of influenza polymerase complex (PB1: PB2: PA) and exhibits a novel mechanism of action. CC-42344 showed excellent antiviral activity against influenza A strains, including avian pandemic strains and Tamiflu resistant strains, and has favorable pharmacokinetic profiles. We are currently conducting additional preclinical IND enabling studies and plan to initiate a Phase 1 study during 2020.

Influenza A/B

On January 2, 2019, the Company entered into an Exclusive License and Research Collaboration Agreement (the "Collaboration Agreement") with Merck Sharp & Dohme Corp. ("Merck") to discover and develop certain proprietary influenza A/B antiviral agents. Under the terms of the Collaboration Agreement, Merck is funding research and development for the program, including clinical development, and will be responsible for worldwide commercialization of any products derived from the collaboration. See Note 10 – Licenses and Collaborations in the notes to the condensed consolidated financial statements under Item I, above, for more information. The Company has identified novel inhibitors effective against both strains A and B that are in the preclinical stage. Several of these have potencies approaching single digit nanomolar.

Norovirus Infections

We continue to identify and develop non-nucleoside polymerase inhibitors using the Company's proprietary structure-based drug design technology platform.

Results of Operations for the Three and Nine Months Ended September 30, 2019 compared to the Three and Nine Months Ended September 30, 2018

Revenues

Collaboration revenue recorded for the three and nine months ended September 30, 2019 was \$492,000 and \$6,162,000, respectively, compared with \$0 for the three and nine months ended September 30, 2018. The 2019 revenue is from an initial license payment and program services and expense reimbursements received for research and development costs associated with our influenza A/B program in accordance with the Merck Collaboration Agreement executed on January 2, 2019. Our expense reimbursement was higher during the three months ended September 30, 2018 compared to the three months ended September 30, 2019 due in part to the transfer of influenza A/B program technology from our third-party vendors to Merck as part of the Merck Collaboration Agreement. As the result, our influenza A/B program expenses decreased during the three and nine months ended September 30, 2019 compared to the prior year periods. See Note 10 within the condensed consolidated financial statements for more information.

Research and Development Expense

Research and development expense consists primarily of compensation-related costs for our employees dedicated to research and development activities and for our Scientific Advisory Board members, as well as lab supplies, lab services, and facilities and equipment costs.

Total research and development expenses for the three months ended September 30, 2019 were \$1,077,000, remaining comparable to expenses of \$1,467,000 for the three months ended September 30, 2018. Total research and development expenses for the nine months ended September 30, 2019 were \$3,046,000, remaining comparable to expenses of \$3,464,000 for the nine months ended September 30, 2018. For the nine months ended September 30, 2019, Merck reimbursed us for certain research and development expenses related to our influenza A/B program in accordance with the Collaboration Agreement and the reimbursement is included in revenues, as discussed above.

General and Administrative Expense

General and administrative expense includes compensation-related costs for our employees dedicated to general and administrative activities, legal fees, audit and tax fees, consultants and professional services, and general corporate expenses.

General and administrative expenses were approximately \$1,223,000 for the three months ended September 30, 2019, compared with \$952,000 for the nine months ended September 30, 2018. The increase of \$271,000 was primarily due to increased audit related fees and legal services that included contracts, litigation and patent related matters.

General and administrative expenses were approximately \$3,597,000 for the nine months ended September 30, 2019, compared with \$3,157,000 for the nine months ended September 30, 2018. The increase of \$440,000 was primarily due to increased audit related fees and legal services that included contracts, litigation and patent related matters.

Interest Expense, Net

Interest expense was \$4,000 and \$16,000 for the three months and nine months ended September 30, 2019, respectively. Interest expense was \$0 and \$55,000 for the three months and nine months ended September 30, 2018, respectively. The interest amounts in 2019 represent interest incurred on finance leased lab equipment, and 2018 interest incurred was on convertible notes which were converted to common stock in May 2018 (refer to Note 12 and Note 7, respectively, in the condensed consolidated financial statements). Interest income was negligible for the three and nine months ended September 30, 2019 and 2018.

Other Income/(Expense)

Change in the fair value of derivative liabilities for the nine months ended September 30, 2019 was \$173,000 compared to \$410,000 for the nine months ended September 30, 2018. In accordance with U.S. GAAP, we record other income or expense based upon the computed change in fair value of our outstanding warrants that are accounted for as liabilities. The fair value of our outstanding warrants is inversely related to the fair value of the underlying common stock; as such, an increase in the price of our common stock during a given period generally results in other expense. Conversely, a decrease in the price of our common stock generally results in other income, which is what occurred during both periods.

Also included as other income for the nine months ended September 30, 2018 is a gain of \$106,000 on the disposal of its mortgage note. The Company resolved all outstanding claims and disputes with 580 Garcia Properties, LLC. In exchange, the Company received \$1,400,000 on February 9, 2018 from a third party. At December 31, 2017, the mortgage note receivable balance was \$1,294,000 resulting in the aforementioned gain.

Income Taxes

No income tax benefit or expense was recognized for the three and nine months ended September 30, 2019. As a result of the Company's cumulative losses, management has concluded that a full valuation allowance against the Company's net deferred tax assets is appropriate.

For the three and nine months ended September 30, 2018, we recognized an income tax benefit of approximately \$554,000 and \$973,000, respectively, primarily due to the change in effective federal income tax rates (from 35% to 21%) used to calculate the Company's deferred tax liability which related to the acquisition of in-process research and development considered to be indefinite-lived intangible assets and totaled \$12,609,000 as of September 30, 2018. The Company abandoned the underlying assets associated with in-process research and development ("IPR&D") intangibles in the fourth quarter of 2018, which were then written off along with the Company's associated deferred tax liability.

Net Income (Loss)

As a result of the above factors, the Company had net loss of approximately \$324,000 compared to a net loss of approximately \$4,762,000 for the nine months ended September 30, 2019 and 2018, respectively, and a net loss of approximately \$1,780,000 and \$1,868,000 for the three months ended September 30, 2019 and 2018, respectively.

Liquidity and Capital Resources

Net cash used by operating activities was \$317,000 for the nine months ended September 30, 2019 compared to net cash used in operating activities of \$6,320,000 for the same period in 2018. This was primarily due to the revenue resulting from the Collaboration Agreement with Merck (refer to Note 10 – Licenses and Collaborations).

Net cash used for investing activities was approximately \$144,000 for the nine months ended September 30, 2019 compared to \$1,387,000 net cash provided by investing activities for the same period in 2018. For the nine months ended September 30, 2019, net cash used for investing activities consisted primarily of capital spending for computers and lab equipment. For the nine months ended September 30, 2018, net cash provided by investing activities primarily consisted of the proceeds from the sale of the mortgage note asset for \$1,400,000.

For the nine months ended September 30, 2019, cash provided by financing activities totaled \$3,753,000. Our 2019 financing activities included approximately \$3,928,000 net proceeds from the issuance of common stock, reduced by payments of \$175,000 made on the Company's lease liabilities for financed lab equipment. Net cash provided by financing activities was \$8,869,000 for the nine months ended September 30, 2018. Net cash provided by financing activities during the nine months ended September 30, 2018 consisted of \$7,684,000 net proceeds from the issuance of common stock, \$1,000,000 in proceeds from the issuance of convertible notes, and \$185,000 in proceeds from the exercise of stock options.

To date we have focused our efforts on research and development activities, including through collaborations with suitable partners. We have never been profitable on an annual basis, have no products approved for sale, have not generated any revenues to date from product sales, and has incurred significant operating losses and negative operating cash flows on an annual basis since inception.

The Company has not yet established an ongoing source of revenue sufficient to cover its operating costs and allow it to continue as a going concern. Based on cash on hand as of November 7, 2019 of approximately \$7.2 million, the Company may not have the capital to finance its operations including any unforeseen expenses such as higher than anticipated legal costs and uninsured catastrophe to the Company operations for the next 12 months. The ability of the Company to continue as a going concern is dependent on the Company obtaining adequate capital to fund its operations until it becomes profitable. If the Company is unable to obtain adequate capital and/or generate additional revenue under the Merck Collaboration Agreement, it could be forced to cease operations or substantially curtail its drug development activities. The accompanying financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and the classification of liabilities should the Company be unable to continue as a going concern.

Historical Financings

Historically, public and private equity offerings have been our principal source of liquidity.

On May 3, 2018, the Company closed a public offering for gross proceeds and net proceeds of approximately \$8,428,000 and \$7,684,000, respectively. The Company sold 4,210,527 shares of common stock to the underwriter at approximately \$1.77 per share which the underwriter sold to the public at \$1.90 per share and issued the underwriter a warrant to purchase 84,211 shares of common stock at \$2.09 per share over a four year period beginning October 27, 2018. On May 14, 2018, the underwriter exercised the option to purchase an additional 225,000 shares of common stock solely to cover overallotments. As of September 30, 2019, the underwriter has no further option to purchase additional shares.

On March 13, 2019, the Company closed a private placement of 1,602,283 shares of its common stock and received gross proceeds of \$4,182,000, before deducting offering expenses and commissions, and net proceeds were approximately \$3,584,000.

On March 20, 2019, the Company by written notice suspended at-the-market sales of its common stock pursuant to the previously disclosed Equity Distribution Agreement, dated July 19, 2018 (the "Distribution Agreement") by and among the Company, Ladenburg Thalmann & Co. Inc., Barrington Research Associates, Inc. ("Barrington"), and Alliance Global Partners ("AGP"). Previously, on December 14, 2018, the Company received notice from Ladenburg regarding the termination of its engagement as a sales agent under the Distribution Agreement. On March 20, 2019, the Company terminated Barrington's engagement as a sales agent under the Distribution Agreement, effective March 21, 2019. The Distribution Agreement remains in place with respect to AGP, subject to the suspension of sales discussed above until further notice is provided by the Company to AGP. In January 2019, we sold 80,000 shares of common stock under the Distribution Agreement and received net proceeds of approximately \$344,000. On October 30, 2019, the Company and AGP amended the Distribution Agreement to reduce the amount that may be sold thereunder from \$10 million to \$2 million.

On November 4, 2019, the Company closed a public offering and received gross proceeds of approximately \$3.0 million and net proceeds of \$2.6 million. The Company sold 3,529,412 shares of common stock to Aegis Capital Corp, the underwriter, at approximately \$0.79 per share which the underwriter sold to the public at \$0.85 per share. The underwriter has a 45 day option to purchase an additional 529,411 shares of common stock solely to cover overallocments.

As the Company continues to incur losses, achieving profitability is dependent upon the successful development, approval and commercialization of its product candidates, and achieving a level of revenues adequate to support the Company's cost structure. The Company may never achieve profitability, and unless and until it does, the Company will continue to need to raise additional capital. Management intends to fund future operations through additional private or public equity offerings and may seek additional capital through arrangements with strategic partners or from other sources. There can be no assurances, however, that additional funding will be available on terms acceptable to the Company, or at all. Any equity financing may be very dilutive to existing shareholders.

Cautionary Note Regarding Forward-Looking Statements

This report includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including statements regarding the future progress of our Phase 2a open-label study in Hong Kong, the expected timing of our Phase 1 Influenza study, our continued future collaboration with Merck under the Collaboration Agreement, and our liquidity. The words "believe," "may," "estimate," "continue," "anticipate," "intend," "should," "plan," "could," "target," "potential," "is likely," "will," "expect" and similar expressions, as they relate to us, are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs.

The results anticipated by any or all of these forward-looking statements might not occur. Important factors that could cause actual results to differ from those in the forward-looking statements include risks arising from our reliance on continued collaboration with Merck, the availability of products manufactured by third parties, the ability of clinical research organizations to recruit subjects and complete studies in a timely manner or at all, including as the result of civil unrest and political instability in Hong Kong, unanticipated events which adversely affect the timing and success of our regulatory filings, general risks arising from clinical trials, failure to develop products which are deemed safe and effective and other issues which affect our ability to commercialize our product candidates, unexpected adverse events affecting our ability to raise capital, unanticipated litigation and other expenses and factors that affect the capital markets in general and early stage biotechnology companies in particular. Further information on our risk factors is contained in our filings with the SEC, including our Annual Report on Form 10-K for the year ended December 31, 2018. We undertake no obligation to publicly update or revise any forward-looking statements, whether as the result of new information, future events or otherwise.

Critical Accounting Policies and Estimates

In our Annual Report on Form 10-K for the year ended December 31, 2018, we disclosed our critical accounting policies and estimates upon which our financial statements are derived. Readers are encouraged to review these disclosures in the Company's Annual Report on Form 10-K for the year ended December 31, 2018 in conjunction with the review of this report.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Our Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of September 30, 2019. We maintain disclosure controls and procedures that are designed to provide reasonable assurance that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow for timely decisions regarding required disclosure. Our management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were not effective as of September 30, 2019.

Changes in Internal Control Over Financial Reporting

With input and oversight from the Audit Committee, management is actively implementing a remediation plan to ensure that control deficiencies contributing to the material weaknesses were remediated such that these controls will operate effectively. We are taking, and expect to continue to take the following remediation actions:

- (i) the implementation of additional review procedures designed to enhance the control owner's execution of controls activities, including entity level controls, through the implementation of improved documentation standards evidencing execution of these controls, oversight, and training;
- (ii) improvement of the control activities and procedures associated with the review of complex accounting areas, including proper segregation of duties and assigning personnel with the appropriate experience as preparers and reviewers over analyses relating to such accounting areas;
- (iii) educating and re-training control owners regarding internal control processes to mitigate identified risks and maintaining adequate documentation to evidence the effective design and operation of such processes; and
- (iv) implementing enhanced controls to monitor the effectiveness of the underlying business process controls that are dependent on the data and financial reports generated from the relevant information systems.

We believe that these actions, and the improvements we expect to achieve as a result, will effectively remediate the material weaknesses identified in 2018. However, the material weaknesses in our internal control over financial reporting will not be considered remediated until the remediated controls operate for a sufficient period of time and management has concluded, through testing, that these controls are operating effectively. We expect that the remediation of these material weaknesses will be completed in 2019.

Other than noted above, there were no changes in internal control over financial reporting that occurred during the nine months ended September 30, 2019, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, the Company is a party to, or otherwise involved in, legal proceedings arising in the normal course of business. During the reporting period, except as set forth below, there have been no material changes to the description of legal proceedings set forth in our Annual Report on Form 10-K for the year ended December 31, 2018 (the "Annual Report"). The following should be read in conjunction with the information provided in Part I, Item 3 of our Annual Report.

On January 16, 2019, Ms. Susan Church, a stockholder of the Company, filed with the United States District Court for the Western District of Washington a derivative suit against certain current and former executive officers and directors of the Company alleging breach of fiduciary duties, unjust enrichment, waste of corporate assets, and violations of the rules governing proxy solicitation. Church seeks, among other things, money damages, disgorgement of profits from alleged wrongful conduct, including cash bonuses, pre-judgment and post-judgment interest, reasonable attorneys' fees, expert fees and other costs. The attorneys have agreed to stay this derivative suit pending resolution of the class action discussed below.

On September 20, 2018, a class action lawsuit was filed with the United States District Court for the District of New Jersey a complaint against the Company, certain current and former executive officers and directors of the Company and the other defendants named therein for violation of Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder. Additionally, the complaint alleges that certain current and former executive officers of the Company violated Section 20(a) of the Exchange Act. The class consists of the persons and entities who purchased the Company's common stock during the period from September 23, 2013 through September 7, 2018. The plaintiffs seek damages, pre-judgment and post-judgment interest, reasonable attorneys' fees, expert fees and other costs. On June 25, 2019, the plaintiffs in the class action lawsuit filed an amended class action complaint.

On July 8, 2019, Mr. Lee Pederson filed a lawsuit in the United States District Court for the District of Minnesota against the Company, Dr. Phillip Frost and Mr. Daniel Fisher. While the Company, to its knowledge, has not been served, it has obtained a copy of the complaint. In his complaint, Pederson alleges tortious interference by the Company and Dr. Frost with the collaboration agreement between Mr. Pederson and Mr. Fisher. Mr. Pederson seeks damages in the amount of \$800,000 or such other amount as may be determined at trial.

ITEM 1.A RISK FACTORS

The information presented below updates, and should be read in conjunction with, the risk factors and information disclosed in our Annual Report on Form 10-K for the year ended December 31, 2018.

Delays and disruptions in our clinical studies, including our Phase 2a Hepatitis C study in Hong Kong, due to political instability, civil unrest, or acts of terrorism could negatively impact our business and future prospects.

The Phase 2a study of CC-31244 for the treatment of HCV, which commenced in May 2019, is being sponsored and conducted by the Humanity & Health Research Centre in Hong Kong, China. Hong Kong has recently experienced a series of large-scale protests, which have grown increasingly violent since they first started in March 2019. The protests may disrupt the Phase 2a study. If the protests continue and/or escalate further, it could prevent the Humanity & Health Research Centre from completing the Phase 2a study in a timely manner or at all. If the Humanity & Health Research Centre fails to complete the Phase 2a study as the result of continuing civil unrest and political instability in Hong Kong, it could negatively affect our ability to advance negotiations with potential strategic collaboration partners for the development and commercialization of CC-31244, which in its turn would have a material adverse effect on our business and future prospects.

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

All recent sales of unregistered securities have been previously reported.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not Applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

The exhibits listed in the accompanying "Exhibit Index" are filed or incorporated by reference as part of this Form 10-Q.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Cocrystal Pharma, Inc.

Dated: November 12, 2019

By: /s/ Gary Wilcox
Gary Wilcox
Chief Executive Officer
(Principal Executive Officer)

Dated: November 12, 2019

By: /s/ James Martin
James Martin
Chief Financial Officer
(Principal Financial Officer)

EXHIBIT INDEX

Exhibit No.	Exhibit Description	Incorporated by Reference			Filed or Furnished Herewith
		Form	Date	Number	
2.1	Agreement and Plan of Merger*	8-K	12/1/14	2.1	
3.1	Certificate of Incorporation, as amended	10-Q	8/9/18	3.1	
3.2	Bylaws	8-K	12/1/14	3.4	
10.1	Exclusive License and Research Collaboration Agreement between the Company and Merck Sharp & Dohme Corp., dated January 2, 2019**	10-K	4/1/19	10.12	
10.2	Amendment to Equity Distribution Agreement, dated March 20, 2019	8-K	3/26/19	10.1	
10.3	Form of Securities Purchase Agreement, dated March 11, 2019*	8-K	3/11/19	10.1	
31.1	Certification of Principal Executive Officer (302)				Filed
31.2	Certification of Principal Financial Officer (302)				Filed
32.1	Certification of Principal Executive and Principal Financial Officer (906)				Furnished***
101.INS	XBRL Instance Document				Filed
101.SCH	XBRL Taxonomy Extension Schema Document				Filed
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document				Filed
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document				Filed
101.LAB	XBRL Taxonomy Extension Label Linkbase Document				Filed
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document				Filed

* Certain exhibits and schedules have been omitted. The Company undertakes to furnish the omitted items to the SEC upon request.

** Confidential treatment has been granted with respect to certain portions of this exhibit. Omitted portions have been submitted separately to the SEC.

*** This exhibit is being furnished rather than filed and shall not be deemed incorporated by reference into any filing, in accordance with Item 601 of Regulation S-K.

Copies of this report (including the financial statements) and any of the exhibits referred to above will be furnished at no cost to our shareholders who make a written request to our Corporate Secretary at Cocrysal Pharma, Inc., 4400 Biscayne Blvd, Suite 101, Miami, FL 33137.

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER

I, Gary Wilcox, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cocrystal Pharma, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 12, 2019

/s/ Gary Wilcox

Gary Wilcox
Chief Executive Officer
(Principal Executive Officer)

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER

I, James Martin, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Cocrystal Pharma, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 12, 2019

/s/ James Martin

James Martin
Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the quarterly report of Cocrystal Pharma, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2019, as filed with the Securities and Exchange Commission on the date hereof, I, Gary Wilcox, certify, pursuant to 18 U.S.C. Sec.1350, as adopted pursuant to Sec.906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

1. The quarterly report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and
2. The information contained in the quarterly report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Gary Wilcox

Gary Wilcox
Chief Executive Officer
(Principal Executive Officer)

Dated: November 12, 2019

In connection with the quarterly report of Cocrystal Pharma, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2019, as filed with the Securities and Exchange Commission on the date hereof, I, James Martin, certify, pursuant to 18 U.S.C. Sec.1350, as adopted pursuant to Sec.906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

1. The quarterly report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 and
2. The information contained in the quarterly report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ James Martin

James Martin
Chief Financial Officer
(Principal Financial Officer)

Dated: November 12, 2019
