

PURE BIOSCIENCE, INC.  
Form 10-K  
October 28, 2014  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-K**

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

**For the fiscal year ended July 31, 2014**

**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 No. 001-14468**

**Pure Bioscience, Inc.**

**(Exact name of registrant as specified in charter)**

**Delaware** **33-0530289**  
**(State or other jurisdiction of** **(IRS Employer**  
**incorporation or organization)** **Identification No.)**

**1725 Gillespie Way**

**El Cajon, California 92020**

**(Address of principal executive office, including zip code)**

**(619) 596-8600**

**(Registrant's telephone number, including area code)**

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

**None**

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

**Common Stock, \$0.01 par value**

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes  No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

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accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

The aggregate market value of the registrant's voting stock held by non-affiliates, as of the last day of the registrant's second quarter, was approximately \$34,538,000 (computed on the basis of the closing price of the common stock on the OTCQB Bulletin Board on January 31, 2014).

As of October 28, 2014, there were 39,780,965 shares of the registrant's common stock, \$0.01 par value per share, outstanding.

**Other Information**

As used in this Annual Report on Form 10-K, the terms we, us, our, PURE and the Company refer to PURE Bioscience, Inc., a Delaware corporation, and its subsidiary, on a consolidated basis, unless otherwise stated.

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**CAUTIONARY STATEMENT REGARDING FORWARD LOOKING STATEMENTS**

Certain statements in this Annual Report on Form 10-K may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, or the Exchange Act. Forward-looking statements are based upon our current assumptions, expectations and beliefs concerning future developments and their potential effect on our business. In some cases, you can identify forward-looking statements by words such as if, shall, may, might, will likely result, should, expect, anticipate, believe, estimate, project, intend, goal, objective, predict, potential or continue, or the terms and other comparable terminology, although the absence of these words does not necessarily mean that a statement is not forward-looking. Additionally, statements concerning future matters such as our business strategy, development of new products, sales levels, expense levels, cash flows, future commercial and financing matters, future partnering opportunities and other statements regarding matters that are not historical are forward-looking statements.

Although the forward-looking statements in this Annual Report reflect our good faith judgment, based on currently available information, they involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by these forward-looking statements. Factors that might cause or contribute to such differences include, but are not limited to, those discussed in the Risk Factors contained in Part I, Item 1A of this Annual Report. As a result of these factors, we cannot assure you that the forward-looking statements in this Annual Report on Form 10-K will prove to be accurate. Except as required by law, we undertake no obligation to update publicly any forward-looking statements for any reason after the date we file this Annual Report with the Securities and Exchange Commission, or to conform these statements to actual results or to changes in our expectations. You should, however, review the factors and risks we describe in the reports we will file from time to time with the Securities and Exchange Commission after the date we file this Annual Report. Readers are urged to carefully review and consider the various disclosures made in this Annual Report.

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**PART I**

**Item 1. Business**

We are focused on developing and commercializing our proprietary antimicrobial products primarily in the food safety arena that provide solutions to the health and environmental challenges of pathogen and hygienic control. Our technology platform is based on patented stabilized ionic silver, and our initial products contain silver dihydrogen citrate, or SDC. SDC is a broad-spectrum, non-toxic antimicrobial agent, which offers 24-hour residual protection and formulates well with other compounds. As a platform technology, SDC is distinguished from existing products in the marketplace because of its superior efficacy, reduced toxicity and the inability of bacteria to form a resistance to it. SDC is manufactured as a liquid delivered in various concentrations. We currently manufacture and distribute SDC-based disinfecting and sanitizing products, which are registered by the Environmental Protection Agency, or EPA. We also manufacture and sell SDC-based formulations to manufacturers for use as a raw material ingredient in the production of personal care products. We believe our technology platform has potential application in a number of industries. We intend to focus our current resources on providing food safety solutions to the food industry.

**Recent Corporate Developments**

***New Board of Directors and Management Team***

On August 13, 2013, the following managerial and corporate governance changes occurred to create a new Board of Directors, or Board, and management team:

Michael L. Krall, Donna Singer, and Dennis Brovarone resigned as members of the Board;

Michael L. Krall, Donna Singer, and Dennis Atchley resigned all positions respectively held by them as officers of the Company;

Dave J. Pfanzelter was appointed by the Board to be the Chairman of the Board;

Dave J. Pfanzelter was appointed by the Board to serve as Interim Chief Executive Officer;

Gary D. Cohee was appointed by the Board to serve as a member of the Board; and

Peter C. Wulff was appointed by the Board to serve as Chief Financial Officer, Chief Operating Officer, and Corporate Secretary.

On July 22, 2013, Jon Carbone and Paul Maier resigned as directors of the Company and as members of the Audit and Compensation Committees.

On September 10, 2013, the Board appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. In connection with the hiring of Henry R. Lambert to serve as our Chief Executive Officer, Dave J.

Pfanzelter resigned his position as our Interim Chief Executive Officer. Mr. Pfanzelter continues to render significant services to us and continues to serve as our Chairman of the Board.

In October 2013, we appointed three additional members to the Board; Dr. David Theno, Jr., Craig Culver and William Otis. On April 9, 2014, Craig Culver resigned from the Board. There were no disagreements between Mr. Culver and the Company relative to his resignation.

On October 24, 2014, we appointed Tom Y. Lee, CPA, to the Board. The Board now consists of six members who provide professional experience in business and finance; food science and food safety; foodservice and food manufacturing; and distribution.

### *New Corporate Strategy*

As a result of a comprehensive business review by our new Board and management team, in August 2013, we announced a new business strategy focused on near-term commercialization of our SDC-based products to provide solutions for food safety across various segments of the food industry. As part of this new business strategy, we intend to license, outsource or shed other non-core competencies and operating activities. We believe we have sufficient resources, and the relevant experience in sales and marketing, product development and production to execute our food safety solutions business strategy.

Our near-term focus is to drive customer adoption in the food industry by addressing food safety risks across the supply chain in order to prevent or mitigate food contamination and/or the potential for food-borne illness with a specific customer focus in foodservice operators, food processors and food manufacturers.

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Additionally, we will, on a limited basis, seek to license and/or collaborate with strategic business partners who have the demonstrated relevant experience and resources necessary to commercialize our SDC technology platform in their industries which have a high need for pathogen and hygiene control.

## **Technology Platform**

The foundation of our technology platform is a proprietary electrochemical process that allows us to generate ionized silver in the presence of organic acid. This process creates a solution containing stabilized ionic silver that can function as an antimicrobial. Our current products all contain SDC, which is produced by ionizing silver in citric acid. SDC is a natural, non-toxic, non-caustic, colorless, odorless antimicrobial agent, which offers 24-hour residual protection, and that formulates well with other compounds. We believe that SDC is distinguished from other products in the marketplace because of its fast acting and superior efficacy against bacteria, viruses and fungi and its beneficial toxicity profile. We have also produced ionic silver-based molecular entities using other organic acids, and we believe these compounds may provide a platform for future product development.

## **Business Strategy**

Our goal is to become a sustainable company by commercializing our proprietary technology platform to deliver leading antimicrobial products through our sales and marketing efforts focused as a food safety solution in the food industry and through licensing and distribution collaborations for other industrial applications.

Key aspects of our new business strategy include:

Expanding sales and distribution for our products into the food industry with a focus on a dual track of food safety market opportunities:

Hard Surface and Food Contact Surface Disinfectant - commercialize the current EPA registered PURE Hard Surface disinfectant and sanitizer for use in foodservice operations and food manufacturing.

Direct Food Contact - commercialize, subject to both FDA and USDA approval, the use of SDC as a food processing and intervention aid for food processors for treating poultry, produce, beef and pork.

Establishing strategic alliances to maximize the commercial potential of our technology platform;

Developing additional proprietary products and applications; and

Protecting and enhancing our intellectual property.

In addition to our current products addressing food safety, we seek to leverage our technology platform through licensing and distribution collaborations to develop new products and enter into new markets that could potentially generate multiple sources of revenue.



***Recent Corporate Accomplishments***

Since the leadership change in August 2013, the Company reports meaningful progress has been made and continues to be made in implementing its new business strategy:

PURE has developed a new customer pipeline of more than 25 national food companies in various stages of evaluating and testing SDC-based products in their operations:

In-field testing results of SDC-based products to-date have shown 90% to 200% superiority in both level and speed of pathogen kill compared with incumbent chemical sanitization products.

We have secured initial commercial pilot orders from 7 U.S. food processors, with customer rollout plans in development.

We completed in-store testing with SUBWAY® Restaurants, a national brand quick serve restaurant, at 650 of its locations, confirming multiple outstanding prior testing results, where SDC-based products have continually been demonstrated to provide superior safety and efficacy. We are developing a phased system-wide sales rollout in the U.S. with SUBWAY®.

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PURE initiated a new development project for the application of SDC as a direct food contact processing aid and / or intervention for poultry, produce and meats:

We believe that the estimated potential addressable U.S. market opportunity for this new direct food contact processing aid exceeds \$1.0 billion for all three categories.

We submitted Food Contact Notification (FCN) to the FDA in July 2014 for *Salmonella* reduction in processing of raw poultry.

We submitted Food Contact Notification (FCN) to the FDA in October 2014 for *Salmonella*, *E. coli* and *Listeria* reduction in the processing of produce.

We initiated pilot testing in September 2014 for the use of SDC as a processing aid for beef and pork. FCN submission expected by early 2015.

In December 2013, PURE implemented a five-year strategic collaboration agreement with Intercon Chemical Company ( ICC ) to out-source manufacturing and supply chain of SDC-based products and establish distribution, which had the following benefits:

Allowed for reduction of non-core operating activities and working capital; reduced facility occupancy costs by approximately 60% and reduced associated production and warehouse personnel.

Provided increased manufacturing capacity for anticipated future SDC-based product market demand.

Provided potential future royalty income for SDC-based products sold through ICC 's institutional cleaning and sanitation distribution channel.

In December 2013, PURE executed a three-year non-exclusive distribution agreement with Brenntag Specialties, Inc., an industry and market leading specialty chemical company, to continue to distribute SDC-based antimicrobial SILVÉRIION® 2400 as an active ingredient or preservative for use in personal care products.

PURE has raised over \$14.5 million in private equity placements to initiate and fund our growth strategy, including a \$7.9 million equity placement completed in August 2014, which provides more than 12 months of working capital. (See *Liquidity and Capital Resources* in Item 7 of this Annual Report).

PURE has eliminated long-term debt and reduced total adjusted liabilities.

## Products

We manufacture and sell (i) SDC-based products for end use, (ii) products preserved with SDC and (iii) SDC as a raw material ingredient for manufacturing use. Our current products are as follows:

Product Name	Product Use	EPA Registration
<i>PURE Complete Solution:</i>		
PURE <sup>®</sup> Hard Surface	Disinfectant and sanitizer	SDC3A
PURE Multi-Purpose Cleaner Concentrate	Cleaner	Not applicable
PURE Multi-Purpose Hi-Foam Cleaner Concentrate	Cleaner	Not applicable
Axen <sup>®</sup> 30(1)	Disinfectant	Axen30
Axenohl <sup>®</sup>	Raw material ingredient	Axenohl
Silvériion <sup>®</sup>	Raw material ingredient	Not applicable

(1) We intend to phase out Axen<sup>®</sup> 30

### *PURE Complete Solution*

Our PURE Complete Solution is comprised of PURE<sup>®</sup> Hard Surface and concentrated cleaning products that were launched as companion products to PURE<sup>®</sup> Hard Surface. The PURE Complete Solution offers a comprehensive, cost-effective and

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user-friendly cleaning, disinfecting and sanitizing product line to end-users including our targeted foodservice, food manufacturing and food processing customers. We can also target this product line to hospital and medical care facilities; janitorial service providers and the distributors that supply them.

### ***PURE® Hard Surface Disinfectant and Sanitizer (Ready-to-Use)***

PURE® Hard Surface is our SDC-based, patented and EPA-registered, ready-to-use hard surface disinfectant and food contact surface sanitizer. We manufacture both consumer and commercial versions of the product. PURE Hard Surface combines high efficacy and low toxicity with 30-second bacterial and viral kill times and 24-hour residual protection. The product completely kills resistant pathogens such as MRSA and Carbapenem-resistant *Klebsiella pneumoniae* (NDM-1), and effectively eliminates dangerous fungi and viruses including HIV, Hepatitis B, Hepatitis C, Norovirus, Influenza A, Avian Influenza and H1N1. It also eradicates hazardous food pathogens such as *E. coli*, *Salmonella*, *Campylobacter* and *Listeria*. PURE® Hard Surface delivers broad-spectrum efficacy yet remains classified as least-toxic by the EPA. The active ingredient, SDC, has been designated as Generally Recognized as Safe, or GRAS, for use on food processing equipment, machinery and utensils.

### ***PURE Multi-Purpose Cleaner Concentrate (End-User Dilutable)***

PURE® Multi-Purpose Cleaner, is an environmentally responsible cleaning product that is protected by SDC. SDC ensures the quality and safety of PURE® Multi-Purpose Cleaner without human or environmental exposure to toxic chemical preservatives. PURE® Multi-Purpose Cleaner is non-toxic and non-flammable and contains no EDTA, phosphates, ammonia or bleach as well as no VOCs or NPEs. PURE Multi-Purpose Cleaner provides professional strength cleaning in a concentrate formula that yields a 1:96 – 1:256 use dilution that is safe for use on all resilient surfaces, including floors, glass and food contact surfaces.

### ***PURE Multi-Purpose Hi-Foam Cleaner Concentrate (End-User Dilutable)***

PURE® Multi-Purpose Hi-Foam Cleaner is an environmentally responsible, professional strength high foam forming cleaning product that is protected by SDC. SDC ensures the quality and safety of PURE Multi-Purpose Hi-Foam Cleaner without human or environmental exposure to toxic chemical preservatives. PURE Multi-Purpose Hi-Foam Cleaner is non-toxic and non-flammable and contains no EDTA, phosphates, ammonia or bleach as well as no VOCs or NPEs. PURE Multi-Purpose Hi-Foam Cleaner provides high foam cleaning in a concentrate formula that yields a 1:50 use dilution that is safe for use on stainless steel equipment, resilient floors, walls and painted surfaces.

### ***Axen® 30 (Ready-to-Use)***

Axen®30 is our patented and EPA-registered hard surface disinfectant and is a predecessor ready-to-use product to PURE® Hard Surface. Axen30 is currently sold on a limited basis by distributors under their respective private labels which we intend to phase out.

### ***Axenohl® (Raw Material Ingredient)***

Axenohl® is our patented and EPA-registered SDC-based antimicrobial formulation for use as a raw material ingredient in the manufacturing of EPA-registered products. Axenohl is a colorless, odorless and stable solution that provides fast acting efficacy against bacteria, viruses and fungi when manufactured into consumer and commercial disinfecting and sanitizing products.

### ***SILVÉRIION® (Raw Material Ingredient)***

SILVÉRION® is our patented SDC-based antimicrobial formulation for use as a raw material ingredient in the manufacturing of personal care products. It can be used as either an active ingredient or a preservative. SILVÉRION is a colorless, odorless and stable solution that provides ionic silver in a water-soluble form. It provides fast acting efficacy at low concentrations against a broad-spectrum of bacteria, viruses, yeast and molds. SILVÉRION is currently sold outside of the United States in various personal care products.

### **EPA Registrations**

We sell our EPA-regulated products under the following three EPA registrations: (i) SDC3A, our hard surface disinfectant and food contact surface sanitizer, (ii) Axen30, our hard surface disinfectant, and (iii) Axenohl, our antimicrobial formulation for use as a raw material in the manufacturing of EPA-registered products.

**Table of Contents****SDC3A Registration**

The EPA registration for SDC3A, marketed as PURE Hard Surface, our disinfectant and food contact surface sanitizer, includes the following efficacy claims:

<b>Organism</b>	<b>Kill Time</b>
<i>Pseudomonas aeruginosa</i>	30 seconds
<i>Salmonella enterica</i>	30 seconds
<i>Staphylococcus aureus</i>	2 minutes
<i>Listeria monocytogenes</i>	2 minutes
Vancomycin resistant <i>Enterococcus faecium</i> (VRE)	2 minutes
Methicillin resistant <i>Staphylococcus aureus</i> (MRSA)	2 minutes
Community Associated Methicillin resistant <i>Staphylococcus aureus</i> (CA-MRSA)	2 minutes
Community Associated Methicillin resistant <i>Staphylococcus aureus</i> (CA-MRSA-PVL)	2 minutes
<i>Escherichia coli</i> O157:H7	2 minutes
<i>Acinetobacter baumannii</i>	2 minutes
<i>Campylobacter jejuni</i>	2 minutes
Carbapenem resistant <i>Escherichia coli</i>	2 minutes
Carbapenem resistant <i>Klebsiella pneumoniae</i>	2 minutes
Carbapenem resistant <i>Klebsiella pneumoniae</i> , NDM-1 +	2 minutes
Trichophyton mentagrophytes (Athlete's Foot Fungus)	5 minutes
HIV type 1	30 seconds
Rotavirus	30 seconds
Human Coronavirus	30 seconds
Influenza A (H1N1)	30 seconds
Swine Influenza A (H1N1)	30 seconds
Respiratory Syncytial Virus	30 seconds
Adenovirus Type 2	30 seconds
Avian Influenza A	30 seconds
Influenza A	30 seconds
Hepatitis B Virus (HBV)	60 seconds
Hepatitis C Virus (HCV)	60 seconds
Murine Norovirus	60 seconds
Norovirus	60 seconds
Herpes Simplex Type 1	60 seconds
Rhinovirus	60 seconds
Polio Type 2	60 seconds

The EPA registration for SDC3A also claims 24-hour residual protection against bacteria.

**Toxicity Categories**

The EPA categorizes the toxicity of antimicrobial products from Category I to Category IV. The following table shows the EPA toxicity categories and required signal words.

Toxicity Category	Signal Word
I	DANGER, POISON
II	WARNING
III	CAUTION
IV	None required

SDC3A is a Category IV product for which no signal words are required.

***Axen30 Registration***

Axen<sup>®</sup>30 is a hard surface disinfectant and is a predecessor product to SDC3A. It offers similar broad-spectrum efficacy but longer kill times. Axen30 is not approved for use on food contact surfaces. Axen30 is currently sold on a limited basis by distributors under their respective private labels which we intend to phase out.

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### ***Axenohl Registration***

Axenohl is registered as a raw material ingredient for the manufacturing of EPA-registered products and as such does not carry specific efficacy claims.

### **U.S. Regulatory Approval of SDC as a Direct Food Contact Processing Aid**

#### **Poultry Processing Aid**

On July 11, 2014, we submitted a Food Contact Notification (FCN) to the U.S. Food and Drug Administration (FDA) for SDC as an online reprocessing (OLR) antimicrobial for raw poultry processing.

Data submitted as part of the Company's FCN showed that, in testing conducted by Dr. James Marsden at Kansas State University, SDC achieved an average reduction in *Salmonella* of 2.75 log<sub>10</sub> CFU/cm<sup>2</sup> when applied as an OLR spray and 6.28 log<sub>10</sub> CFU/cm<sup>2</sup> when combined with an immersion chilling process simulating current U.S. industry practices.

The importance of this data indicates that the use of SDC antimicrobial solution in poultry processing has the potential to enable plants to achieve non-detectable *Salmonella* levels post-chill process.

Additionally, a sensory evaluation of SDC showed no difference in color, appearance or odor in treated poultry. The Company believes that these test results exceed current U.S. industry best practices. In addition, given the non-toxic properties of SDC, the Company believes there are safety benefits for users, production line personnel and the surrounding environment.

SDC offers a highly effective alternative to hazardous and difficult to blend chemicals currently used as OLR treatments in raw poultry processing.

SDC is a significant improvement over current processing practices. The product is:

Easier to handle and dilute

Non-corrosive to processing equipment

Does not create noxious fumes

The Company believes that poultry processors will also benefit from the highly stable solution, ease of use and improved worker safety.

#### **Produce Processing Aid**



On October 7, 2014, the Company submitted a Food Contact Notification (FCN) to the FDA for SDC as an produce processing aid.

Data submitted as part of the Company's FCN for produce showed that, in testing conducted by Dr. James Marsden at Kansas State University, SDC achieved average reductions in up to 2.36  $\log_{10}$  CFU/cm<sup>2</sup> when applied alone as a spray and up to 3.10  $\log_{10}$  CFU/cm<sup>2</sup> when combined with chlorine wash, simulating current processing practices. Sensory evaluations of produce treated with SDC indicated no difference in color, appearance or odor to untreated controls; and SDC had no effect on the nutritional composition of the produce.

Currently, produce processors target achieving only a 1  $\log_{10}$  CFU/cm<sup>2</sup> reduction per intervention treatment. Data suggests that by incorporating SDC, processors can improve their results 100-fold with only one step. This represents a significant advantage to produce processors as well as improvement to the safety of processed produce going to the consumer.

### **Other Processing Aids under Development**

The Company is developing the use of SDC as an intervention in the processing of beef and pork. Subject to successful pilot testing results, the Company intends to submit for both FDA and USDA approval. In addition, the Company may identify other food processing opportunities for SDC.

### **FDA and USDA Approval Process**

The FDA's FCN Program ensures the safety of Food Contact Substances (FCS) used in food processing and packaging.

The FCN review period is 120 days from filing, after which, if there are no concerns from the FDA, the FCN automatically becomes effective.

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An FCN is considered to be proprietary as it applies only to the specific product and manufacturer or supplier identified in the FCN.

Upon the FDA's granting of the FCN, PURE will immediately submit the FCN to the Food Safety and Inspection Service (FSIS) of the USDA for a new technology review.

As part of the FSIS review process, PURE will conduct three in-plant process validation and optimization trials with the authorization of the USDA.

After completion of the three in-plant validation trials, PURE expects the USDA to issue a Letter of No Objection and list SDC as an OLR poultry processing aid in Attachment 1 of FSIS Directive 7120.1, Safe and Suitable Ingredients Used in the Production of Meat and Poultry Products.

Subject to receipt of both FDA and USDA approval PURE will begin commercialization of SDC in Q1 2015 for use in poultry processing.

## **Intellectual Property**

Our policy is to pursue patents, pursue trademarks, maintain trade secrets and use other means to protect our technology, inventions and improvements that are commercially important to the development of our business.

We have applied for U.S. and foreign patent protection for our SDC technology. Currently, we own twelve U.S. issued patents. Approximately twenty-six patents have been issued outside of the U.S. and we own approximately ten patents pending around the world. The expiration dates for our ten U.S. issued patents begin in 2018 and end in 2030. In September 2013, we decided to abandon pending and issued patents in non-strategic international territories. Future patent prosecution and defense efforts are intended primarily for North America, Europe, Asia and Mexico.

Additional patent applications may not be granted, or, if granted, may not provide adequate protection to us. We also intend to rely on whatever protection the law affords to trade secrets, including unpatented know-how. Other companies, however, may independently develop equivalent or superior technologies or processes and may obtain patents or similar rights with respect thereto.

Although we believe that we have developed our technology independently and have not infringed, and do not infringe, on the patents of others, third parties may make claims that our technology does infringe on their patents or other intellectual property. In the event of infringement, we may, under certain circumstances, be required to modify our infringing product or process or obtain a license. We may not be able to do either of those things in a timely manner if at all, and failure to do so could have a material adverse effect on our business. In addition, we may not have the financial or other resources necessary to enforce a patent infringement or proprietary rights violation action or to defend ourselves against such actions brought by others. If any of the products we develop infringe upon the patent or proprietary rights of others, we could, under certain circumstances, be enjoined or become liable for damages, which would have a material adverse effect on our business.

We also rely on confidentiality and nondisclosure agreements with our employees, customers, consultants, advisors, licensees and potential partners to protect our technology, intellectual property and other proprietary property. Pursuant to the foregoing and for other reasons, we face the risk that our competitors may acquire information which

we consider to be proprietary, that such parties may breach such agreements or that such agreements will be inadequate or unenforceable.

Further, we own the registered trademarks or pending trademark applications for PURE Bioscience®, Powered by SDC Ag+®, PURE®, Axenohl®, Axen®, Silvérion®, Nutripure®, Elderguard®, and Critterguard®. In addition, we have applications for other trademarks pending around the world, which may or may not be granted. In the last year, we allowed the marks Kinderguard®, Cruise Control®, and Staphacide® to go abandoned, as they were no longer in line with our food safety business strategy.

## **Scientific Background**

### ***Silver as an Antimicrobial***

The use of silver as an antimicrobial dates back to ancient times when water, wine and other beverages were kept in silver vessels to maintain freshness. Ancient Egyptians applied thin strips of beaten silver around wounds to avoid infection, and early royalty ate from silver plates and with silver utensils to stay healthy. In the past half-century, silver in colloidal and ionic forms has been used successfully in a wide array of antimicrobial applications, including water purification and topical treatments for burn victims. Silver must be in an ionic or colloidal form to be effective at killing microorganisms. The short shelf-life of previous ionic silver solutions has limited the development of ionic-silver based antimicrobials. SDC, as a stabilized silver ion complex, has a shelf life of more than a decade because the weak bond of the silver ion to the citric acid allows the ion to remain stable in solution while at the same time making it bioavailable for antimicrobial action.

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### *Silver Dihydrogen Citrate is a Stabilized Silver Ion Complex*

SDC is a patented antimicrobial based on a stabilized silver ion complex. SDC is produced by a unique electrochemical process using silver and citric acid. The resulting solution is a colorless, low viscous liquid containing a water soluble silver salt of citric acid.

### *Mechanisms of Action*

The rapid and broad-spectrum efficacy of SDC is attributed to its dual mechanisms of action, both with respect to killing bacteria and other microorganisms and acting against viruses.

SDC can kill microorganisms at both the extracellular and intracellular levels. SDC attracts bacteria because the citric acid is recognized by the organism as a food source. SDC easily enters the microorganism through membrane transport proteins. Once inside the organism, SDC binds to DNA and intracellular proteins causing irreversible damage to the DNA and protein structure. Metabolic and reproductive functions halt, and the organism dies. SDC can also act on an organism's outer membrane. Silver ions are highly attracted to sulfur-containing thiol groups found in metabolic and structural proteins bound to the membrane surface. SDC targets these critical proteins and destroys their structure. This disruption of the organism's membrane function and integrity lyses the membrane and the organism dies.

Viruses are much smaller than bacteria and present fewer target sites on which a biocide can act. The efficacy of SDC against enveloped and non-enveloped viruses comes from its ability to destroy not only the viral envelope, preventing the virus from attaching to a host cell, but also the infectious component of the virus, the nucleic acid.

### *Safety Profile*

Research has shown that silver is an effective antimicrobial and not toxic to humans. In addition, our data shows the components of SDC, ionic silver and citric acid, to be non-toxic, particularly at the low concentrations required to eliminate microorganisms. At higher concentrations, citric acid can be an eye irritant. We have tested a concentrated SDC formulation using standard protocols to measure acute toxicity. Our results demonstrate that there is no toxicity associated with SDC. Acute oral and dermal toxicity was not observed at doses up to and including 5000 mg/kg, indicating lack of toxicity. Data from the eye and skin studies showed only slight irritation and no dermal sensitization.

### *GRAS Status as Contact Biocide*

A committee of independent experts critically reviewed efficacy and toxicity data for SDC and the SDC-based PURE® Hard Surface disinfectant and food contact surface sanitizer. The committee found no evidence that SDC demonstrates a hazard to the public when used as a contact biocide on food contact surfaces and food-use utensils. The committee, therefore, concluded such use to be generally recognized as safe, consistent with the EPA registration, allowing for use on food manufacturing and processing equipment and food preparation surfaces.

### *Efficacy*

Formulations containing SDC provide complete, quick and broad-spectrum antimicrobial efficacy against gram positive and gram negative bacteria, enveloped and non-enveloped viruses, and fungi. In addition to quick kill times, SDC provides residual antimicrobial activity. SDC also provides rapid kill times against multiple drug resistant bacteria including Methicillin-resistant *Staphylococcus aureus*, or MRSA, Vancomycin resistant *Enterococcus*

*faecium*, or VRE, Carbapenem resistant *Escherichia coli*, Carbapenem resistant *Klebsiella pneumoniae* and Carbapenem resistant *Klebsiella pneumoniae*, NDM-1. See the section of this Item 1 entitled EPA Registrations for detailed efficacy data.

*Natural and Environmentally Responsible*

SDC is made of simple and all-natural ingredients: water, citric acid and minute amounts of ionic silver. SDC is non-toxic. The safety profile for silver has been extensively reviewed in public literature and by US government agencies and international organizations including the EPA, the Food and Drug Administration, or FDA, the Agency for Toxic Substances and Disease Registry, the World Health Organization and the National Resource Center for Health Information Technology. There is no evidence of mutagenicity, carcinogenicity, neurotoxicity, reproductive or developmental effects due to silver.

SDC does not harm the environment. If introduced to water systems, the low concentrations of ionic silver in SDC would react with naturally present substances such as chlorides, sulfides and organic matter. These reactions would create insoluble silver complexes and render the silver inert.

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SDC is manufactured through a zero waste process in which no byproducts or environmental effluent are created.

### **Research and Development**

We recognize the importance of innovation to our long-term success. A key aspect of our business strategy is to leverage our technology platform to develop additional proprietary products and applications. We are focused on the development of end use products and raw material formulations derived from our technology platform. We conduct our primary research and development activities in-house and use third-party laboratories to conduct independent testing. We also engage development partners to perform research and development activities at their own expense for specific products and processes using SDC. Amounts spent on research and development activities during the fiscal years ended July 31, 2014 and 2013 were \$1,032,000 and \$1,169,000, respectively.

We have developed several new SDC-based products, including a dilutable sanitizer and virucide. In addition, we may continue to develop or may develop with strategic partners various other SDC-based product candidates including a dilutable food contact surface sanitizer, hard surface disinfecting and skin cleansing wipes, formulations for industrial biofilm control, high level disinfectants, agriculture treatments, food processing aids, food additives and preservatives as well as medical products.

### **U.S. Food Safety Market Overview**

#### ***U.S. Incidence and Cost of Foodborne Illness***

In the U.S., the CDC estimated in 2011 that foodborne illnesses affect over 48 million people annually, causing 128,000 hospitalizations and 3,000 fatalities. The CDC estimates that more than 9 million of these foodborne illnesses are attributed to major pathogens. According to FoodNet, a collaborative project among FSIS, [CDC](#), and the [FDA](#) to identify, control, and prevent foodborne disease hazards, foodborne illnesses continue to exceed national food safety goals and remain a public health problem in the U.S.

The CDC identified that produce is responsible for approximately 46% of foodborne illnesses caused by pathogens while poultry is responsible for more deaths than any other food commodity. This indicates that the greatest need for improvement in pathogen control efforts is in produce and poultry processing.

Among the top pathogens contributing to foodborne illness in the U.S. is Norovirus, *Salmonella*, *Campylobacter*, *Staphylococcus*, Shiga toxin producing *Escherichia coli* and *Listeria*. *Salmonella* is the leading cause of hospitalization, followed by Norovirus, and is the leading cause of deaths related to foodborne illness.

According to an Ohio State University study published in the Journal of Food Protection, completed by Dr. Scharff, a consumer science professor, foodborne illness poses a \$77.7 billion economic burden in the United States annually. This cost estimate includes health related costs associated medical costs, productivity losses, mortality, and pain and suffering. The study noted that excluding the estimated costs for pain and suffering that health related costs exceeded \$51 billion. The study does not include costs to the food industry, including reduced consumer confidence, reduced brand value, product recall costs, and litigation, nor does it include the cost to public health agencies, local, state, and federal, that respond to illnesses and outbreaks.

In addition, the study cited *Salmonella* as the most costly pathogen with an economic burden estimated to be in excess of \$11 billion primarily due to its high incidence and mortality rate.

#### ***Increased Regulatory Requirements in the U.S.***

The increasing trend of reported foodborne illness over the last decade has resulted in heightened awareness by various government agencies, national media and social media outlets affecting consumer confidence and elevating federal and state regulatory scrutiny.

In 2011, the Food Safety Modernization Act was passed by the U.S. Congress, resulting in increased regulatory requirements for preventive controls, verification and validation of food safety plans by food processors. Additionally, in December 2013 the Food Safety and Inspection Service (FSIS) of the USDA, announced its *Salmonella* Action Plan (SAP), which is focused on identifying solutions to reduce the incidence of *Salmonella* in meat and poultry. The Company believes that the implementation of the SAP will increase the need for new, effective interventions to assist in reducing the incidence of *Salmonella* in meat and poultry.

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### *Positioning of SDC-based Products as a Food Safety Solution*

The statistics of the U.S. public health problems attributed to pathogens in the food supply chain demonstrate the increasing need for more effective, efficient and safer interventions. The Company believes the U.S. food industry continues to use toxic chemicals as processing aids or interventions during food processing operations for which pathogens are becoming increasingly resistant and rendering current interventions less efficacious. Most of these chemicals carry various warning labels for their toxicity characteristics and negatively affect safety of processing plant personnel, plant operating equipment and the plant environment and its surroundings.

Among the chemicals in current use are: peracetic acid, acidified sodium chlorite (ASC), ozone, trisodium phosphate, cetylpyridinium chloride (CPC), organic acid rinses (lactic acid), hypobromous acid and chlorine dioxide. Some of these chemicals can be difficult to work with as a processing aid as they may require heating to become effective or are difficult to mix and stabilize prior to use. Certain of these chemicals are only specific for processing aid use to treat against specific pathogens on only certain foods. In addition, some of these chemicals can produce noxious fumes that over time have been linked to upper respiratory illness and typically require in-plant decontamination of their effluence.

Several large and established corporations currently supply these chemicals and also provide other related food safety services such as environmental sanitation programs and food safety consultation and audit services.

The Company believes that SDC as a natural product based on its proprietary silver-ion, which is stabilized in a citric acid solution, is well positioned as a new and disruptive technology. Given its broad spectrum antimicrobial efficacy and non-toxic properties, SDC provides significant improvements over current chemical interventions that the Company believes strengthens food safety practices for eliminating various pathogens present during food processing operations.

Pilot poultry processing studies showed that SDC achieved an average reduction in *Salmonella* of 2.75 log<sub>10</sub> CFU/cm<sup>2</sup> when applied as an OLR spray and 6.28 log<sub>10</sub> CFU/cm<sup>2</sup> when combined with an immersion chilling process simulating current U.S. industry practices. This data indicates that the use of SDC in poultry processing has the potential to achieve non-detectable *Salmonella* levels.

Pilot produce processing studies showed that SDC achieved average reductions up to 2.36 log<sub>10</sub> CFU/cm<sup>2</sup> when applied alone as a spray and up to 3.10 log<sub>10</sub> CFU/cm<sup>2</sup> when combined with chlorine wash, simulating current processing practices.

Currently, produce processors hope to achieve only a 1 log<sub>10</sub> CFU/cm<sup>2</sup> reduction per intervention treatment. This data suggests that by incorporating SDC, produce processors can improve their results 100-fold with only one step.

Sensory evaluations of both poultry and produce treated with SDC indicated no difference in color, appearance or odor to untreated controls; and SDC had no effect on the nutritional composition of either poultry or produce.

The Company believes that SDC is a significant improvement over current processing chemicals because the product is:

More effective in reducing or eliminating pathogens



Easier to handle and dilute

Non-corrosive to processing equipment

Non-toxic whereby it does not create noxious fumes or other detrimental environmental effluence  
The Company believes that the performance and characteristics of SDC represent as a significant advantage to food processors and provides significant improvement to the safety of processed foods going to consumers.

## **Sales and Marketing**

### ***Overview***

A critical aspect of our business strategy is to leverage the industry experience of our internal sales force and management team in order to maximize the commercial potential of our technology platform in the food industry. During 2013 and 2014, we strengthened our internal sales and marketing capability by adding to our team experienced food industry sales professionals and our chief executive officer and board members who have significant food industry management experience.

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According to the CDC, FDA and other food industry sources, food contamination and food borne illnesses have been increasing. We believe our focus on food safety is addressing a significant need to provide safe non-toxic and effective solutions to mitigate the increase of food contamination and food borne illnesses. We believe our products can be used effectively to prevent or mitigate the risk of food contaminants in various stages of the food supply chain. Our current sales and marketing efforts include demonstrating our SDC products' effectiveness as a hard surface disinfectant and sanitizer for:

1. Foodservice operators such as food preparation and cooking surfaces; consumer eating and common areas; and drink and ice dispensers.

2. Food manufacturers and processors such as food production and transportation equipment.

We intend to expand our market penetration in the food industry based on future product development and regulatory efforts to offer our SDC technology as a direct food contact processing aid where it is applied as a spray wash for poultry, produce and beef and pork as an intervention to prevent, reduce or eliminate various food-borne pathogens.

Our sales team is actively developing customer relationships with certain segments of foodservice operators, food processors and food manufacturers. Due to both the technical nature of our products and existence of established brands, the sales cycle to secure a new customer is long and unpredictable. We have recently conducted numerous successful product evaluation trials and comparative testing of our SDC-based products with prospective customers, which we believe will result in future revenue. We believe our products provide superior pathogen and hygiene control performance characteristics as compared with legacy chemical products, which also have higher toxicity profiles than our SDC-based products.

In addition to our direct sales and marketing efforts, we intend to selectively form partnerships with industry leaders for a variety of uses and applications of our products and technology. These partnerships may be for both U.S. and international markets where we believe we may leverage the product development, sales and marketing resources of business partners to commercialize our SDC technology in their respective markets.

A significant portion of our historical revenues were generated by an international chemical distributor who sold our SDC-based formulations to other manufacturers for use as a raw material ingredient in the production of personal care products. Other historical revenues were primarily to U.S. distributors who sold our SDC-based products into the consumer and industrial janitorial and sanitization market.

### ***Sales Concentration***

Net product sales were \$550,000 and \$820,000 for the years ended July 31, 2014 and 2013, respectively. For the year ended July 31, 2014, two customers accounted for 66% of our net product sales. No other individual customer accounted for 10% or more of our net product sales. The geographic breakdown of net product sales was as follows: 100% U.S. For the year ended July 31, 2013, three customers accounted for 69% of our net product sales. No other individual customer accounted for 10% or more of our net product sales. The geographic breakdown of net product sales was as follows: 86% U.S. and 14% foreign.

From time to time, one or a small number of our customers may represent a significant percentage of our revenue. Our two largest customers accounted for 66% of our revenue for the fiscal year ended July 31, 2014. One customer accounted for 51%, and the other for 15%. Although we have agreements with many of our customers, these

agreements typically do not prohibit customers from purchasing products and services from competitors. A decision by any of our major customers to significantly reduce the amount of product ordered or license fees paid, or their failure or inability to pay amounts owed to us in a timely manner, or at all, could have a significant adverse effect on our business.

### **Competition**

The markets for SDC, our SDC-based products and each of their potential applications are highly competitive. We have a number of competitors that vary in size, scope and breadth of products offered. Such competitors include some of the largest global corporations, and most of our competitors have significantly greater financial resources than we do. We expect to face additional competition from other competitors in the future.

Because SDC is a new antimicrobial technology to the food industry, our success will depend, in part, upon our ability to achieve a share of our target markets at the expense of established and future products. Even where SDC may have technological competitive advantages over competing products, we, our partners or our distributors, will need to invest significant resources in order to attempt to displace traditional technologies sold by, what are in many cases, well-known industry leaders.

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### **Manufacturing**

On December 11, 2013, the Company entered into a five-year strategic collaboration agreement with St. Louis-based Intercon Chemical Company (ICC). The agreement consists of a multi-prong approach to accelerate the commercialization of PURE's unique and proprietary SDC-based products. The strategic collaboration agreement provides:

ICC licenses from PURE its patents and technology know-how for the exclusive manufacture of our SDC-based products.

ICC will invest in plant improvements to allow for expanded SDC production.

ICC's R&D team will collaborate on SDC product line development.

ICC licenses the distribution rights for SDC-based products into its core businesses of institutional cleaning and sanitation products.

ICC will also develop a new initiative focused on US hospital, healthcare and medical facilities.

PURE earns royalty income on SDC-products sold by ICC and its affiliates.

The agreement may be terminated by mutual written consent, or by either party upon the material breach of the terms of the agreement by the other party.

Silver is the primary active ingredient in SDC and is a readily available commodity. The other active and inactive ingredients in our products are readily available from multiple sources.

### **Government Regulation**

Our business is subject to various government regulations relating to the protection of public health and the environment. Among these are laws that regulate the manufacture, storage, distribution and labeling of our products, as well as the use, handling, storage and disposal of certain materials in the manufacturing of our products.

#### ***Regulation in the United States***

Certain environmental and regulatory matters significant to us are discussed below.

#### **Requirements Imposed by the EPA and Similar State Agencies**

We manufacture and sell in the U.S. certain disinfecting products that kill or reduce microorganisms (bacteria, viruses, fungi). The manufacture, labeling, handling and use of these products are regulated by the EPA under the Federal Insecticide, Fungicide, and Rodenticide Act, or FIFRA. We currently sell three products registered by the EPA under

FIFRA, certain of which are approved for use on food contact surfaces and others of which are approved for use on non-food contact hard surfaces. EPA product registration requires meeting certain efficacy, toxicity and labeling requirements and paying ongoing registration fees.

Although states do not generally impose substantive requirements different from those of the EPA, each state in which our products are sold requires registration and payment of a fee. California and certain other states have adopted additional regulatory programs applicable to these types of products that, in some cases, impose a fee on total product sales in the state.

Based on our experience and our knowledge of current trends, we expect the costs and delays in receiving necessary federal and state approvals for these types of products may increase in the coming years.

*Requirements Imposed by Ingredient Legislation*

Numerous federal, state and local laws regulate the sale of products containing certain identified ingredients that may impact human health and the environment. For instance, California has enacted Proposition 65, which requires the disclosure of specified listed ingredient chemicals on the labels of products. Although none of the ingredients in our current products is reportable under Proposition 65, this and other similar legislation may become more comprehensive in the future and/or new products we may develop could be subject to these regulations.

*Requirements Imposed by Other Environmental Laws*

A number of federal, state and local environmental, health and safety laws govern the use, handling, storage and disposal of certain materials. Our current manufacturing process for SDC-based products is a zero waste process, meaning that no byproducts are created, and we do not use hazardous materials, as defined by applicable environmental laws, in the manufacturing of these products. As such, some of these U.S. environmental laws are not generally applicable to us in their current form. However, these laws may in the future identify as hazardous materials certain materials that we use in our manufacturing processes, or we may opt to or be forced to change our manufacturing procedures in a way that subjects our products or operations to these laws.

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### ***Requirements Imposed by the FDA and USDA***

Various laws and regulations have been enacted by federal, state, local and foreign jurisdictions regulating certain products we anticipate manufacturing and selling for controlling microbial growth on foods. In the United States, these requirements generally are administered by the FDA. However, the U.S. Department of Agriculture and EPA also may share in regulatory jurisdiction of antimicrobials applied directly to food as it pertains to poultry and meats.

### ***Regulation Outside the United States***

The commercialization of SDC-based products in countries other than the U.S. may require that we, or companies with whom we partner for such foreign commercialization, obtain necessary approvals from foreign regulatory authorities comparable to the EPA, among others. Applicable approval processes and ongoing requirements vary from country to country and may involve more time and expense than that required to obtain approvals in the U.S. In international markets, we currently sell our products under active registrations held by us, or by our distributors. We intend to continue to process registrations ourselves or through distributors as required.

We currently hold a registration from Health Canada for our disinfectant product. A third-party distributor holds a registration for our disinfectant products in South Africa. Other third-party distributors are actively pursuing registrations for our disinfectant products in various Asian markets. Additionally, an opinion has been granted under the Scientific Committee on Consumer Products to sell SDC in the European Union for use in cosmetics, which includes personal care products.

### **Employees**

As of October 28, 2014, we employed 12 regular full-time employees. We believe that we have been successful in attracting skilled and experienced personnel, but competition for personnel is intense and there can be no assurance that we will be able to attract and retain qualified personnel in the future. None of our employees are covered by collective bargaining agreements and we consider relations with our employees to be good.

### **Company Information**

We were incorporated in the state of California in August 1992 as Innovative Medical Services. In September 2003, we changed our name to Pure Bioscience. In March 2011, we reincorporated in the state of Delaware under the name Pure Bioscience, Inc.

Our corporate offices are located at 1725 Gillespie Way, El Cajon, California 92020. Our telephone number is (619) 596-8600. Our website address is [www.purebio.com](http://www.purebio.com). We make available free of charge on our website our periodic and current reports, proxy statements and other information as soon as reasonably practicable after such reports are filed with the Securities and Exchange Commission, or SEC. Information contained on, or accessible through, our website is not part of this report or our other filings with the SEC. Our SEC filings are also available to the public from the SEC's website at [www.sec.gov](http://www.sec.gov).

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### **Item 1A. Risk Factors**

*You should carefully consider the following information about risks and uncertainties that may affect us or our business, together with the other information appearing elsewhere in this Annual Report on Form 10-K, including our consolidated financial statements and the related notes thereto. If any of the following events, described as risks, actually occur, either alone or taken together, our business, financial condition, results of operations and future growth prospects would likely be materially and adversely affected. In these circumstances, the market price of our common stock could decline, and you may lose all or part of your investment in our securities. An investment in our securities is speculative and involves a high degree of risk. You should not invest in our securities if you cannot bear the economic risk of your investment for an indefinite period of time and cannot afford to lose your entire investment. There may be additional risks that we do not presently know of or that we currently believe are immaterial which could also impair our business and financial position.*

#### **Risks Related to Our Business and Industry**

##### **We have a history of losses, and we may not achieve or maintain profitability.**

We had a loss of \$11.1 million for the fiscal year ended July 31, 2014, and a loss of \$7.7 million for the fiscal year ended July 31, 2013. As of July 31, 2014, we have incurred a cumulative net loss of approximately \$81 million. Although we expect to continue to have losses in future periods, we are unable to predict the extent of our future losses or when or if we will become profitable, and it is possible we will never become profitable. Even if we do achieve profitability, we may not be able to sustain or increase profitability on an ongoing basis.

None of our existing agreements, including with Subway, contain provisions that guarantee us any minimum revenues. If the penetration into the marketplace of silver dihydrogen citrate, or SDC, and SDC-based products is unsuccessful, revenue growth is slower than anticipated or operating expenses exceed expectations, it may take an unforeseen period of time to achieve or maintain profitability and we may never achieve or maintain profitability. Slower than anticipated revenue growth could force us to reduce research, testing, development and marketing of our technologies, and/or force us to reduce the size and scope of our operations, to sell or license our technologies to third parties, or to cease operations altogether.

The risks associated with our business may be more acute during periods of economic slowdown or recession. In addition to other consequences, these periods may be accompanied by decreased consumer and institutional spending in general, as well as decreased demand for, or additional downward pricing pressure on, our products. Accordingly, any prolonged economic slowdown or a lengthy or severe recession with respect to either the U.S. or the global economy is likely to have a material adverse effect on our results of operations, financial condition and business prospects. As a result, given the current weakness and uncertainties in the U.S. and in certain overseas economies, we expect that our business will continue to be adversely affected for so long as, and to the extent that, such adverse economic conditions and uncertainty exist.

##### **Our future capital needs are uncertain, and we currently expect that we will need additional funds in the future which may not be available on acceptable terms or at all**

Our capital requirements will depend on many factors, including, among other factors:

the acceptance of, and demand for, our products;

the success of our strategic partners in developing and selling products derived from our technology;

the costs of further developing our existing, and developing new, products or technologies;

the extent to which we invest in new technology, testing and product development;

the timing of vendor payments and of the collection of receivables, among other factors affecting our working capital;

the exercise of outstanding options or warrants to acquire our common stock;

the number and timing of acquisitions and other strategic transactions, if any; and

the costs associated with the continued operation, and any future growth, of our business.

We believe that our current cash resources are sufficient to meet our anticipated needs during the next twelve months, however we do not yet have, and we may never have, significant cash inflows from product sales or from other sources of revenue to offset our ongoing and planned investments in corporate infrastructure, research and development projects, regulatory submissions, business development activities, and sales and marketing, among other investments. Some or all of our ongoing or planned investments may not be successful. In addition, irrespective of our cash resources, we may be contractually or legally obligated to make certain investments, which cannot be postponed.



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We expect that we will need to increase our liquidity and capital resources by one or more measures, which may include reducing operating expenses, raising additional financing in future periods through the issuance of debt, equity, or convertible securities, entering into partnerships, licenses, or other arrangements with third parties, reducing the exercise price of outstanding warrants, or through other means, any one of which could reduce the value to us, perhaps substantially, of our technology and its commercial potential. There is no guarantee that we would be able to obtain capital on terms acceptable to us, or at all. Insufficient funds would result in a material adverse effect on our business and operations and could cause us to fail to execute our business plan, fail to take advantage of future opportunities, or fail to respond to competitive pressures or customer requirements, and further may require us to delay, scale back or eliminate some or all of our research and product development programs, license to third parties the right to commercialize products or technologies that we would otherwise commercialize ourselves, or to reduce or cease operations. If adequate funds are not available when needed, we may be required to significantly modify our business model and operations to reduce spending to a sustainable level. Such modification of our business model and operations could also result in an impairment of assets which cannot be determined at this time. Furthermore, if we issue equity or convertible debt securities to raise additional funds, our existing shareholders may experience dilution, and in addition the new equity or debt securities may have rights, preferences and privileges senior to those of our existing shareholders. If we incur additional debt, it may increase our leverage relative to our earnings or to our equity capitalization.

As of October 28, 2014, we have 50,569,632 shares of common stock issued and outstanding or reserved for issuance. Shares reserved for issuance include shares under equity compensation plans, vested and unvested options, warrants, and unvested restricted stock units. Our current authorized capital stock is limited to 100,000,000 shares of common stock and 5,000,000 shares of preferred stock. Any increase in our authorized capital stock would require the approval of a majority of our shareholders as well as the approval of our Board of Directors. If we were unable to increase our authorized capital stock for any reason, our ability to raise additional capital through the issuance of equity or convertible debt would be severely compromised and we may be unable to obtain equity or convertible debt capital at all.

### **Raising additional funds by issuing securities or through collaboration and licensing arrangements may cause dilution to existing stockholders, restrict our operations or require us to relinquish proprietary rights.**

We expect that we will need to increase our liquidity and capital resources in future periods. We have a history of raising funds through offerings of our common stock, and we may in the future raise additional funds through public or private equity offerings, debt financings or corporate collaborations and licensing arrangements. To the extent that we raise additional capital by issuing equity securities, our stockholders' ownership will be diluted. Additionally, any debt financing we obtain may involve covenants that restrict our operations. These restrictive covenants may include, among other things, limitations on borrowing, specific restrictions on the use of our assets, as well as prohibitions on our ability to create liens on our assets, pay dividends on or redeem our capital stock or make investments. In addition, if we raise funds through collaboration and licensing arrangements, it may be necessary to grant licenses on terms that are not favorable to us or relinquish potentially valuable rights to our products or proprietary technologies. We may be required in future collaborations to relinquish all or a portion of our sales and marketing rights with respect to our products or license intellectual property that enable licensees to develop competing products in order to complete any such transaction.

As a result of the reverse stock split that we effected on August 14, 2012, the number of our outstanding shares of common stock was reduced at a ratio of one-for-eight, while the number of our authorized shares of common and preferred stock did not change. Accordingly, our authorized common stock remains 100,000,000 shares. In addition to capital raising activities, other possible business and financial uses for our authorized common stock include, without limitation, future stock splits, acquiring other companies, businesses or products in exchange for shares of common

stock, issuing shares of our common stock to partners in connection with strategic alliances, attracting and retaining employees by the issuance of additional securities under our various equity compensation plans, satisfying any debt we may have by issuing equity securities, or other transactions and corporate purposes that our Board of Directors, or Board, deems are in our best interest. Additionally, shares of common stock could be used for anti-takeover purposes or to delay or prevent changes in control or management of the Company. For example, without further stockholder approval, our Board could approve the sale of shares of common stock in a private transaction to purchasers who may oppose a takeover or favor our current Board. We cannot provide assurances that any issuances of common stock will be consummated on favorable terms or at all, that they will enhance stockholder value, or that they will not adversely affect our business or the trading price of our common stock.

Under our Certificate of Incorporation, our Board could also authorize the issuance of up to 5,000,000 shares of preferred stock on terms determined by the Board. If any common or preferred stock is issued, the interests of holders of our common stock could be diluted, and shares of preferred stock could be issued in a financing in which investors purchase preferred stock with rights, preferences and privileges that may be superior to those of the common stock, and the market price of our common stock could decline.

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**If outstanding options and warrants to purchase shares of our common stock are exercised, the interests of our stockholders could be diluted.**

As of July 31, 2014, in addition to 29,394,940 shares of common stock issued and outstanding, we had 462,343 shares reserved for issuance under equity compensation plans for vested and unvested stock options and 4,825,000 shares reserved for issuance for vested and unvested restricted stock units. We also had 849,012 shares reserved for issuance on the exercise of outstanding warrants.

We may elect to reduce the exercise price of outstanding warrants as a means of providing additional financing to us. The exercise of options and warrants, and the sale of shares underlying such options or warrants, could have an adverse effect on the market for our common stock, including the price that an investor could obtain for their shares. Investors may experience dilution in the net tangible book value of their investment upon the exercise of options and warrants currently outstanding, as well as options and warrants that may be granted or issued in the future.

**Because we are an early stage company, it is difficult to evaluate our prospects and our financial results may fluctuate, which may cause our stock price to fall.**

Since acquiring the rights to our SDC technology, we have encountered and likely will continue to encounter risks and difficulties associated with introducing or establishing our products in rapidly evolving markets. These risks include the following, among others:

we may not increase our sales to our existing customers and/or expand our customer base;

we may not succeed in materially penetrating markets and applications for our SDC technology;

our new sales and marketing strategy, which is built on our direct control of the sales and marketing of our products, may not be successful;

we may not be successful in obtaining any required regulatory approvals on a timely basis, or at all;

we or our partners and/or distributors may not establish or maintain effective marketing programs to create product awareness or brand identity;

our partners and/or distributors goals and objectives may not be consistent with our own;

we may not attract and retain key business development, technical and management personnel;

we may not maintain existing, or obtain new, regulatory approvals for our technology and products;

we may not succeed in locating strategic partners and licensees of our technology;

we may not effectively manage our anticipated growth, if any; and

we may not be able to adequately protect our intellectual property.

Any failure to successfully address these risks and uncertainties could seriously harm our business and prospects. We may not succeed given the technological, marketing, strategic and competitive challenges we face. In addition, because of our limited operating history and the early stage of market development for our SDC technology, we have limited insight into trends that may emerge and affect our business. Forecasting future revenues is difficult, especially because our technology is novel, and market acceptance of our products could change rapidly. In addition, our customers and potential customers in the foreseeable future are highly concentrated. Fluctuations in the buying patterns of our current or potential customers could significantly affect the level of our sales on a period to period basis. As a result, our financial results could fluctuate to an extent that may adversely affect our stock price. There are a number of other factors that could cause our financial results to fluctuate unexpectedly, including product sales, the mix of product sales, the cost of product sales, our ability for any reason to be able to meet demand, the achievement and timing of research and development and regulatory milestones, changes in expenses, including non-cash expenses such as the fair value of stock options granted, and manufacturing or supply issues, among other factors.

**A loss of one or more of our key customers could adversely affect our business.**

From time to time, one or a small number of our customers may represent a significant percentage of our revenue. Our two largest customers accounted for 66% of our revenue for the fiscal year ended July 31, 2014. One customer accounted for 51%, and the other for 15%. Although we have agreements with many of our customers, these agreements typically do not prohibit customers from purchasing products and services from competitors. A decision by any of our major customers to significantly reduce the amount of product ordered or license fees paid, or their failure or inability to pay amounts owed to us in a timely manner, or at all, could have a significant adverse effect on our business.

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### **We are dependent on our core SDC technology and if our efforts to achieve or maintain market acceptance of our core SDC technology are not successful, we are unlikely to attain profitability.**

We have and are currently focusing substantially all of our time and financial resources in the development and commercialization of our core SDC technology. We believe SDC has applications in multiple industries and we expect that sales of SDC and SDC-based products will constitute a substantial portion, or all, of our revenues in future periods. Any material decrease in the overall level of sales or expected sales of, or the prices for, SDC or SDC-based products, whether as a result of competition, change in customer demand, or any other factor, would have a materially adverse effect on our business, financial condition and results of operations. We are marketing our antimicrobial silver ion technology to industrial and consumer markets. These technologies and the products that incorporate them have not yet been accepted into the marketplace, and may never be accepted. In addition, even if our products achieve market acceptance, we may not be able to maintain product sales or other forms of revenue over time if new products or technologies are introduced that are more favorably received than our products, are more cost-effective or otherwise render our products less attractive or obsolete.

### **We are subject to intense competition.**

Our SDC-based products compete in highly competitive markets dominated by prominent chemical and pharmaceutical companies. Most of our competitors have been in business for a longer period of time than we have, and have a greater number of products on the market and greater financial and other resources than we do. Many of our competitors already have well established brands and distribution capabilities, and in some cases are able to leverage the sale of other products with more favorable terms for products competing with our own. We also have significantly fewer employees than virtually all of our competitors. Furthermore, recent trends in this industry are for large chemical and pharmaceutical companies to consolidate into a smaller number of very large entities, which further concentrates financial, technical and market strength and increases competitive pressure in the industry. If we directly compete with these very large entities for the same markets and/or products, their financial strength could prevent us from capturing a share of those markets. It is also possible that developments by our competitors will make our technologies or products noncompetitive or obsolete. Our ability to compete will depend upon our ability, and the ability of our distributors and other partners, to develop brand recognition and novel distribution methods, and to displace existing, established and future products in our relevant target markets. We, or our distributors and partners, may not be successful in doing so, which would have a materially adverse effect on our business, financial condition and results of operations.

### **We have limited sales, marketing and product distribution experience.**

We have limited experience in the sales, marketing and distribution of our products. While we previously relied primarily on product distribution arrangements and/or sales and marketing services provided by third parties, we have now developed and obtained registration by the Environmental Protection Agency, or EPA, of our proprietary brand, PURE® Hard Surface disinfectant and food contact surface sanitizer, and have resumed direct control of our sales of this product through a restructuring of our sales strategy and operations. Our new sales and marketing strategy requires that we enact various operational changes in our business, including making significant investments in our own sales and marketing organization. We intend to market and sell our PURE® Hard Surface and related SDC-based products into consumer, commercial and institutional markets through both traditional and alternative distribution channels. Additionally, Subway has agreed to make the Pure Hard Surface disinfectant available in its franchised locations in the U.S; however, we cannot assure you whether any franchisees will choose to purchase and use the product.

We have commenced the launch of a multi-channel national sales program, which involves our development of an internal team of industry sales experts to manage each of our key channels and our deployment of contract sales representatives within each of those channels. Our current sales, distribution and marketing strategies and programs may not be successful, and we may not be able to establish the sales, marketing, and distribution capabilities necessary to directly control and manage these aspects of our operations. If we are not able to successfully sell, market and distribute these products directly, we may seek to establish product distribution arrangements with third parties, which may not be available on terms acceptable to us, if at all.

**We rely on third parties to develop SDC-based products, and they may not do so successfully or diligently.**

On December 11, 2013, we entered into a five-year strategic collaboration agreement with St. Louis-based Intercon Chemical Company (ICC) where we granted ICC distribution and certain development rights and rights to be the exclusive manufacture for all our SDC-based products.

We may also rely in part, on other third parties to whom we license rights to our technology to develop and commercialize products containing SDC for many of the applications for which we believe SDC-based products have, or may have, market opportunities.

Our reliance on ICC and other third parties for development activities reduces our control over these activities. In such arrangements, we have relied, and expect in the future to rely, on the third party to fund and direct product development

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activities and appropriate regulatory filings. Any of these third parties may not be able to successfully develop such SDC-based products due to, among other factors, a lack of capital, a lack of appropriate diligence, insufficient devotion to sales efforts, a change in the evaluation by the third party of the market potential for SDC-based products, technical failures, and poorer than expected results from testing or trial use of any products that may be developed. If the third parties on which we rely are not successful in such development activities, our business and operating results would be adversely affected.

### **If we are unable to successfully develop or commercialize new applications of our SDC technology, or if such efforts are delayed, our operating results will suffer.**

In addition to its use on hard surfaces, we are pursuing potential applications of our SDC technology as a broad-spectrum antimicrobial for use as a direct food contact processing aid where it is applied as a wash for produce, meat and poultry as an intervention to prevent or kill various food-borne pathogens. Any product that may be developed in these fields may be delayed or may never achieve regulatory approval or be commercialized. Delays in achieving regulatory approvals for particular applications of our products could significantly impact our product development costs. If indications are commercialized, we may not receive a share of future revenues that provides an adequate return on our historical or future investment.

### **We are dependent on third-party manufacturers, over whom we have limited control, to manufacture our products.**

We do not have any manufacturing facilities ourselves and we currently rely on ICC to manufacture our SDC-based products and may in the future rely on one or more third-party manufacturers to properly manufacture our products. We may not be able to quickly replace our manufacturing capacity if ICC is unable to manufacture our products as a result of a fire, natural disaster (including an earthquake), equipment failure or other difficulty, or if such ICC facilities are deemed not in compliance with current good manufacturing practices, and the noncompliance could not be rapidly rectified. ICC is our single manufacturer for our SDC-based products and may not be replaced without significant effort and delay in production. A supply interruption or an increase in demand beyond our current manufacturer's capabilities could harm our ability to manufacture such products until new manufacturers are identified and qualified, which would have a significant adverse effect on our business and results. Any third-party manufacturer that we find may not match our quality standards or be able to meet customer requirements.

Additionally, our inability or reduced capacity to have our products manufactured would prevent us from successfully evaluating or commercializing our proposed products. Our dependence upon third parties for the manufacture of our products may adversely affect our profit margins and our ability to develop and deliver proposed products on a timely and competitive basis.

### **If we are not able to manage any growth we achieve effectively, we may not become profitable.**

If our efforts to achieve and maintain market acceptance of our SDC technology are successful, we will need to expand our business operations. We may not have sufficient resources to do so. If we invest in additional infrastructure, we may not be effective in expanding our operations and our systems, procedures or controls may not be adequate to support any such expansion. In addition, we would need to provide additional sales and support services to our partners, potentially in multiple markets, which we may not be able to do. Failure to properly manage increased customer demands, if any, could result in a material adverse effect on customer satisfaction, our ability to meet our contractual obligations, and our operating results.

### **The industries in which we operate are heavily regulated and we may be unable to compete effectively.**

We are focused on the marketing and continued development of our SDC antimicrobial technology. We believe that products derived from our SDC technology, or products that may be derived from our SDC technology in future periods, require or will require approval by government agencies prior to marketing or sale in the U.S. or in foreign markets. Complying with applicable government regulations and obtaining necessary approvals can be, and has historically been, time consuming and expensive, due in part, we believe, to the novel nature of our technology. Regulatory review could involve delays or other actions adversely affecting the development, manufacture, marketing and sale of our products. While we cannot accurately predict the outcome of any pending or future regulatory review processes or the extent or impact of any future changes to legislation or regulations affecting review processes, we expect such processes to remain time consuming and expensive as we, or our partners, apply for approval to make new or additional efficacy claims for current products or to market new product formulations. Obtaining approvals for new SDC-based products in the U.S., or in markets outside the U.S., could take several years, or may never be accomplished.

SDC is a platform technology rather than a single use applied technology. As such, products developed from the platform may fall under the jurisdiction of multiple U.S. and international regulatory agencies. Our disinfectant and sanitizer products are regulated in the U.S. by the EPA. In addition to the EPA, each of the 50 United States has its own government agencies that



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regulate the sale or shipment of our products into their state. We have obtained registration for these products from the EPA and all states into which such products are currently marketed and sold. We are required to meet certain efficacy, toxicity and labeling requirements and pay ongoing fees in order to maintain such registrations. We may not be able to maintain these registrations in the future, which may eliminate our continued ability to market and sell our products in some or all parts of the U.S. We also may not be able to obtain necessary registrations with the EPA and applicable states for other SDC disinfectant and sanitizer products that we or our partners may develop, which would limit our ability to sell any such products in the future.

Some potential applications of SDC, such as those aimed at healthcare, veterinary and certain food preparation markets, may require approval of other government agencies prior to marketing or sale in the U.S. or in foreign markets, such as the U.S Food and Drug Administration, or FDA, or the United States Department of Agriculture, or USDA. Obtaining FDA and/or USDA approval is a complicated and expensive process and such approvals may never be obtained for any SDC products. If FDA and/or USDA approvals are obtained, the approvals may limit the uses for which SDC products may be marketed such that they may not be profitable to us, and the applicable products would be subject to pervasive and continuing regulation by the FDA and/or USDA that could lead to withdrawal or limitation of any product approvals.

We intend to fund and manage certain of our EPA-regulated product development internally, in conjunction with engaging regulatory consultants and partnering with other third parties. We have partnered, or intend to partner, with third parties who are seeking, or intend to seek, approvals to market SDC-based products in markets outside the U.S., and with other third parties who are developing FDA-regulated SDC-based products who, upon such development, would seek FDA approvals of such products. Our ability to market and sell our products is dependent on our and our partners' ability to obtain and maintain required registrations and approvals of applicable regulatory agencies. Failure by our partners or us to comply with applicable regulations could result in fines or the withdrawal of approval for us or our partners and distributors to market our products in some or all jurisdictions or for certain indications, which could cause us to be unable to successfully commercialize SDC or otherwise achieve revenues from sales of such products.

### **We are subject to substantial regulation related to quality standards applicable to our manufacturing and quality processes, and our partners, including our third-party manufacture, failure to comply with applicable quality standards could affect our ability to commercialize SDC products.**

The EPA and other applicable U.S. and foreign government agencies regulate our and our partners' systems and processes, including those of ICC, for manufacturing SDC-based products. These regulations require that we and our partners observe good manufacturing practices in order to ensure product quality, safety and effectiveness. Failure by us or our partners to comply with current or future government regulations and quality assurance guidelines could lead to temporary manufacturing shutdowns, product recalls or related field actions, product shortages, and/or delays in product manufacturing, any or all of which could cause significant cost to us. Further, efficacy or safety concerns and/or manufacturing quality issues with respect to our products or those of our partners could lead to product recalls, fines, withdrawal of approvals, and/or declining sales, any or all of which could result in our failure to successfully commercialize SDC or otherwise achieve revenue growth.

### **Pricing and supply issues may have a material impact on our margins and our ability to supply our customers.**

All of the supply ingredients used to manufacture our products are available from multiple suppliers. However, commodity prices for some ingredients can vary significantly and the margins that we are able to generate could decline if prices rise. For example, both silver and citric acid prices have been volatile in recent periods.

In addition to such commodities, for finished products we also rely on producers of specialized packaging inputs such as bottles and labels. Due to their specialized nature, the supply of such inputs can be periodically constrained and result in additional costs to obtain these items, which may in turn inhibit our ability to supply products to our customers.

We are generally unable to raise our product prices to our customers, partners and distributors quickly to maintain our margins, and significant price increases for key inputs could therefore have an adverse effect on our results of operations. Price increases can also result in lost sales, and any inability to supply our customers' orders can lead to lost future sales to such customers.

While we expect to be the sole source supplier of SDC concentrate, in future periods we may use third parties to blend, package and provide fulfillment activities for our finished products. We expect that our margins would be reduced by using such third parties, and our ability to maintain product quality may not be as extensive or effective as when we produce these products in our own facility(ies). Any quality control issues could lead to product recalls and/or the loss of future sales, which would reduce our revenues and/or profits.

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### **If we suffer negative publicity concerning the safety or efficacy of our products, our sales may be harmed.**

If concerns should arise about the safety or efficacy of any of our products that are marketed, regardless of whether or not such concerns have a basis in generally accepted science or peer-reviewed scientific research, such concerns could adversely affect the market for those products. Similarly, negative publicity could result in an increased number of product liability claims, whether or not those claims are supported by applicable law.

### **Third parties may claim that we infringe their proprietary rights and may prevent us from manufacturing and selling some of our products.**

Our manufacture, use and sale of SDC-based products may subject us to lawsuits relating to the validity and infringement of patents or other proprietary rights of third parties. Litigation may be costly and time-consuming, and could divert the attention of our management and technical personnel. If we are found to have violated the trademark, trade secret, copyright, patent or other intellectual property or proprietary rights of others, such a finding could result in the need to cease use of a trademark, trade secret, copyrighted work or patented invention in our business and our obligation to pay a substantial amount for past infringement. If the rights holders are willing to permit us to continue to use their intellectual property rights, it may be necessary for us to enter into license arrangements with unfavorable terms and pay substantial amounts in royalty and other license fees. Either having to cease use or pay such fees could prevent us, or our third-party manufacture, from manufacturing and selling our products, which could make us much less competitive in our industry and have a material adverse impact on our business, operating results and financial condition.

### **We may become subject to product liability claims.**

As a business that manufactures and markets products for use by consumers and institutions, we may become liable for any damage caused by our products, whether used in the manner intended or not. Regardless of merit or potential outcome, product liability claims against us may result in, among other effects, the inability to commercialize our products, impairment of our business reputation, and distraction of management's attention from our primary business. If we cannot successfully defend ourselves against product liability claims we could incur substantial liabilities. Although we maintain general and product liability insurance, our insurance may not cover potential claims and may not be adequate to indemnify for liabilities that may be imposed. Any imposition of liability that is not covered by insurance or is in excess of insurance coverage could harm our business and operating results.

### **Litigation or the actions of regulatory authorities may harm our business or otherwise distract our management.**

Substantial, complex or extended litigation could cause us to incur major expenditures and would distract our management. For example, lawsuits against us or our officers or directors by employees, former employees, stockholders, partners, customers, or others, or actions taken by regulatory authorities, could be very costly and substantially disrupt our business. Such lawsuits and actions are not uncommon, and we may not be able to resolve such disputes or actions on terms favorable to us, and there may not be sufficient capital resources available to defend such actions effectively, or at all.

### **Maintaining compliance with our obligations as a public company may strain our resources and distract management, and if we do not remain compliant our stock price may be adversely affected.**

Our common stock is registered under the Exchange Act. It is therefore subject to the information, proxy solicitation, insider trading and other restrictions and requirements of the SEC under the Exchange Act. Both the U.S. Congress

and the SEC continue to issue new and proposed rules, and complying with existing and new rules has caused, and will continue to cause, us to devote significant financial and other resources to maintain our status as a public company. These regulatory costs and requirements will continue to increase our losses in future periods, and we expect that an increasing amount of management time and effort will be needed to meet our regulatory obligations. In addition, in April 2008 we obtained a listing of our common stock on The NASDAQ Capital Market, adding the additional cost and administrative burden of maintaining such a listing. Such costs significantly increased during the period between September 2011 and September 2012 due to a series of notices and a lengthy appeal process in connection with the potential delisting of our common stock from The NASDAQ Capital Market. However, NASDAQ delisted us and suspended trading in our securities effective with the open of business on Friday, May 17, 2013 as a result of our determination that we would be unable to evidence compliance with the \$2.5 million stockholders' equity requirement for continued listing on The NASDAQ Capital Market by June 18, 2013. On May 17, 2013 our common stock began trading on the OTCQB marketplace.

Section 404 of the Sarbanes-Oxley Act of 2002 requires that we evaluate our internal control systems and that management report on and attest to the adequacy of our internal controls. Recent SEC pronouncements suggest that in the next several years we may be required to report our financial results using new International Financial Reporting Standards, replacing GAAP, which would require us to make significant investments in training, hiring, consulting and information technology, among other investments. All of these and other reporting requirements and heightened corporate governance obligations that we

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face, or may face in the future, will further increase the cost to us, perhaps substantially, of remaining compliant with our obligations under the Exchange Act and other applicable laws, including the Sarbanes-Oxley Act and the Dodd-Frank Act of 2010. In order to meet these incremental obligations, we will need to invest in our corporate and accounting infrastructure and systems, and acquire additional services from third party auditors and advisors. As a result of these requirements and investments, we may incur significant additional expenses and may suffer a significant diversion of management's time. There is no guarantee that we will be able to continue to meet these obligations in a timely manner. If we fail to do so, we could be subject to sanctions or investigation by regulatory authorities such as the SEC. Any such actions could adversely affect the market price of our common stock, perhaps significantly.

**Our publicly filed reports are reviewed from time to time by the SEC, and any significant changes or amendments required as a result of any such review may result in material liability to us and may have a material adverse impact on the trading price of our common stock.**

The reports and other securities filings of publicly traded companies are subject to review by the SEC from time to time for the purpose of assisting companies in complying with applicable disclosure requirements. The SEC is required, pursuant to the Sarbanes-Oxley Act of 2002, to undertake a comprehensive review of a company's reports at least once every three years, although an SEC review may be initiated at any time. While we believe that our previously filed SEC reports comply, and we intend that all future reports will comply, in all material respects with the published rules and regulations of the SEC, we could be required to modify, amend or reformulate information contained in our filings as a result of any SEC review. Any modification, amendment or reformulation of information contained in such reports could be significant and result in material liability to us and have a material adverse impact on the trading price of our common stock.

**If we are unable to build and integrate our new management team, our business could be harmed.**

As previously announced on our Form 8-K filed with the SEC on August 20, 2013 and as described elsewhere in this Report, on August 13, 2013, Michael L. Krall, Donna Singer, and Dennis Atchley resigned all positions respectively held by them as officers of the Company and as members of the Board. Mr. Krall previously served as our Chief Executive Officer and interim Chief Financial Officer and on the Board. Ms. Singer served as our Executive Vice President and as a member of the Board and Mr. Atchley served as Corporate Secretary. Simultaneously with the resignations, Dave J. Pfanzelter was appointed by the Board to serve as Interim Chief Executive Officer and Chairman of the Board, Peter C. Wulff was appointed by the Board to serve as Chief Financial Officer, Chief Operating Officer, and Corporate Secretary and Gary D. Cohee was appointed by the Board to serve as a member of the Board.

On September 10, 2013, the Board appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. In connection with the hiring of Henry R. Lambert to serve as our Chief Executive Officer, Dave J. Pfanzelter resigned his position as our Interim Chief Executive Officer, but continues to serve as a member of the Board.

In October 2013, we appointed three additional members to the Board: Dr. David Theno, Jr., Craig Culver and William Otis.

On April 9, 2014, Mr. Culver resigned from our Board. There were no disagreements between Mr. Culver and the Company relative to his resignation.

On October 24, 2014, we appointed Tom Y. Lee, CPA, to the Board.

Our success depends largely on the execution of our business strategy by our management team. Management will be evaluating how to best execute our near-term strategy to drive customer adoption in the food industry by addressing food safety solutions across the supply chain in order to prevent or mitigate food contamination or the potential for food-borne illness with specific customer focus in foodservice providers, food processors and food manufacturers. However, we cannot assure you that management will succeed in driving customer adoption in the food industry or generally execute on our business strategy in the near-term or at all, which could harm our business and financial prospects. Further, integrating new management into existing operations may be challenging. If we are unable to effectively integrate our new management, our operations and prospects could be harmed.

**We depend on key personnel for our continued operations and future success, and a loss of certain key personnel could significantly hinder our ability to move forward with our business plan.**

Our success depends largely upon the continued services of our executive officers and other key personnel. Our executive officers and key personnel could terminate their employment with us at any time without notice and without penalty.

We do not maintain key person life insurance policies on our executive officers or other employees. The loss of one or more of our executive officers or key employees could seriously harm our business, results of operations, financial condition, and/or

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the market price of our common stock. We cannot assure you that in such an event we would be able to recruit qualified personnel able to replace these individuals in a timely manner, or at all, on terms acceptable to either us or to any qualified candidate.

### **Because competition for highly qualified business development and bioengineering personnel is intense, we may not be able to attract and retain the employees we need to support our potential growth.**

To successfully meet our objectives, we must attract and retain highly qualified business development and bioengineering personnel with specialized skill sets focused on the industries in which we compete, or intend to compete. Competition for qualified business development and bioengineering personnel can be intense. Our ability to meet our business development objectives will depend in part on our ability to recruit, train and retain top quality people with advanced skills who understand our technology and business. In addition, it takes time for our new personnel to become productive and to learn our business. If we are unable to hire or retain qualified business development and bioengineering personnel, it will be difficult for us to sell our products or to license our technology or to achieve or maintain regulatory approvals, and we may experience a shortfall in revenue and not achieve our anticipated, or any, growth.

### **We have recently had significant changes to the composition of our Board of Directors.**

On August 13, 2013, Michael L. Krall, Donna Singer, and Dennis Brovarone resigned as members of the Board. Subsequently on September 10, 2013, the Board appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. In October 2013, the Board appointed three additional members to the Board: Dr. David Theno, Craig Culver and Bill Otis. On April 9, 2014, Mr. Culver resigned from our Board. On October 24, 2014, we appointed Tom Y. Lee, CPA, to the Board. Following such resignations and appointments, the Board consists of six directors, three of whom are independent within the meaning of the applicable listing standards of the NYSE MKT.

The transition in the composition of our Board and its committees may result in inefficiencies in Board activity, disagreements regarding our business models or other operational strategies, and disruptions to our business, which may have an adverse effect on our business strategy and results of operations.

### **We may engage in strategic transactions that could impact our liquidity, increase our expenses and present significant distractions to our management.**

From time to time we may consider engaging in strategic transactions, such as acquisitions of companies, asset purchases and out-licensing or in-licensing of products, product candidates or technologies. Any such transaction may require us to incur non-recurring or other charges, may increase our near and long-term expenditures and may pose significant integration challenges or disrupt our management or business, which could adversely affect our operations and financial results. For example, these transactions may entail numerous operational and financial risks, including, among others, exposure to unknown liabilities, disruption of our business and diversion of our management's time and attention in order to develop acquired products, product candidates or technologies, difficulty and cost in combining the operations and personnel of any acquired businesses with our operations and personnel, and inability to retain key employees of any acquired businesses. Accordingly, although we may not choose to undertake or may not be able to successfully complete any transactions of the nature described above, any transactions that we do undertake or complete could have a material adverse effect on our business, results of operations, financial condition and prospects.

### **We may invest or spend our cash in ways with which you may not agree or in ways which may not yield a significant return.**

Our management has considerable discretion in the use of our cash. Our cash may be used for purposes that do not increase our operating results or market value. Until the cash is used, it may be placed in investments that do not produce significant income or that may lose value. The failure of our management to invest or spend our cash effectively could result in unfavorable returns and uncertainty about our prospects, each of which could cause the price of our common stock to decline.

**We may not be able to utilize all, or any, of our tax net operating loss carry-forwards and our future after-tax earnings, if any, could be reduced.**

At July 31, 2014, we had federal and California tax net operating loss carry-forwards of approximately \$83.6 million and \$71.8 million, respectively. Utilization of these net operating loss carry-forwards may be subject to a substantial annual limitation due to ownership change limitations that may have occurred, including with respect to our recent private placements, or that could occur in the future, as required by Section 382 of the Internal Revenue Code as well as similar state provisions. These ownership changes may limit the amount of net operating loss carry-forwards that can be utilized annually to offset future taxable income and tax, respectively. In general, an ownership change, as defined by Section 382 of the



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Internal Revenue Code, results from a transaction or series of transactions over a three-year period resulting in an ownership change of more than 50 percentage points of the outstanding stock of a company by certain stockholders or public groups. Since our formation, we have raised capital through the issuance of capital stock on several occasions (both before and after our initial public offering in 1996) which, combined with the purchasing stockholders subsequent disposition of those shares, may have resulted in such an ownership change, or could result in an ownership change in the future based upon subsequent disposition. While we believe that we have not experienced an ownership change, the pertinent tax rules related thereto are complex and subject to varying interpretations, and thus the applicable taxing authorities may take an alternative position.

Our current federal tax loss carry-forwards began expiring in the year ended July 31, 2011 and, unless previously utilized, will completely expire in the year ending July 31, 2034. The balance of our current federal net operating loss carry-forwards will expire between July 31, 2019 and July 31, 2034. Our California tax loss carry-forwards will begin to expire in the year ending July 31, 2015, and will completely expire in the year ending July 31, 2034. If we are unable to earn sufficient profits to utilize the carry-forwards by these dates, they will no longer be available to offset future profits, if any.

### **We are subject to tax audits by various tax authorities in multiple jurisdictions.**

From time to time we may be audited by tax authorities to whom we are subject. Any assessment resulting from such audits, if any, could result in material changes to our past or future taxable income, tax payable or deferred tax assets, and could require us to pay penalties and interest that could materially adversely affect our financial results.

### **Risks Related to Our Intellectual Property**

*If we are unable to obtain, maintain or defend the patent and other intellectual property rights relating to our technology, we or our collaborators and distributors may not be able to develop and market proprietary products based on our technology, which would have a material adverse impact on our results of operations.*

We rely and expect in the future to continue to rely on a combination of patent, trademark, trade secret and copyright protections, as well as contractual restrictions, to protect the proprietary aspects of our technology and business.

Legal protections of our intellectual property and proprietary rights afford only limited protection. For instance, we currently own twelve U.S. patents related to our SDC technology. The lives of these patents, and any patents that we may obtain in the future, are not indefinite, and the value to us of some or all of our patents may be limited by their terms. Further, although we have a number of U.S. and international patent applications pending, some or all of those applications may not result in issued patents, and the intellectual property claims therein would be unprotected. Additionally, obtaining and maintaining patent protection depends on our compliance with various procedural, document submission, fee payment and other requirements imposed by government patent agencies, and our patent protection could be reduced or eliminated for non-compliance with these requirements. Furthermore, the patent positions of bioscience companies can be highly uncertain and often involve complex legal, scientific and factual questions, and, therefore, we cannot predict with certainty whether we will be able to ultimately enforce our patents or other intellectual property rights. Third parties may challenge, invalidate or circumvent our patents and patent applications relating to our products, product candidates and technologies. In addition, our patent positions might not protect us against competitors with similar products or technologies because competing products or technologies may not infringe our patents.

From time to time, U.S. and other policymakers have proposed reforming the patent laws and regulations of their countries. In September 2011, after years of Congressional debate regarding patent reform legislation, President

Obama signed into law the America Invents Act (the Act) considered by many to be the most substantial revision of U.S. patent law since 1952. The Act's various provisions will go into effect over an 18-month period. The Act changes the current first-to-invent system to a system that awards a patent to the first-inventor-to-file for an application for a patentable invention. This change alters the pool of available materials that can be used to challenge patents and eliminates the ability to rely on prior research work in order to lay claim to patent rights. Disputes as to whether the first filer is in fact the true inventor will be resolved through newly implemented derivation proceedings. The Act also creates mechanisms to allow challenges to newly issued patents in the patent office in post-grant proceedings and new inter partes reexamination proceedings. Although many of the changes bring U.S. law into closer harmony with European and other national patent laws, the new bases and procedures may make it easier for competitors to challenge our patents, which could result in increased competition and have a material adverse effect on our product sales, business and results of operations. The changes may also make it harder to challenge third-party patents and place greater importance on being the first inventor to file a patent application on an invention.

In addition, to the extent that we operate internationally, the laws of foreign countries may not protect our proprietary rights to the same extent as the laws of the U.S. As stated above, many countries have a first-to-file trademark registration system, which may prevent us from registering or using our trademarks in certain countries if third parties have previously filed applications to register or have registered the same or similar trademarks. Additionally, changes in the patent and/or trademark

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laws or interpretations of such laws in the U.S. or other countries could diminish the value of our intellectual property rights. Moreover, our competitors may develop competing technologies that are not covered by the claims of, and therefore do not infringe upon, our issued patents, which could render our patents less valuable to us. If certain of our proprietary rights cannot be, or are not sufficiently, protected by patent and trademark registrations, it could have a material adverse impact on our business and our ability to commercialize or license our technology and products.

Our own efforts to protect our intellectual property and other proprietary rights may also be insufficient. Despite efforts to protect our proprietary rights, including without limitation through confidentiality and other similar contractual restrictions, our means of protecting such rights may not be adequate and unauthorized parties may attempt to copy aspects of our proprietary technology, obtain and use information that we regard as proprietary, or otherwise misappropriate our intellectual property. In addition, unpatented proprietary rights, including trade secrets and know-how, can be difficult to protect and may lose their value if they are independently developed by a third party or if their secrecy is lost. It is possible that, despite our efforts, competitors or others will create and use products, adopt service names similar to our service names or otherwise violate or misappropriate our proprietary rights. The infringement of such rights could have a material negative impact on our business and on our results of operations.

Litigation may be necessary to enforce our intellectual property and other proprietary rights, which would be expensive and could consume time and other resources. The result of any such litigation may be the court's ruling that our patents or other intellectual property rights are invalid and/or should not be enforced. Additionally, even if the validity of such rights is upheld, the court could refuse to stop a third party's infringing activity on the ground that such activities do not infringe our rights. The U.S. Supreme Court has recently revised certain tests regarding granting patents and assessing the validity of patents to make it more difficult to obtain patents. As a consequence, issued patents may be found to contain invalid claims according to the newly revised standards. Some of our patents may be subject to challenge and subsequent invalidation or significant narrowing of claim scope in a reexamination proceeding, or during litigation, under the revised criteria.

### **We may incur substantial costs as a result of litigation or other proceedings relating to patent and other intellectual property rights and we may be unable to protect our rights to, or use, our technology.**

If we choose to go to court to stop someone else from using the inventions claimed in our patents, that individual or company has the right to ask the court to rule that these patents are invalid and/or should not be enforced against that third party. These lawsuits are expensive and would consume time and other resources even if we were successful in stopping the infringement of these patents. In addition, there is a risk that the court will decide that these patents are not valid and that we do not have the right to stop the other party from using the inventions. There is also the risk that, even if the validity of these patents is upheld, the court will refuse to stop the other party on the ground that such other party's activities do not infringe our rights to these patents.

Furthermore, a third party may claim that we are using inventions covered by the third party's patent rights and may go to court to stop us from engaging in our normal operations and activities, including making or selling our products. These lawsuits are costly and could affect our results of operations and divert the attention of managerial and technical personnel. There is a risk that a court would decide that we are infringing the third party's patents and would order us to stop the activities covered by the patents. In addition, there is a risk that a court will order us to pay the other party damages for having violated the other party's patents. The biotechnology industry has produced a proliferation of patents, and it is not always clear to industry participants, including us, which patents cover various types of products or methods of use. The coverage of patents is subject to interpretation by the courts, and the interpretation is not always uniform. If we are sued for patent infringement, we would need to demonstrate that our products or methods of use either do not infringe the patent claims of the relevant patent and/or that the patent claims are invalid, and we may

not be able to do this. Proving invalidity, in particular, is difficult since it requires a showing of clear and convincing evidence to overcome the presumption of validity enjoyed by issued patents.

Because some patent applications in the United States may be maintained in secrecy until the patents are issued, patent applications in the United States and many foreign jurisdictions are typically not published until eighteen months after filing, and publications in the scientific literature often lag behind actual discoveries, we cannot be certain that others have not filed patent applications for technology covered by our issued patents or our pending applications or that we were the first to invent the technology. Our competitors may have filed, and may in the future file, patent applications covering technology similar to ours. Any such patent application may have priority over our patent applications and could further require us to obtain rights to issued patents covering such technologies. If another party has filed a United States patent application on inventions similar to ours, we may have to participate in an interference proceeding declared by the PTO, to determine priority of invention in the United States. The costs of these proceedings could be substantial, and it is possible that such efforts would be unsuccessful, resulting in a loss of our United States patent position with respect to such inventions.

Some of our competitors may be able to sustain the costs of complex patent litigation more effectively than we can because they have substantially greater resources. In addition, any uncertainties resulting from the initiation and continuation of any litigation could have a material adverse effect on our ability to raise the funds necessary to continue our operations.

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**Confidentiality agreements with employees and others may not adequately prevent disclosure of our trade secrets and other proprietary information and may not adequately protect our intellectual property, which could limit our ability to compete.**

We may rely in part on trade secret protection in order to protect our proprietary trade secrets and unpatented know-how. However, trade secrets are difficult to protect, and we cannot be certain that others will not develop the same or similar technologies on their own. We have taken steps, including entering into confidentiality agreements with our employees, consultants, outside scientific collaborators, sponsored researchers and other advisors, to protect our trade secrets and unpatented know-how. These agreements generally require that the other party keep confidential and not disclose to third parties all confidential information developed by the party or made known to the party by us during the course of the party's relationship with us. We also typically obtain agreements from these parties which provide that inventions conceived by the party in the course of rendering services to us will be our exclusive property. However, these agreements may not be honored and may not effectively assign intellectual property rights to us. Enforcing a claim that a party illegally obtained and is using our trade secrets or know-how is difficult, expensive and time consuming, and the outcome is unpredictable. In addition, courts outside the United States may be less willing to protect trade secrets or know-how. The failure to obtain or maintain trade secret protection could adversely affect our competitive position.

**We may be subject to claims that our employees have wrongfully used or disclosed alleged trade secrets of their former employers.**

As is common in the biotechnology, food, chemical and pharmaceutical industries, we employ individuals who were previously employed at other biotechnology, food, chemical or pharmaceutical companies, including our competitors or potential competitors. Although no claims against us are currently pending, we may be subject to claims that these employees or we have inadvertently or otherwise used or disclosed trade secrets or other proprietary information of their former employers. Litigation may be necessary to defend against these claims. Even if we are successful in defending against these claims, litigation could result in substantial costs and be a distraction to management.

## **Risks Related to our Common Stock**

***We failed to meet applicable NASDAQ Stock Market requirements and as a result we delisted our stock from The NASDAQ Capital Market, which could adversely affect the market liquidity of our common stock and harm our businesses.***

On May 15, 2013, we received a letter indicating that the NASDAQ Listing Qualifications Panel (the Panel) determined to delist our common stock from The NASDAQ Stock Market LLC. Trading in our securities on NASDAQ was suspended effective with the open of business on Friday, May 17, 2013. The suspension was the result of our determination that we would be unable to evidence compliance with the \$2.5 million stockholders' equity requirement for continued listing on The NASDAQ Capital Market, as set forth in NASDAQ Listing Rule 5550(b), by June 18, 2013, as required by the Panel's decision in this matter. On May 17, 2013, our common stock began trading on the OTC Markets' OTCQB marketplace under the ticker symbol PURE. We continue to file periodic reports with the Securities and Exchange Commission in accordance with the requirements of Section 12(g) of the Securities Exchange Act of 1934, as amended.

Our delisting from The NASDAQ Capital Market and commencement of trading on the OTCQB Marketplace has resulted and may continue to result in a reduction in some or all of the following, each of which could have a material adverse effect on our stockholders:

the liquidity of our common stock;

the market price of shares of our common stock;

our ability to obtain financing for the continuation of our operations;

the number of institutional and other investors that will consider investing in shares of our common stock;

the number of market makers in shares of our common stock;

the availability of information concerning the trading prices and volume of shares of our common stock; and

the number of broker-dealers willing to execute trades in shares of our common stock.

***Following the delisting of our common stock from The NASDAQ Capital Market, our common stock is deemed to be penny stock, which may make it more difficult for investors to sell their shares due to suitability requirements.***

As a result of the delisting of our common stock from the NASDAQ, shares of our common stock are subject to the so-called

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penny stock rules as that term is defined in Rule 3a51-1 promulgated under the Securities Exchange Act of 1934. These requirements may reduce the potential market for our common stock by reducing the number of potential investors. This may make it more difficult for investors in our common stock to sell shares to third parties or to otherwise dispose of them. This could cause our stock price to decline.

Broker-dealers dealing in penny stocks are required to provide potential investors with a document disclosing the risks of penny stock. Moreover, broker-dealers are required to determine whether an investment in a penny stock is a suitable investment for a prospective investor. Such requirements may discourage broker-dealers from effecting transactions in our common stock, which could limit the market price and liquidity of our common stock.

*The price of our common stock may be volatile, which may cause investment losses for our stockholders.*

The price and trading volume of our common stock have historically been volatile. For example, in the twelve months through July 31, 2014, the closing market price of our common stock ranged from \$0.50 per share to \$1.65 per share, and the monthly trading volume varied from approximately 573,000 shares to 3,603,000 shares. The market price of our common stock may continue to be volatile and could fluctuate substantially due to many factors, including, among others, the following:

actual or anticipated fluctuations in our results of operations;

the determination that our shares of common stock are penny stock which will require brokers trading in our shares of common stock to adhere to more stringent rules, likely resulting in a reduced level of trading activity in the secondary trading market for our shares of common stock;

the sale by us of our common or preferred stock or other securities, or the anticipation of sales of such securities;

the trading volume of our common stock, particularly if such volume is light;

the trading market of our common stock;

the introduction of new products or services, or product or service enhancements by us or our competitors;

developments with respect to our or our competitors' intellectual property rights or regulatory approvals or denials;

announcements of significant acquisitions or other agreements by us or our competitors;

sales or anticipated sales of our common stock by our insiders (management and directors);

conditions and trends in our industry;

changes in our pricing policies or the pricing policies of our competitors;

changes in the estimation of the future size and growth of our markets; and

general economic conditions.

In addition, the stock market in general, the OTCQB, and the market for shares of novel technology and biotechnology companies in particular, have experienced extreme price and volume fluctuations that in some cases may be unrelated or disproportionate to the operating performance of those companies. Further, the market prices of bioscience companies' stock have been unusually volatile in recent periods, and such volatility may continue for the foreseeable future. These broad market and industry factors may materially harm the market price of our common stock, regardless of our operating performance. In addition, this volatility could adversely affect an investor's ability to sell shares of our common stock, and/or the available price for such shares, at any given time.

Following periods of volatility in the market price of a company's securities, stockholder derivative lawsuits and securities class action litigation are common. Such litigation, if instituted against us or our officers and directors, could result in substantial costs and a diversion of management's attention and resources.

***Potential future sales or issuances of our common stock to raise capital, or the perception that such sales could occur, could cause dilution to our current stockholders and the price of our common stock to fall.***

Although we are pursuing various sources of potential funding, we have historically supported our operations through the issuance of equity and expect to continue to do so in the future. Although we may not be successful in obtaining financing through equity sales on terms that are favorable to us, if at all, any such sales that do occur could result in substantial dilution to the interests of existing holders of our common stock. Additionally, the sale of a substantial number of shares of our common stock or other equity securities to any new investors, or the anticipation of such sales, could cause the trading price of our common stock to fall.



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***We have never paid dividends on our capital stock, and we do not anticipate paying any cash dividends in the foreseeable future.***

The continued operation and expansion of our business will require substantial funding. Investors seeking cash dividends in the foreseeable future should not purchase our common stock. We have paid no cash dividends on any of our capital stock to date and we currently intend to retain our available cash to fund the development and growth of our business. Any determination to pay dividends in the future will be at the discretion of our Board and will depend upon results of operations, financial condition, contractual restrictions, restrictions imposed by applicable law and other factors our Board deems relevant. We do not anticipate paying any cash dividends on our common stock in the foreseeable future. Any return to stockholders will therefore be limited to the appreciation of their stock, which may never occur.

***Anti-takeover provisions under our charter documents and Delaware law could delay or prevent a change of control and could also limit the market price of our stock.***

Certain provisions of our charter and bylaws may delay or frustrate the removal of incumbent directors and may prevent or delay a merger, tender offer, or proxy contest involving us that is not approved by our Board, even if such events may be beneficial to the interests of stockholders. For example, our Board, without stockholder approval, has the authority and power to authorize the issuance of up to 5,000,000 shares of preferred stock and such preferred stock could have voting or conversion rights that could adversely affect the voting power of the holders of our common stock. Further, the one-for-eight reverse stock split of our outstanding common stock that we effected on August 14, 2012 has increased the proportion of unissued and authorized common shares to issued and outstanding common shares, which could allow our Board to issue large numbers of additional shares of our common stock that could significantly reduce the voting power of our current stockholders. In addition, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which may discourage, delay or prevent certain business combinations with stockholders owning 15% or more of our outstanding voting stock. These and other provisions in our charter documents may make it more difficult for stockholders or potential acquirers to initiate actions that are opposed by our then-current board of directors, including delaying or impeding a merger, tender offer, or proxy contest or other change of control transaction involving the Company. Any delay or prevention of a change of control transaction could cause stockholders to lose a substantial premium over the then-current market price of their shares.

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**Item 1B. Unresolved Staff Comments**

Not applicable.

**Item 2. Properties**

We lease a facility in El Cajon, California covering a total of approximately 7,400 square feet. This is our only facility and it includes our corporate offices, research and development laboratory and warehouse. Our current lease on this facility expires in December 2016.

**Item 3. Legal Proceedings**

From time to time, we may become involved in various lawsuits and legal proceedings which arise in the ordinary course of business. The impact and outcome of litigation, if any, is subject to inherent uncertainties, and an adverse result in these or other matters may arise from time to time that may harm our business. We are not currently aware of any such legal proceedings or claims to which we or our wholly owned subsidiary is a party or of which any of our property is subject that we believe will have, individually or in the aggregate, a material adverse effect on our business, financial condition or results of operations.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Table of Contents****PART II****Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities****Information About Our Common Stock**

Our common stock is approved for quotation on the OTC Markets OTCQB marketplace under the symbol PURE. The OTC QB is a regulated quotation service that displays real-time quotes, last-sale prices and volume information in over-the-counter equity securities. The OTC QB securities are traded by a community of market makers that enter quotes and trade reports. This market is limited in comparison to the national stock exchanges and any prices quoted may not be a reliable indication of the value of our common stock. On May 17, 2013 our common stock was delisted from The NASDAQ Capital Market and began trading on the OTCQB Marketplace under the ticker symbol PURE.

On October 24, 2014, the closing price of our common stock reported on the OTCQB was \$1.10 per share. The following table sets forth, for each of the quarterly periods indicated, the high and low sales prices of our common stock, as reported on the OTCQB. All per share information of our common stock has been adjusted to reflect the application of the reverse stock that we effected on August 14, 2012.

	<b>High</b>	<b>Low</b>
<b>Year Ended July 31, 2014</b>		
First Quarter	\$ 1.70	\$ 0.45
Second Quarter	\$ 1.57	\$ 1.02
Third Quarter	\$ 1.51	\$ 1.01
Fourth Quarter	\$ 1.20	\$ 0.95
<b>Year Ended July 31, 2013</b>		
First Quarter	\$ 3.57	\$ 0.90
Second Quarter	\$ 1.25	\$ 0.61
Third Quarter	\$ 0.86	\$ 0.48
Fourth Quarter	\$ 0.60	\$ 0.22

 **Holders**

As of October 24, 2014, we had approximately 112 holders of record of our common stock. This does not include beneficial owners holding common stock in street name.

**Dividend Policy**

We have never paid dividends and have no current plans to do so. We currently anticipate that we will retain all of our future earnings, if any, for use in the development and expansion of our business and for general corporate purposes. Any determination to pay dividends in the future will be at the discretion of our Board and will depend upon our results of operations, financial condition and other factors that the Board, in its discretion, may deem relevant.

**Repurchase of Equity Securities**

None.

**Information About Our Equity Compensation Plans**

The information required under this heading is incorporated herein by reference to the applicable information set forth in Item 12 of this Annual Report on Form 10-K.

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### **Item 6. Selected Financial Data**

As a Smaller Reporting Company, as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.

### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*All references to PURE, we, our, us and the Company in this Item 7 refer to Pure Bioscience, Inc. and our wholly owned subsidiary.*

*The discussion in this section contains forward-looking statements. These statements relate to future events or our future financial performance. We have attempted to identify forward-looking statements by terminology such as anticipate, believe, can, continue, could, estimate, expect, intend, may, plan, potential, predict, should, would or will or the negative of these terms or other comparable terminology, but their absence does not mean that a statement is not forward-looking. These statements are only predictions and involve known and unknown risks, uncertainties and other factors, which could cause our actual results to differ from those projected in any forward-looking statements we make. Several risks and uncertainties we face are discussed in more detail under Risk Factors in Part I, Item 1A of this Annual Report or in the discussion and analysis below. You should, however, understand that it is not possible to predict or identify all risks and uncertainties and you should not consider the risks and uncertainties identified by us to be a complete set of all potential risks or uncertainties that could materially affect us. You should not place undue reliance on the forward-looking statements we make herein because some or all of them may turn out to be wrong. We undertake no obligation to update any of the forward-looking statements contained herein to reflect future events and developments, except as required by law. The following discussion should be read in conjunction with the consolidated financial statements and the notes to those statements included elsewhere in this Annual Report on Form 10-K.*

*Unless otherwise noted, all information in this Item 7 regarding share amounts of our common stock and prices per share of our common stock has been adjusted to reflect the application of the one-for-eight reverse stock split of our common stock that we effected on August 14, 2012, as further described below, on a retroactive basis.*

## **Overview**

### ***Company Overview***

We are focused on developing and commercializing our proprietary antimicrobial products primarily in the food safety arena that provide solutions to the health and environmental challenges of pathogen and hygienic control. Our technology platform is based on patented stabilized ionic silver, and our initial products contain silver dihydrogen citrate, or SDC. SDC is a broad-spectrum, non-toxic antimicrobial agent, which offers 24-hour residual protection and formulates well with other compounds. As a platform technology, SDC is distinguished from existing products in the marketplace because of its superior efficacy, reduced toxicity and the inability of bacteria to form a resistance to it. SDC is manufactured as a liquid delivered in various concentrations. We currently manufacture and distribute SDC-based disinfecting and sanitizing products, which are registered by the Environmental Protection Agency, or EPA. We also manufacture and sell SDC-based formulations to manufacturers for use as a raw material ingredient in the production of personal care products. We believe our technology platform has potential application in a number of industries. We intend to focus our current resources on providing food safety solutions to the food industry.

Our goal is to become a sustainable company by commercializing our proprietary technology platform to deliver leading antimicrobial products through our sales and marketing efforts focused on the food industry and through licensing collaborations in other industries. Our current products are as follows:

Product Name	Product Use	EPA Registration
PURE Complete Solution: PURE® Hard Surface	Disinfectant and sanitizer	SDC3A
PURE Multi-Purpose Cleaner Concentrate	Cleaner	Not applicable
PURE Multi-Purpose Hi-Foam Cleaner Concentrate	Cleaner	Not applicable
Axen® 30(1)	Disinfectant	Axen30
Axenohl®	Raw material ingredient	Axenohl
Silvérion®	Raw material ingredient	Not applicable

(1) We intend to phase out Axen® 30

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### ***PURE Complete Solution***

Our PURE Complete Solution is comprised of PURE<sup>®</sup> Hard Surface and concentrated cleaning products that were launched as companion products to PURE<sup>®</sup> Hard Surface. The PURE Complete Solution offers a comprehensive, cost-effective and user-friendly cleaning, disinfecting and sanitizing product line to end-users including our targeted foodservice, food manufacturing and food processing customers. We can also target this product line to hospital and medical care facilities; janitorial service providers and the distributors that supply them.

### ***PURE<sup>®</sup> Hard Surface Disinfectant and Sanitizer (Ready-to-Use)***

PURE<sup>®</sup> Hard Surface is our SDC-based, patented and EPA-registered, ready-to-use hard surface disinfectant and food contact surface sanitizer. We manufacture both consumer and commercial versions of the product. PURE Hard Surface combines high efficacy and low toxicity with 30-second bacterial and viral kill times and 24-hour residual protection. The product completely kills resistant pathogens such as MRSA and Carbapenem-resistant *Klebsiella pneumoniae* (NDM-1), and effectively eliminates dangerous fungi and viruses including HIV, Hepatitis B, Hepatitis C, Norovirus, Influenza A, Avian Influenza and H1N1. It also eradicates hazardous food pathogens such as *E. coli*, *Salmonella*, *Campylobacter* and *Listeria*. PURE<sup>®</sup> Hard Surface delivers broad-spectrum efficacy yet remains classified as least-toxic by the EPA. The active ingredient, SDC, has been designated as Generally Recognized as Safe, or GRAS, for use on food processing equipment, machinery and utensils.

### ***PURE Multi-Purpose Cleaner Concentrate (End-User Dilutable)***

PURE<sup>®</sup> Multi-Purpose Cleaner, is an environmentally responsible cleaning product that is protected by SDC. SDC ensures the quality and safety of PURE<sup>®</sup> Multi-Purpose Cleaner without human or environmental exposure to toxic chemical preservatives. PURE<sup>®</sup> Multi-Purpose Cleaner is non-toxic and non-flammable and contains no EDTA, phosphates, ammonia or bleach as well as no VOCs or NPEs. PURE Multi-Purpose Cleaner provides professional strength cleaning in a concentrate formula that yields a 1:96 – 1:256 use dilution that is safe for use on all resilient surfaces, including floors, glass and food contact surfaces.

### ***PURE Multi-Purpose Hi-Foam Cleaner Concentrate (End-User Dilutable)***

PURE<sup>®</sup> Multi-Purpose Hi-Foam Cleaner is an environmentally responsible, professional strength high foam forming cleaning product that is protected by SDC. SDC ensures the quality and safety of PURE Multi-Purpose Hi-Foam Cleaner without human or environmental exposure to toxic chemical preservatives. PURE Multi-Purpose Hi-Foam Cleaner is non-toxic and non-flammable and contains no EDTA, phosphates, ammonia or bleach as well as no VOCs or NPEs. PURE Multi-Purpose Hi-Foam Cleaner provides high foam cleaning in a concentrate formula that yields a 1:50 use dilution that is safe for use on stainless steel equipment, resilient floors, walls and painted surfaces.

### ***Axen<sup>®</sup> 30 (Ready-to-Use)***

Axen<sup>®</sup>30 is our patented and EPA-registered hard surface disinfectant and is a predecessor ready-to-use product to PURE<sup>®</sup> Hard Surface. Axen30 is currently sold on a limited basis by distributors under their respective private labels which we intend to phase out.

### ***Axenohl<sup>®</sup> (Raw Material Ingredient)***

Axenohl<sup>®</sup> is our patented and EPA-registered SDC-based antimicrobial formulation for use as a raw material ingredient in the manufacturing of EPA-registered products. Axenohl is a colorless, odorless and stable solution that

provides fast acting efficacy against bacteria, viruses and fungi when manufactured into consumer and commercial disinfecting and sanitizing products.

***SILVÉRIION® (Raw Material Ingredient)***

SILVÉRIION® is our patented SDC-based antimicrobial formulation for use as a raw material ingredient in the manufacturing of personal care products. It can be used as either an active ingredient or a preservative. SILVÉRIION is a colorless, odorless and stable solution that provides ionic silver in a water-soluble form. It provides fast acting efficacy at low concentrations against a broad-spectrum of bacteria, viruses, yeast and molds. SILVÉRIION is currently sold outside of the United States in various personal care products.



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We were incorporated in the state of California in August 1992 as Innovative Medical Services. In September 2003, we changed our name to Pure Bioscience. In March 2011, we reincorporated in the state of Delaware under the name Pure Bioscience, Inc. We operate in one business segment.

## **Recent Corporate Developments**

### ***New Board of Directors and Management Team***

On August 13, 2013, the following managerial and corporate governance changes occurred to create a new Board of Directors, or Board, and management team:

Michael L. Krall, Donna Singer, and Dennis Brovarone resigned as members of the Board;

Michael L. Krall, Donna Singer, and Dennis Atchley resigned all positions respectively held by them as officers of the Company;

Dave J. Pfanzelter was appointed by the Board to be the Chairman of the Board;

Dave J. Pfanzelter was appointed by the Board to serve as Interim Chief Executive Officer;

Gary D. Cohee was appointed by the Board to serve as a member of the Board; and

Peter C. Wulff was appointed by the Board to serve as Chief Financial Officer, Chief Operating Officer, and Corporate Secretary.

On July 22, 2013, Jon Carbone and Paul Maier resigned as directors of the Company and as members of the Audit and Compensation Committees.

On September 10, 2013, the Board appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. In connection with the hiring of Henry R. Lambert to serve as our Chief Executive Officer, Dave J. Pfanzelter resigned his position as our Interim Chief Executive Officer. Mr. Pfanzelter continues to render significant services to us and continues to serve as our Chairman of the Board.

In October 2013, we appointed three additional members to the Board; Dr. David Theno, Jr., Craig Culver and William Otis. On April 9, 2014, Craig Culver resigned from the Board. There were no disagreements between Mr. Culver and the Company relative to his resignation.

On October 24, 2014, we appointed Tom Y. Lee, CPA, to the Board. The Board now consists of six members who provide professional experience in business and finance; food science and food safety; foodservice and food manufacturing; and distribution.

### ***Early Extinguishment of Debt***

On January 25, 2013, we entered into a Letter Agreement (the Agreement ) with Morrison & Foerster LLP ( Morrison ). Under the terms of the Agreement, we issued a Promissory Note (the Note ) in favor of Morrison in the principal amount of \$1,125,000. In consideration for the Note, Morrison agreed to waive \$1,519,000 of amounts due and payable to Morrison for legal services rendered. The Note bore interest at the rate of 7.5% per annum, but the then outstanding balance would accrue interest at the rate of 10% per annum upon the occurrence of an event of default (as defined in the Note). Beginning March 31, 2013, and on or before the last business day of each calendar month thereafter, we were required to pay all accrued but unpaid interest on the then unpaid amount of outstanding principal. Beginning on February 28, 2014, we were required to pay equal monthly principal installments of approximately \$47,000, plus interest. We could prepay the outstanding balance under the Note in full or in part at any time, which would result in a discount of the then outstanding balance. The Note was to mature on February 28, 2016, unless accelerated pursuant to an event of default or upon the consummation of a change of control. As a result of the Agreement, we reclassified the amount due and payable to Morrison from accounts payable to note payable during the fiscal year ended July 31, 2013.

In consideration for Morrison's acceptance of the Note in lieu of payment for its legal services, we issued Morrison a warrant to purchase 375,000 shares of our common stock at an exercise price of \$0.83 per share. The warrant was exercisable immediately and expires on January 24, 2018. The warrant may be exercised by Morrison with a cash payment or, in lieu thereof, at its election, through a net exercise, as set forth in the warrant agreement. Neither the warrant nor the shares to be

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issued upon exercise thereof are registered for sale or resale under the Securities Act of 1933, as amended (the Securities Act ), and have been or will be issued in reliance on an exemption from registration under the Securities Act pursuant to Section 4(a)(2) thereof based on the offering of such securities to one investor and the lack of any general solicitation or advertising in connection with such issuance. We determined that the warrants issued in connection with the Note were equity instruments and did not represent derivative instruments. The fair value of the warrants issued to Morrison was \$245,000, based on the Black-Scholes valuation method assuming no dividend yield, volatility of 134%, a risk-free interest rate of 0.35%, and an expected life of five years.

During the fiscal year ended July 31, 2014, we entered into a Promissory Note Payoff Agreement ( Payoff Agreement ) with Morrison. Under the Payoff Agreement, we paid \$500,000 in cash to Morrison to extinguish \$1,227,000 in unsecured debt owed to Morrison under the Note, dated January 25, 2013. We have no further obligations or liability under the Note. As a result of the Payoff Agreement, we recorded a gain of \$727,000 that is reflected in the other income (expense) section of the consolidated statement of operations.

## ***Financial Overview***

This financial overview provides a general description of our revenue and expenses.

### **Revenue**

We manufacture and sell SDC-based products for end use, and as a raw material for manufacturing use. We also license our products and technology to development and commercialization partners. Revenue is recognized when realized or realizable and earned. Any amounts received prior to satisfying revenue recognition criteria are recorded as deferred revenue.

### **Cost of Goods Sold**

Cost of goods sold for product sales includes direct and indirect costs to manufacture products, including materials consumed, manufacturing overhead, shipping costs, salaries, benefits, reserved inventory, and related expenses of operations. Depreciation related to manufacturing is systematically allocated to inventory produced, and expensed through cost of goods sold at the time inventory is sold.

### **Selling, General and Administrative**

Selling, general and administrative expense consists primarily of salaries and other related costs for personnel in business development, sales, finance, accounting, information technology, and executive functions. Other selling, general and administrative costs include product marketing, advertising, and trade show costs, as well as public relations and investor relations, facility costs, and legal, accounting and other professional fees.

### **Research and Development**

Our research and development activities are focused on leveraging our technology platform to develop additional proprietary products and applications. Research and development expense consists primarily of personnel and related costs, product registration expenses, and third-party testing. We expense research and developments costs as incurred.

### **Other Income (Expense)**

We record interest income, interest expense, change in derivative liabilities, as well as other non-operating transactions, as other income (expense) in our consolidated statements of operations.

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**Table of Contents****Results of Operations Comparison of the Years Ended July 31, 2014 and 2013*****Fluctuations in Operating Results***

Our results of operations have fluctuated significantly from period to period in the past and are likely to continue to do so in the future. We anticipate that our results of operations will be affected for the foreseeable future by several factors that may contribute to these periodic fluctuations, including fluctuations in the buying patterns of our current or potential customers for which we have no visibility, the mix of product sales including a change in the percentage of higher or lower margin formulations and packaging configurations of our products, the cost of product sales including component costs and contract labor as needed to meet fluctuations in demand not supportable by our existing workforce, our inability for any reason to be able to meet demand, the achievement and timing of research and development and regulatory milestones, unforeseen changes in expenses, including non-cash expenses such as the fair value of stock options granted, the calculation of which includes several variable assumptions, and unforeseen manufacturing or supply issues, among other issues. Due to these fluctuations, we believe that the period-to-period comparisons of our operating results are not a reliable indication of our future performance. As of the date of this filing, other than the impact of our change in corporate strategy, we are not aware of any trends in these factors or events or conditions that we believe are reasonably likely to impact our results of operations in the future.

***Net Product Sales***

Net product sales were \$550,000 and \$820,000 for the years ended July 31, 2014 and 2013, respectively. The decrease of \$270,000 was primarily attributable to sales fluctuations within our existing legacy customer base. Our top three customers accounted for \$397,000 of net product sales for the year ended July 31, 2014.

For the year ended July 31, 2014, two individual customers accounted for 66% of our net product sales. No other individual customer accounted for 10% or more of our net product sales. The geographic breakdown of net product sales was as follows: 100% U.S.

For the year ended July 31, 2013, three individual customers accounted for 69% of our net product sales. No other individual customer accounted for 10% or more of our net product sales. The geographic breakdown of net product sales was as follows: 86% U.S. and 14% foreign.

***Cost of Goods Sold***

During the fiscal year ended July 31, 2014, we established an inventory reserve of \$128,000 for slow moving finished goods inventory that was manufactured in prior years. During the fiscal year ended July 31, 2013, we established a reserve for \$347,000. The majority of the reserve related to components such as, plastic bottles, spray triggers, miscellaneous plastics, and numerous corrugated cardboard configurations.

Cost of goods sold was \$344,000 and \$565,000 for the years ended July 31, 2014 and 2013, respectively. The decrease of \$221,000 was primarily attributable to decreased product sales. Cost of goods sold, excluding the inventory reserves discussed above, was \$216,000 and \$218,000 for the years ended July 31, 2014 and 2013, respectively. The decrease is primarily attributable to periodic inventory adjustments that took place during the current year, as well as, the sale of higher margin products during the prior year.

Gross margin, as a percentage of net product sales, or gross margin percentage, was 37% and 31% for the years ended July 31, 2014 and 2013, respectively. Gross margin percentage, excluding the reserves discussed above, was 61% and 73% for the years ended July 31, 2014 and 2013, respectively. The decrease in gross margin percentage was primarily

attributable to the sale of lower margin formulations and packaging configurations of our products during the year ended July 31, 2014 as compared with prior year.

***Selling, General and Administrative Expense***

Selling, general and administrative expense was \$5,056,000 and \$5,154,000 for the years ended July 31, 2014 and 2013, respectively. The decrease of \$98,000 was primarily attributable to reductions in personnel costs, professional services, and facility costs.

***Research and Development Expense***

Research and development expense was \$1,032,000 and \$1,169,000 for the years ended July 31, 2014 and 2013, respectively. The decrease of \$137,000 was primarily attributable to decreases in personnel and related costs.

***Share-Based Compensation***

Share-based compensation expense was \$2,958,000 and \$720,000 for the years ended July 31, 2014 and 2013, respectively. The increase of \$2,238,000 is primarily due to the restricted stock units granted to employees and directors supporting our selling, general and administrative, and research and development functions (See Note 9).

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***Other Share-Based Expenses***

Other share-based expense was \$308,000 and zero for the years ended July 31, 2014 and 2013, respectively. The increase is due to \$285,000 of expense incurred from the amendment of the subscription agreements for investors who participated in the October 2013 private placements and \$23,000 of expense associated with warrants issued in connection with the April 24, 2013 private placement (See Note 8).

***Restructuring Costs***

Restructuring expense was \$2,754,000 and zero for the years ended July 31, 2014 and 2013, respectively. As discussed above, on August 13, 2013, Michael L. Krall, Donna Singer, and Dennis Brovarone resigned all positions respectively held by them as officers and directors of the Company and a new management team and Board were appointed. Based on the corporate governance change we incurred the following expenditures:

Mr. Krall and Ms. Singer received a onetime separation payment of \$150,000 and \$45,000, respectively; Mr. Brovarone received \$91,000, payable in 60 monthly installments of \$1,600, commencing 120 days after the separation date; Mr. Krall is entitled to receive a cash severance of \$540,000 payable over an eighteen month period; Ms. Singer is entitled to receive a cash severance of \$204,000 payable over a twelve month period; Mr. Krall received 850,000 shares of common stock, valued at \$595,000; Ms. Singer received 300,000 shares of common stock, valued at \$210,000; and Mr. Krall and Ms. Singer will continue to receive health insurance coverage over the terms of their respective severance periods. Medical and dental insurance for Mr. Krall and Ms. Singer will cost the Company \$20,000 and \$18,000, respectively. Per the terms of the agreements, we recorded a onetime expense of \$1,782,000 related to Mr. Krall's and Ms. Singer's separation payments, future severance payments, stock received, and future medical and dental insurance payments. All but \$7,000 due to Mr. Brovarone was accrued in prior periods for services previously provided.

We issued 300,000 shares of common stock to Bibicoff & MacInnis for investor relations services related to the corporate restructuring, valued at \$210,000.

We issued 250,000 shares of common stock, with a value of \$175,000, for corporate finance and restructuring activities to Wulff Services Inc. Wulff Services, Inc. is primarily owned by our current Chief Financial Officer / Chief Operating Officer, Peter C. Wulff. In addition, Wulff Services, Inc. received a onetime payment of \$75,000 related to the corporate finance and restructuring efforts.

We issued 300,000 shares of registered common stock, with a value of \$210,000, for corporate reorganization services previously provided by the principal of Pillar Marketing Group, Inc. In addition, Pillar also received a onetime payment of \$152,000 related to the reorganization efforts.

We incurred \$73,000 in legal fees associated with the corporate finance and restructuring activities. In addition, on January 23, 2014, we entered into a settlement agreement with a former employee. Under the terms of the agreement, we will pay \$50,000 over a six-month period with payments commencing in March 2014, and issue 15,000 shares of common stock valued at \$20,000.

***Impairment of Patents***

Due to the significant changes in our strategic business objectives and utilization of our assets, we have determined cost associated with the pending patent applications in numerous foreign geographic locations have been impaired. As a result, during our year ended July 31, 2013, we reduced the carrying value of our patents and recorded a \$551,000 patent impairment. There were no patent impairments for our year ended July 31, 2014.

***Change in Derivative Liability***

Change in derivative liability for the years ended July 31, 2014 and 2013 was a decrease of \$55,000 and an increase of \$268,000, respectively. The change is primarily due to adjustments of the estimated fair value, and the settlement of derivative warrants exercised during the year ended July 31, 2014 (See Note 5).

***Interest Expense, net***

Interest expense for the years ended July 31, 2014 and 2013 was \$10,000 and \$593,000, respectively. The decrease was primarily attributable to non-cash amortization of debt discounts recognized in the prior year related to the secured convertible promissory notes that we issued in July 2012 in connection with the Bridge Loan.

***Gain on Extinguishment of Debt***

Gain on extinguishment of debt for the year ended July 31, 2014 and 2013 was \$727,000 and zero respectively. The \$727,000 gain is attributable to the repayment of the Promissory Note (See Note 4).



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***Other (Expense) Income, net***

Other income for the year ended July 31, 2014 was \$190,000 compared with other expense of \$7,000 for year ended July 31, 2013. The increase is primarily attributable to the sale of reserved inventory and accounts payable vendor settlements.

**Liquidity and Capital Resources**

Since our inception, we have financed our operations primarily through public and private offerings of securities, debt financing, and revenue from product sales and license agreements. We have a history of recurring losses, and as of July 31, 2014 we have incurred a cumulative net loss of \$81,221,000.

For the year ended July 31, 2014, we completed private placements pursuant to which we sold 12,082,194 shares of our common stock. The shares were sold at a per share purchase price ranging from \$0.20 per share to \$1.00 per share, resulting in approximately \$6,777,000 in aggregate proceeds to the Company. After deducting fees of \$160,000, the net proceeds to us were \$6,617,000. The shares of common stock issued under the private placements were offered and sold without registration under the Securities Act of 1933, as amended (the Securities Act), or state securities laws, in reliance on the exemptions provided by Section 4(a)(2) of the Securities Act and Regulation D promulgated thereunder and in reliance on similar exemptions under applicable state laws, based on the lack of any general solicitation or advertising in connection with the sale of the securities; the representation of each investor to the Company that it is an accredited investor (as that term is defined in Rule 501 of Regulation D) and that it was purchasing the securities for its own account and without a view to distribute them. The securities may not be offered or sold in the United States without an effective registration statement or pursuant to an exemption from applicable registration requirements.

In addition, during the year ended July 31, 2014, we received \$337,000 from the exercise of warrants to purchase 518,000 shares of our common stock. There were no stock options exercised in the current year.

During the year ended July 31, 2014, we entered into a promissory note payoff agreement with Morrison & Foerster LLP (Morrison). Under the payoff agreement, we paid \$500,000 to Morrison to extinguish \$1,227,000 in unsecured debt owed to Morrison under the note, dated January 25, 2013. We have no further obligations or liability under the note (See Note 4).

As of July 31, 2014, we had \$86,000 in cash and cash equivalents compared to \$32,000 in cash and cash equivalents as of July 31, 2013. Additionally, as of July 31, 2014, we had \$1,829,000 of current liabilities, including \$1,096,000 in accounts payable, compared to \$2,153,000 of current liabilities, including \$1,134,000 in accounts payable as of July 31, 2013. The net decrease in current liabilities primarily relates to the repayment of the Morrison promissory note, offset by the terms of Mr. Krall's and Ms. Singer's separation agreements discussed above. All future severance and medical and dental insurance liabilities for Mr. Krall, Ms. Singer, and Mr. Brovarone have been accrued and are reflected in the restructuring liability section of the consolidated balance sheets.

During the period from July 31, 2014 until present, we issued a total of 9,990,659 shares of common stock and warrants to purchase 3,996,259 shares of common stock for gross proceeds of approximately \$7.49 million. The shares of common stock and the warrants issued under the private placements were offered and sold without registration under the Securities Act, or state securities laws, in reliance on the exemptions provided by Section 4(a)(2) of the Securities Act and Regulation D promulgated thereunder and in reliance on similar exemptions under applicable state laws, based on the lack of any general solicitation or advertising in connection with the sale of the securities; the representation of each investor to the Company that it is an accredited investor (as that term is

defined in Rule 501 of Regulation D) and that it was purchasing the securities for its own account and without a view to distribute them. The securities, including the shares underlying the warrants, may not be offered or sold in the United States without an effective registration statement or pursuant to an exemption from applicable registration requirements.

The following table summarizes our contractual obligations as of July 31, 2014.

	<b>Total</b>	<b>Payments due by period</b>		
		<b>Less than 1 year</b>	<b>1-3 years</b>	<b>3-5 years More than 5 years</b>
Operating lease obligations	\$ 203,000	\$ 83,000	\$ 120,000	
	\$ 203,000	\$ 83,000	\$ 120,000	

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In addition, from time to time we have entered into employment agreements with our executives that, under certain cases, provide for the continuation of salary and certain other benefits if these executives are terminated under specified circumstances. These agreements generally expire upon termination for cause or when we have met our obligations under these agreements. As of July 31, 2014, no events have occurred resulting in the obligation of any such payments. On August 13, 2013, we entered into Purchase, Severance, and Release Agreements with our named executive officers, which is further described in Item 11 to this Annual Report and Note 7 to the audited consolidated financial statements set forth in Part II, Item 8 of this Annual Report.

Our future capital requirements depend on numerous forward-looking factors. These factors may include, but are not limited to, the following: the acceptance of, and demand for, our products; our success and the success of our partners in selling our products; our success and the success of our partners in obtaining regulatory approvals to sell our products; the costs of further developing our existing products and technologies; the extent to which we invest in new product and technology development; and the costs associated with the continued operation, and any future growth, of our business. The outcome of these and other forward-looking factors will substantially affect our liquidity and capital resources.

We expect that we will need to increase our liquidity and capital resources by one or more measures. These measures may include, but are not limited to, the following: reducing operating expenses; obtaining financing through the issuance of equity, debt, or convertible securities; entering into partnerships, licenses, or other arrangements with third parties; and reducing the exercise price of outstanding warrants. Any one of these measures could substantially reduce the value to us of our technology and its commercial potential as it may be necessary to enter into arrangements with less favorable terms than otherwise possible. Additionally, a reduction in operating expenses will require a reduction in the sales, marketing, and other commercialization activities required to bring our products to market. If we issue equity, debt or convertible securities to raise additional funds, our existing stockholders may experience dilution, and the new equity, debt or convertible securities may have rights, preferences and privileges senior to those of our existing stockholders. There is no guarantee that we would be able to obtain capital on terms acceptable to us, or at all.

If we are unable to obtain sufficient capital, it would have a material adverse effect on our business and operations. It could cause us to fail to execute our business plan, fail to take advantage of future opportunities, or fail to respond to competitive pressures or customer requirements. It also may require us to delay, scale back or eliminate some or all of our research and development programs, to license to third parties the right to commercialize products or technologies that we would otherwise commercialize ourselves, or to reduce or cease operations altogether. If adequate funds are not available when needed, we may be required to significantly modify our business model and operations to reduce spending to a sustainable level.

We believe our current efforts to raise capital, our current efforts to market and sell our products, and our ability to significantly reduce expenses, will provide sufficient cash resources to satisfy our needs over the next 12 months. However, we do not yet have, and we may never have, significant cash inflows from product sales or from other sources of revenue to offset our ongoing and planned investments in corporate infrastructure, research and development projects, regulatory submissions, business development initiatives, and sales and marketing activities, among other investments. Some or all of our ongoing or planned investments may not be successful and could result in further losses. In addition, irrespective of our cash resources, we may be contractually or legally obligated to make certain investments which cannot be postponed.

## **Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition and results of operations are based on our audited consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the

United States, or GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures. We evaluate our estimates on an ongoing basis. We base our estimates on historical experience and on other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

We believe the following accounting policies and estimates are critical to aid you in understanding and evaluating our reported financial results.

***Revenue Recognition***

We sell our products to distributors and end users. We record revenue when we sell products to our customers, rather than when our customers resell products to third parties. When we sell products to our customers, we reduce the balance of our inventory with a corresponding charge to cost of goods sold. We do not currently have any consignment sales.

Terms of our product sales are generally FOB shipping point. Product sales are recognized when delivery of the products has occurred (which is generally at the time of shipment), title has passed to the customer, the selling price is fixed or

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determinable, collectability is reasonably assured and we have no further obligations. Any amounts received prior to satisfying these revenue recognition criteria are recorded as deferred revenue. We record product sales net of discounts at the time of sale and report product sales net of such discounts.

We also license our products and technology to development and commercialization partners. License fee revenue consists of product and technology license fees earned. If multiple-element arrangements require on-going services or performance, then upfront product and technology license fees under such arrangements are deferred and recognized over the period of such services or performance. Non-refundable amounts received for substantive milestones are recognized upon achievement of the milestone. Any amounts received prior to satisfying these revenue recognition criteria are recorded as deferred revenue.

### ***Share-Based Compensation***

We grant equity-based awards under share-based compensation plans. We estimate the fair value of share-based payment awards using the Black-Scholes option valuation model. This fair value is then amortized over the requisite service periods of the awards. The Black-Scholes option valuation model requires the input of subjective assumptions, including price volatility of the underlying stock, risk-free interest rate, dividend yield, and expected life of the option. Share-based compensation expense is based on awards ultimately expected to vest, and therefore is reduced by expected forfeitures. Changes in assumptions used under the Black-Scholes option valuation model could materially affect our net loss and net loss per share.

### ***Impairment of Long-Lived Assets***

In accordance with GAAP, if indicators of impairment exist, we assess the recoverability of the affected long-lived assets by determining whether the carrying value of such assets can be recovered through undiscounted future operating cash flows. If impairment is indicated, we measure the amount of such impairment by comparing the carrying value of the asset to the fair value of the asset and we record the impairment as a reduction in the carrying value of the related asset and a charge to operating results. Estimating the undiscounted future cash flows associated with long-lived assets requires judgment, and assumptions could differ materially from actual results. During the year ended July 31, 2013 we incurred, \$551,000 of expense relating to the impairment of long-lived assets (See Note 3). No impairment expense was recorded during the year ended July 31, 2014.

For purposes of testing impairment, we group our long-lived assets at the lowest level for which there are identifiable cash flows independent of other asset groups. Currently, there is only one level of aggregation for our intangible assets. We assess the impairment of long-lived assets, consisting of property, plant, equipment and finite-lived intangible assets primarily consisting of the worldwide patent portfolio of our silver ion technologies, annually, or whenever events or circumstances indicate that the carrying value may not be recoverable. Examples of such events or circumstances include:

an asset group's inability to continue to generate income from operations and positive cash flow in future periods;

loss of legal ownership or title to an asset;

significant changes in our strategic business objectives and utilization of the asset(s); and

the impact of significant negative industry or economic trends.

Additionally, on a quarterly basis we review the significant assumptions underlying our impairment assessment to determine that our previous conclusions remain valid. As part of our review, we consider changes in revenue growth rates, operating margins, working capital needs and other expenditures. With the exception of the impairment discussed above we have not identified any asset groups where undiscounted cash flows were not substantially in excess of carrying value.

Recoverability of assets to be held and used in operations is measured by a comparison of the carrying amount of an asset to the future net cash flows expected to be generated by the assets. The factors used to evaluate the future net cash flows, while reasonable, require a high degree of judgment and the results could vary if the actual results are materially different than the forecasts. In addition, we base useful lives and amortization or depreciation expense on our subjective estimate of the period that the assets will generate revenue or otherwise be used by us. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less selling costs.

We also periodically review the lives assigned to our intangible assets to ensure that our initial estimates do not exceed any revised estimated periods from which we expect to realize cash flows from the technologies. If a change were to occur in any of the above-mentioned factors or estimates, the likelihood of a material change in our reported results would increase.

#### ***Derivative Financial Instruments***

We do not use derivative instruments to hedge exposures to cash flow or market or foreign currency risks.

We review the terms of the common stock, warrants and convertible debt we issue to determine whether there are derivative

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instruments, including embedded conversion options that are required to be bifurcated and accounted for separately as derivative financial instruments. In circumstances where the host instrument contains more than one embedded derivative instrument, including a conversion option, that is required to be bifurcated, the bifurcated derivative instruments are accounted for as a single, compound derivative instrument.

Derivatives are initially recorded at fair value and are then revalued at each reporting date with changes in the fair value reported as non-operating income or expense. When the equity or convertible debt instruments contain embedded derivative instruments that are to be bifurcated and accounted for as liabilities, the total proceeds received are first allocated to the fair value of all the bifurcated derivative instruments. The remaining proceeds, if any, are then allocated to the host instruments themselves, usually resulting in those instruments being recorded at a discount from their face value.

## **Recent Accounting Pronouncements**

Information regarding recent accounting pronouncements is contained in Note 2 to the Consolidated Financial Statements, included elsewhere in this report.

## **Off Balance Sheet Arrangements**

We do not have any off balance sheet arrangements.

## **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

As a Smaller Reporting Company as defined by Rule 12b-2 of the Exchange Act and in Item 10(f)(1) of Regulation S-K, we are electing scaled disclosure reporting obligations and therefore are not required to provide the information requested by this Item.

## **Item 8. Consolidated Financial Statements and Supplementary Data**

The consolidated financial statements and supplementary data required by this Item 8 are set forth at the end of this Annual Report.

## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

Not applicable.

## **Item 9A. Controls and Procedures**

### **Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports 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 Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

As required by Rule 13a-15(b) under the Exchange Act, our management conducted an evaluation, under the supervision and with the participation of our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Annual Report. Based on the foregoing evaluation, our principal executive officer and principal financial officer concluded that as of the end of the period covered by this report our disclosure controls and procedures were effective.

### **Changes in Our Controls**

There were no changes in our internal controls over financial reporting during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect our internal controls over financial reporting.

### **Management's Report on Internal Control Over Financial Reporting**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Exchange Act Rules 13a-15(f) and 15d-15(f). With the participation of our Chief Executive Officer and Chief Financial Officer, management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the



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framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on its evaluation under this framework, our management concluded that our internal control over financial reporting was effective as of July 31, 2014.

**Item 9B. Other Information**

None.

Table of Contents**PART III****Item 10. Directors, Executive Officers and Corporate Governance****Information Regarding Our Board of Directors**

Pursuant to our bylaws, the number of directors is fixed and may be increased or decreased from time to time by resolution of our Board of Directors, or the Board. The Board has fixed the number of directors at six members.

Information with respect to our current directors is shown below.

<b>Name</b>	<b>Age</b>	<b>Director Since</b>	<b>Position(s) Held</b>
Dave J. Pfanzelter	61	2013	Chairman
Henry R. Lambert	63	2013	Director, Chief Executive Officer
Gary D. Cohee	68	2013	Director
David Theno, Jr., PhD	64	2013	Director
William Otis	58	2013	Director
Tom Y. Lee, CPA	65	2014	Director

**Dave J. Pfanzelter** was appointed as our Chairman on August 13, 2013. He previously served as a director of the Company from February 2013 to July 2013. Mr. Pfanzelter served as senior vice president of Kellogg Company, president of Kellogg's Specialty Channels and president of Kellogg Canada from May 2004 to May 2010, while also serving as part of the Kellogg Executive Committee and Global Leadership Team. Mr. Pfanzelter began his career in the food service industry in 1975 with Oscar Mayer Foods Corporation, serving in several key sales and marketing positions, including director of marketing and national sales manager. In 1995 he was appointed vice president of sales of Kraft Foodservice, representing the combined manufactured brands of Oscar Mayer, General Foods, and Kraft Foods. In 1998 Mr. Pfanzelter joined Keebler, serving as vice president and general manager of the food service division prior to Keebler's acquisition by Kellogg in 2001. Since 1998 Mr. Pfanzelter has been on the board of directors of Doctor's Associates, the parent company of Subway Restaurants, the nation's largest restaurant chain. In February 2012, Mr. Pfanzelter joined the Advisory Board of Wrigley Foods. He also served on the Board of the International Food Service Manufacturer's Association as chairman and member of its executive committee.

**Henry R. Lambert** joined our Board and was appointed as our Chief Executive Officer on September 10, 2013. Mr. Lambert is an accomplished food industry and consumer products executive with broad management skills, including strategic planning and business development, go-to-market execution, business integration and food safety. He has over 35 years of food industry experience, having worked at such notable companies as Heublein Inc.; RJ Reynolds; Nabisco, Inc.; and, Pinnacle Foods. He has held various business unit leadership positions servicing the foodservice and leading consumer food brands markets. Mr. Lambert has also served on boards and as a member of various food industry associations, including the International Foodservice Manufacturers Association (IFMA), Institute of Food Technologists and Safe Supply of Affordable Food Everywhere (SSAFE). From 2010 through June 2013, Mr. Lambert served as general manager of the global food and water business of Underwriter Laboratories, where he was responsible for the start-up of the company's food safety services business. From 2007 to 2010, Mr. Lambert served as Senior Vice President of Business Development, and then President, of Arrowstream Transportation, Inc., a provider of innovative supply chain management solutions to the foodservice industry whose key customers included Wendy's, Applebee's, Arby's, TGIF, Sysco, and DMA. Prior to 2007, Mr. Lambert held executive positions with a number of high profile companies in the foodservice industry. Mr. Lambert earned his

MBA in Finance from the University of Chicago, Booth School of Business, and his BA in Economics (with Honors) from Union College, Schenectady, N.Y.

**Gary D. Cohee** was appointed to our Board on August 13, 2013. He has over 40 years of experience as an investment banker, having started his career in 1973 with Blyth, Eastman Dillon. Since 2004 Mr. Cohee has served as President and CEO of PMB Securities Corp. From 2011 until 2012 Mr. Cohee served on the Advisory Board of Force Fuels, Inc. During his career in the investment banking business Mr. Cohee worked for a number of prestigious firms, including Bateman Eichler and Paulson Investment Company. Mr. Cohee graduated from California State University-Long Beach in 1968 with a BS degree in Business Administration. He is Past President of Long Beach Bond Club; Southern California Options Society; and Long Beach Century Club.

**David Theno, Jr., PhD** joined our Board on October 1, 2013. Dr. Theno is a widely respected food safety expert, previously served on the Company's Advisory Panel. Dr. Theno is currently the Chief Executive Officer of Gray Dog Partners, Inc., a technical consulting firm specializing in food safety and manufacturing, restaurant operations, supply chain management,

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strategic planning and facility design, where he served since October 2008. Gray Dog Partners has also provided consultation to federal, state and local regulatory bodies. From 1993 to 2008, Dr. Theno was employed by Jack in the Box, Inc. where he last served as the Senior Vice President and Chief Food Safety Officer and previously served as Corporate Vice President Technical Services. Dr. Theno has two Doctorate Degrees in Food Science and Animal Science and also Master's Degrees in Animal Science and Veterinary Pharmacology from the University of Illinois.

**William Otis** was appointed to our Board on October 8, 2013. Mr. Otis is currently the President and Chief Operating Officer of Patrick Cudahy, LLC and Saratoga Food Specialties. Both companies are food manufacturing companies of John Morrell Food Group and Smithfield Foods. Mr. Otis began his career in 1980 with Oscar Mayer Foods Corporation serving in several operations, finance and marketing positions. In 1995, Mr. Otis joined Patrick Cudahy, serving as Vice President of Sales and Marketing and in 2004 was promoted to President and COO. Mr. Otis also took over the President and COO role at Saratoga Food Specialties in 2012. Mr. Otis earned his Master's Degree in Business Management from the University of Wisconsin-Madison.

**Tom Y. Lee, CPA** was appointed to our Board on October 24, 2014. Mr. Lee is currently the Chairman and CEO of Swabplus, Inc., a contract manufacturer of single-dose applicator and formulation OEM products, and has served as Chairman and CEO since 2008. Mr. Lee has experience in manufacturing and selling applicator and formulation OEM products, manufacturing and distributing products in Asia and is experienced in accounting matters. Mr. Lee was formerly audit committee chairman at First Continental Bank (which merged with United Commercial Bank in 2003). Mr. Lee has been an active CPA since 1983 and earned his Master of Science in accounting from California State University Long Beach and his Bachelors in Business Administration from TamKang University in Taipei, Taiwan.

**Information Regarding Our Executive Officers**

Information with respect to our current named executive officers is shown below. Since Henry R. Lambert also serve as a member of the Board, his executive officer's biography is set forth under Information Regarding the Board of Directors above.

<b>Name</b>	<b>Age</b>	<b>Position(s) Held</b>	<b>Position(s) Held Since</b>
Henry R. Lambert	63	Chief Executive Officer	2013
Peter C. Wulff	55	Chief Financial Officer / Chief Operating Officer	2012

**Peter C. Wulff** was appointed as our Chief Financial Officer and Chief Operating Officer on August 13, 2013. He previously served as our Chief Financial Officer from November 2012 until May 2013. Mr. Wulff served as the principal of Wulff Services Inc. from May 2011 until October 2012 and from May 2013 to August 2013, a consulting services firm focusing on development stage companies in the medical technology industry. From June 2008 until April 2011 Mr. Wulff provided services for Alphatec Holdings, Inc. (NASDAQ: ATEC) and Alphatec Spine, a developer and manufacturer of spinal implant products, serving as its Chief Financial Officer, Vice President and Treasurer from June 2008 until October 2010, and its Senior Vice President, Strategic Initiatives, from October 2010 until April 2011. He also served as a Partner and Managing Director for two of Alphatec Spine's subsidiaries, respectively. From January 2005 until May 2008 he served as the Chief Financial Officer, and from February 2007 until May 2008 he also served as the Executive Vice President, of Artes Medical, Inc., a formerly publicly traded medical device company. Artes Medical is no longer publicly traded and filed for bankruptcy protection within two years after the departure of Mr. Wulff. From June 2004 until December 2004, Mr. Wulff was a managing partner of Acumen Biomedical, a consulting services firm that specialized in providing services to medical technology companies. From May 2001 to May 2004, Mr. Wulff served as Vice President Finance, Chief Financial Officer,

Treasurer and Assistant Secretary of CryoCor, Inc., a medical device company. From November 1999 to May 2001, Mr. Wulff served as Chief Financial Officer and Treasurer of Natural Alternatives International, Inc., a publicly traded and international nutritional supplement manufacturer. Mr. Wulff earned an M.B.A. in Finance and a bachelor's degree in Economics and Germanic Languages, each from Indiana University.

### **Family Relationships**

There is no family relationship between any current director or executive officer, or any director or executive officer during the fiscal year ended July 31, 2014.

### **Corporate Governance**

#### **Overview**

We are committed to maintaining the highest standards of business conduct and corporate governance, which we believe are

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fundamental to the overall success of our business, serving our stockholders well and maintaining our integrity in the marketplace. Our Corporate Governance Guidelines and Code of Business Conduct and Ethics, together with our Certificate of Incorporation, Bylaws and the charters of our Board Committees, form the basis for our corporate governance framework. As discussed below, our Board of Directors has established two standing committees to assist it in fulfilling its responsibilities to the Company and its stockholders: the Audit Committee and the Compensation Committee. The Board of Directors performs the functions typically assigned to a Nominating and Corporate Governance Committee.

## **Recent Corporate Developments**

### ***New Board of Directors and Management Team***

On August 13, 2013, the following managerial and corporate governance changes occurred to create a new Board of Directors, or Board, and management team:

Michael L. Krall, Donna Singer, and Dennis Brovarone resigned as members of the Board;

Michael L. Krall, Donna Singer, and Dennis Atchley resigned all positions respectively held by them as officers of the Company;

Dave J. Pfanzelter was appointed by the Board to be the Chairman of the Board;

Dave J. Pfanzelter was appointed by the Board to serve as Interim Chief Executive Officer;

Gary D. Cohee was appointed by the Board to serve as a member of the Board; and

Peter C. Wulff was appointed by the Board to serve as Chief Financial Officer, Chief Operating Officer, and Corporate Secretary.

On July 22, 2013, Jon Carbone and Paul Maier resigned as directors of the Company and as members of the Audit and Compensation Committees.

On September 10, 2013, the Board appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. In connection with the hiring of Henry R. Lambert to serve as our Chief Executive Officer, Dave J. Pfanzelter resigned his position as our Interim Chief Executive Officer. Mr. Pfanzelter continues to render significant services to us and continues to serve as our Chairman of the Board.

In October 2013, we appointed three additional members to the Board; Dr. David Theno, Jr., Craig Culver and William Otis. On April 9, 2014, Craig Culver resigned from the Board. On October 24, 2014, we appointed Tom Y. Lee, CPA, to the Board. The Board now consists of six members who provide professional experience in business and finance; food science and food safety; foodservice and food manufacturing; and distribution. We believe our new Board will be able to contribute incremental insight and guidance on business strategy from their collective experience

in business and finance; food science and food safety; and foodservice and food manufacturing.

### **Corporate Governance Guidelines**

Our Corporate Governance Guidelines are designed to ensure effective corporate governance of our Company. Our Corporate Governance Guidelines cover topics including, but not limited to, director qualification criteria, director responsibilities, director compensation, director orientation and continuing education, communications from stockholders to the Board, succession planning and the annual evaluations of the Board and its Committees. Our Corporate Governance Guidelines are reviewed regularly by the Board and revised when appropriate. The full text of our Corporate Governance Guidelines can be found in the Corporate Governance section of our website accessible at [www.purebio.com](http://www.purebio.com). A printed copy may also be obtained by any stockholder upon request to our Corporate Secretary.

### **Code of Business Conduct and Ethics**

We have adopted a Code of Business Conduct and Ethics that applies to all of our employees, officers and directors. This Code constitutes a code of ethics as defined by the rules of the SEC. This Code also contains whistle blower procedures adopted by our Audit Committee regarding the receipt, retention and treatment of complaints related to accounting, internal accounting controls or auditing matters and procedures for confidential anonymous employee complaints related to questionable accounting or auditing matters. Copies of the code may be obtained free of charge from our website, [www.purebio.com](http://www.purebio.com). Any amendments to, or waivers from, a provision of our code of ethics that applies to any of our executive officers will be posted on our website in accordance with the rules of the SEC. Other than as specifically referenced herein, the information contained on, or that can be accessed through, our website is not a part of this proxy statement.

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### **Director Independence**

We are not currently listed on any national securities exchange or in an inter-dealer quotation system that has established a standard for independence. However, in evaluating the independence of our members and the composition of the committees of our Board of Directors, our Board utilizes the definition of independence as that term is defined by applicable listing standards of the NYSE MKT. As of the date hereof, our Board consists of six members, three of whom are considered independent as that term is defined by applicable listing standards of the NYSE MKT. Our independent directors include: Messrs. Otis and Lee and Dr. Theno.

In addition to Messrs. Pfanzelter Otis and Dr. Theno, the following individuals served as directors during our fiscal year ended July 31, 2014; Gary D. Cohee, Henry R. Lambert, Michael L. Krall, Donna Singer, Dennis Brovarone and Craig Culver. Mr. Culver qualified as an independent director during his respective service on the Board as that term is defined by the applicable listing standards of the NYSE MKT. The other directors were not independent based on their services as executive officers or service providers to the Company.

### **Board and Committee Attendance**

During the year ended July 31, 2014, the Board of Directors met 12 times and it took action by unanimous written consent 4 times. During the last fiscal year, we believe based on available records that each of our directors attended at least 75% of the total number of meetings of the Board and all Board Committees on which such director served during that period.

### **Director Attendance at Annual Meeting**

We believe the annual meeting of stockholders provides a good opportunity for our directors to hear any feedback the stockholders may share with the Company at the meeting. As a result, we encourage our directors to attend our annual meeting. We reimburse our directors for the reasonable expenses incurred by them in attending the annual meeting.

### **Executive Sessions**

Executive sessions of our independent directors are held at each regularly scheduled meeting of our Board and at other times as necessary and are chaired by the Chairman of the Board. The Board's policy is to hold executive sessions without the presence of management, including our President and Chief Executive Officer, who is the only non-independent director on the Board. Our Board Committees also generally meet in executive session at the end of each committee meeting.

### **Board Committees**

*Compensation Committee.* The Compensation Committee of the Board of Directors currently consists of Dr. Theno (Chair). The functions of the Compensation Committee include the approval of the compensation offered to our executive officers and recommending to the full Board of Directors the compensation to be offered to our directors, including our Chairman. The Board has determined that Dr. Theno is an independent director under the listing standards of the NYSE MKT. In addition, the members of the Compensation Committee qualify as non-employee directors for purposes of Rule 16b-3 under the Exchange Act and as outside directors for purposes of Section 162(m) of the Internal Revenue Code of 1986, as amended. The Compensation Committee is governed by a written charter approved by the Board of Directors, a copy of which is available on our website at [www.purebio.com](http://www.purebio.com).



*Audit Committee.* The Audit Committee of the Board of Directors, currently consists of Messrs. Cohee (Chair), Lee and Otis. The functions of the Audit Committee include the retention of our independent registered public accounting firm, reviewing and approving the planned scope, proposed fee arrangements and results of the Company's annual audit, reviewing the adequacy of the Company's accounting and financial controls and reviewing the independence of the Company's independent registered public accounting firm. The Board has determined that each of Messrs. Otis and Lee is an independent director under the listing standards of the NYSE MKT. Mr. Cohee is not independent because the Company has retained Mr. Cohee to provide financial advisory services to the Company. See *Certain Relationships and Related Transactions* for additional information regarding the Company's retention of Mr. Cohee. The Board determined that it was in the Company's and its stockholders best interests for Mr. Cohee to continue to serve on the audit committee, based on his accounting and financial expertise, until the Board adds additional independent directors. The Board of Directors has also determined that Messrs. Cohee, Lee and Otis are each an audit committee financial expert within the applicable definition of the SEC. The Audit Committee is governed by a written charter approved by the Board of Directors, a copy of which is available on our website at [www.purebio.com](http://www.purebio.com).

*Nominating Committee.* The Board has not established a Nominating Committee, and as a result performs the functions typically assigned to a Nominating Committee, including the identification, recruitment and nomination of candidates for the

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Board and its committees, determining the structure, composition and functioning of the Board and its committees including the reporting channels through which the Board receives information and the quality and timeliness of the information, developing and recommending to the Board corporate governance guidelines applicable to the Company and annually reviewing and recommending changes, as necessary or appropriate, overseeing the annual evaluation of the Board's effectiveness and performance.

### **Board and Committee Effectiveness**

The Board and each of its Committees performs an annual self-assessment to evaluate their effectiveness in fulfilling their obligations. The Board and Committee evaluations cover a wide range of topics, including, among others, the fulfillment of the Board and Committee responsibilities identified in the Corporate Governance Guidelines and charters for each Committee.

### **Board Leadership Structure**

Our Bylaws provide our Board with flexibility to combine or separate the positions of Chairman of the Board and Chief Executive Officer in accordance with its determination that utilizing one or the other structure would be in the best interests of our company. At the current time, Mr. Pfanzelter serves as our Chairman of the Board, and Mr. Lambert serves as our Chief Executive Officer. Our Board believes our leadership structure enhances the accountability of our Chief Executive Officer to the Board and encourages balanced decision making. In addition, the Board believes that this structure provides an environment in which its independent directors are fully informed, have significant input into the content of Board meetings and are able to provide objective and thoughtful oversight of management. Our Board also separated the roles in recognition of the differences in responsibilities. While our Chief Executive Officer is responsible for the day-to-day leadership of the Company and its business operations, the Chairman of the Board provides guidance to the Board, sets the agenda for Board meetings and presides over the meetings of the full Board and the meetings of the Board's non-management directors. The Board Chairman also provides performance feedback on behalf of the Board to our Chief Executive Officer. The Board intends to carefully evaluate from time to time whether our Chief Executive Officer and Chairman positions should remain separate based on what the Board believes is best for the Company and its stockholders.

### **Board Oversight of Risk**

The Board is actively involved in the oversight of risks that could affect the Company. The Board as a whole has responsibility for risk oversight of the Company's risk management policies and procedures, with reviews of certain areas being conducted by the relevant Board committee. The Board satisfies this responsibility through reports by each Committee Chair regarding the Committee's considerations and actions, as well as through regular reports directly from management responsible for oversight of particular risks within the Company. Specifically, the Board committees address the following risk areas:

The Compensation Committee is responsible for overseeing the management of risks related to the Company's executive compensation plans and arrangements.

The Audit Committee discusses with management the Company's major financial risk exposures and the steps management has taken to monitor and control such exposures.

The Board as a whole considers risks related to regulatory and compliance matters as well as risks related to the Company's sales and marketing and research and development initiatives.

The Board encourages management to promote a corporate culture that incorporates risk management into the Company's day-to-day business operations.

### **Stockholder Recommendations for Director Nominees**

In nominating candidates for election as a director, the Board will consider a reasonable number of candidates recommended by a single stockholder who has held over 20% of PURE Bioscience Common Stock for over one year and who satisfies the notice, information and consent provisions set forth in our Bylaws and Corporate Governance Guidelines. Stockholders who wish to recommend a candidate may do so by writing to the Board of Directors in care of the Corporate Secretary, PURE Bioscience, Inc., 1725 Gillespie Way, El Cajon, California 92020. The Board of Directors will use the same evaluation process for director nominees recommended by stockholders as it uses for other director nominees. A printed copy of our Bylaws may be obtained by any stockholder upon request to our Corporate Secretary.

### **Identification and Evaluation of Director Nominees**

In evaluating nominees for membership on our Board, our Board applies the Board membership criteria set forth in our Corporate Governance Guidelines. Under these criteria, the Board takes into account many factors, including an individual's

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business experience and skills (including skills in core areas such as operations, management, technology, accounting and finance, strategic planning and international markets), as well as independence, judgment, knowledge of our business and industry, professional reputation, leadership, integrity and ability to represent the best interests of the Company's stockholders. In addition, the Board also considers the ability to commit sufficient time and attention to the activities of the Board, as well as the absence of any potential conflicts with the Company's interests. The Board does not assign specific weights to particular criteria and no particular criterion is necessarily applicable to all prospective nominees. The Board does not have a formal policy with respect to diversity of nominees. Rather, our Board considers Board membership criteria as a whole and seeks to achieve diversity of occupational and personal backgrounds on the Board.

Our Board regularly assesses the appropriate size of our Board, and whether any vacancies on our Board are expected due to retirement or otherwise. In the event that vacancies are anticipated, or otherwise arise, the Board will consider various potential candidates who may come to the attention of the Board through current Board members, professional search firms, stockholders or other persons. Each candidate brought to the attention of the Board, regardless of who recommended such candidate, is considered on the basis of the criteria set forth in our corporate governance guidelines. As stated above, our Board will consider candidates proposed for nomination by our significant stockholders. Stockholders may propose candidates by submitting the names and supporting information to: Corporate Secretary, PURE Bioscience, Inc., 1725 Gillespie Way, El Cajon, California 92020. Supporting information should include (a) the name and address of the candidate and the proposing stockholder, (b) a comprehensive biography of the candidate and an explanation of why the candidate is qualified to serve as a director taking into account the criteria identified in our corporate governance guidelines, (c) proof of ownership, the class and number of shares, and the length of time that the shares of our voting securities have been beneficially owned by each of the candidate and the proposing stockholder, and (d) a letter signed by the candidate stating his or her willingness to serve, if elected.

**Item 11. Executive Compensation**

*All information in this Item 11 regarding share amounts of our common stock and prices per share of our common stock has been adjusted to reflect the application of the one-for-eight reverse stock split of our common stock that we effected on August 14, 2012, as further described elsewhere in this Annual Report, on a retroactive basis.*

**Summary Compensation Table**

The following table sets forth a summary of cash and non-cash compensation awarded, earned or paid for services rendered to us during the years ended July 31, 2014 and July 31, 2013 by our named executive officers, consisting of (i) each individual serving as principal executive officer during the year ended July 31, 2014, and (ii) our Chief Financial Officer/Chief Operating Officer, our other executive officer.

Name and Principal Position	Fiscal Year	Salary (\$)(1)	Bonus(2)	Option Awards(3)	Stock Awards(4)	All Other Compensation	Total Compensation (\$)
						(\$)(5)(6)	
Henry R. Lambert Chief Executive Officer	2014	\$ 301,539	\$ 105,000		\$ 700,000		\$ 1,106,539
	2013						
Peter C. Wulff (7) Chief Financial Officer	2014	\$ 300,000	\$ 97,500		\$ 1,400,000	\$ 13,655	\$ 1,811,155
Chief Operating Officer	2013	\$ 143,845			\$ 37,815	\$ 12,195 (8)	\$ 193,855

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Dave J. Pfanzelter (9) Interim Chief Executive Officer and Chairman	2014	\$ 92,885		\$ 3,920,000	\$ 24,750	\$ 4,037,635
	2013	\$ 7,500	\$ 24,500			\$ 32,000
Michael L. Krall (10) Former President, Chief Executive Officer	2014	\$ 331,280		\$ 595,000	\$ 13,467	\$ 939,747
	2013	\$ 317,361	\$ 28,644		\$ 10,183	\$ 356,188

- (1) Amounts reflect salary and severance actually paid during the respective fiscal years. During the year ended July 31, 2013, Mr. Krall deferred a portion of his salary totaling \$37,639.
- (2) Annual bonuses for the year ended July 31, 2014, were awarded by the Compensation Committee after the completion of the fiscal year taking into account the Company's performance against corporate goals. The bonuses awarded to Mr. Lambert and Mr. Wulff were based on the terms of their respective employment agreements, whereas they may receive up to 50% of their base salary. During the year ended July 31, 2014, the Compensation Committee awarded Mr. Lambert and Mr. Wulff bonuses based 60% of their targeted bonus potential.

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- (3) Amounts for the year ended July 31, 2014 and July 31, 2013 reflect the grant date fair value for financial statement reporting purposes with respect to stock options granted during the respective fiscal years, calculated in accordance with authoritative guidance.
- (4) Amounts for the year ended July 31, 2014 and July 31, 2013 reflect the grant date fair value for financial statement reporting purposes with respect to stock awards granted during the respective fiscal years, calculated in accordance with authoritative guidance.
- (5) Amount includes the cost of benefits paid by the Company on behalf of each named executive officer for health, dental, vision and life insurance.
- (6) Amount includes a tax liability incurred by the Company and payable to Mr. Wulff and Mr. Pfanzelter for RSUs that vested during the year ended July 31, 2014. Per the terms of their restricted stock unit agreements, Mr. Wulff and Mr. Pfanzelter are entitled to \$7,817 and \$24,750, respectively.
- (7) Mr. Wulff was appointed as our Chief Financial Officer effective as of November 5, 2012. Mr. Wulff separated from the Company on May 13, 2013. Mr. Wulff was reappointed as our Chief Financial Officer on August 13, 2013.
- (8) Amount includes \$9,918 representing accrued vacation paid to Mr. Wulff upon his separation in May 2013.
- (9) On August 13, 2013, Mr. Pfanzelter, our Chairman and a member of the Board, was appointed by the Board to serve as Interim Chief Executive Officer. On September 10, 2013, in connection with the hiring of Mr. Lambert to serve as our Chief Executive Officer, Mr. Pfanzelter resigned his position as our Interim Chief Executive Officer. Mr. Pfanzelter continues to serve as the Chairman of the Board and his total compensation he received was received in connection with serving as Chairman of the Board and is set forth above. The Company considers Mr. Pfanzelter an executive officer due to his service as Chairman. During the year ended July 31, 2013, Mr. Pfanzelter earned \$7,500 as a member of our Board.
- (10) Effective August 13, 2014, we entered into a Purchase, Severance, and Release Agreement, with our former Chief Executive Officer, Michael L. Krall (the Krall Release Agreement). During the year ended July 31, 2014, per the terms of the Krall Release Agreement, Mr. Krall received \$330,000 in severance, a onetime payment of \$150,000, \$12,755 for continued benefit coverage, and received 850,000 shares of common stock valued at \$595,000.

**Outstanding Equity Awards at Year-End**

The following table provides a summary of equity awards outstanding at July 31, 2014, for each of our named executive officers.

Name	Option Awards				Stock Awards	
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Option Exercise Price (\$)	Option Expiration Date	Number of shares or Units of stock that have not vested (#)	Market Value of shares or Units of stock that have not vested (\$)(1)
Henry R. Lambert					500,000	\$ 500,000(2)
Peter C. Wulff					750,000	\$ 750,000(3)
Dave J. Pfanzelter					2,100,000	\$ 2,100,000(4)
Michael L. Krall					850,000	\$ 850,000(5)

- (11) The market value of RSU s and stock awards is determined by multiplying the number of shares underlying the units by the closing price for our common stock of \$1.00 on July 31, 2014.
- (12) The RSUs vest 60% on September 10, 2014 and the vesting of the remaining 40% depends on the achievement of certain quarterly sales goals over a two year period.
- (13) 25% of Mr. Wulff s RSU s vested on March 15, 2014, 25% will vest on March 15, 2015 and 50% will vest on March 15, 2016.
- (14) 25% of Mr. Pfanzelter s RSU s vested on February 15, 2014, 25% will vest on February 15, 2015, and 50% will vest on February 15, 2016.
- (15) During the year ended July 31, 2014, per the terms of the Krall Release Agreement discussed above, Mr. Krall received 850,000 shares of common stock.

During the year ended July 31, 2014, 250,000 of Mr. Wulff s restricted stock units vested. The value realized on vesting was \$325,000. In addition, during the year ended July 31, 2014, 700,000 of Mr. Pfanzelter s restricted stock units vested. The value realized on vesting was \$1,029,000. No other option or stock awards vested for our named executive officers.

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**Employment Agreements; Potential Payments Upon Termination or a Change in Control for Current Executive Officers**

*Agreements with our Chief Executive Officer and our Chief Financial Officer and Chief Operating Officer*

As described elsewhere in this annual report, on (i) August 13, 2013, we appointed Peter C. Wulff as our Chief Financial Officer, Chief Operating Officer, and Corporate Secretary and (ii) September 10, 2013, we appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. The following describes each of Messrs. Lambert's and Wulff's respective employment agreements.

The terms of each employment agreement with Messrs. Lambert and Wulff provides that such agreement continues until termination by either the Company or the applicable executive officer. During the term of each employment agreement, the executive officers are entitled to an annual base salary, which may be increased, but not decreased, by the Board or the Compensation Committee in their discretion. The annual base salaries of Mr. Lambert is \$350,000 and of Mr. Wulff is \$325,000.

Each agreement provides that, during the term of such agreement, the applicable executive officer is eligible for equity compensation grants to be awarded at the discretion of the Compensation Committee and the Board, and also provided for annual bonus targets equal to, as applicable, 50% of the executive's then current annual base salary, in each case to be awarded at the sole discretion of the Compensation Committee and the Board. Additionally, pursuant to the terms of Mr. Lambert's employment agreement, we granted Mr. Lambert a restricted stock unit for 500,000 shares of our common stock and pursuant to Mr. Wulff's employment agreement we granted Mr. Wulff a restricted stock unit for 1,000,000 shares of our common stock.

In each case, the employment agreements with Messrs. Lambert and Wulff provides for certain compensation to be paid such executive officer if his employment is terminated by the Company without Cause or terminated by the executive for Good Reason. In summary, Cause is the commission by the executive of an act of fraud or another felony, or gross misconduct resulting in a material adverse effect on the Company; refusal by the executive to perform his or her duties under the agreement or to otherwise breach the agreement, or a violation of confidentiality, non-competition and/or non-solicitation provisions to which the Company is bound. Good Reason is a material reduction of the executive's base salary or target bonus percentage; a material reduction by the Company of the executive's authority, duties or responsibilities; a relocation of the Company's offices that requires an increase in the executive's one-way driving distance of more than fifty miles; or a material breach of the agreement by the Company.

Upon such event, the executive, upon signing a release in favor of the Company, would be entitled to severance pay in the form of continued payments. In the case of Mr. Lambert, he would be entitled to receive his base salary then in effect and group health and dental benefits in accordance with COBRA for a period of 6 months from the date of his termination and in the case of Mr. Wulff, he would be entitled to receive his base salary then in effect and group health and dental benefits in accordance with COBRA for a period of 12 months from the date of his termination. Additionally, each agreement provides that all outstanding vested stock options held by the applicable executive at the date of such termination would continue to be exercisable for a period of up to 90 days following such termination, but in no event beyond the maximum permitted expiration date.

The employment agreements with each of Messrs. Lambert and Wulff also provides for compensation if the executive's employment is terminated by the Company without Cause within twelve months following a Change in Control, or the executive resigns for Good Reason within such period. A Change in Control is the closing of the sale, transfer or other disposition of all or substantially all of the Company's assets or the exclusive license of substantially all of the intellectual property of the Company; the consummation of a merger or consolidation of the Company with



or into another entity; any person (subject to certain exemptions) becomes the beneficial owner of securities of the Company representing 35% or more of the total combined voting power of the Company; or if individuals who, as of 60 days after the effective date of the agreement are members of the Board, or are nominees of such Board members, cease to constitute at least a majority of the members of the Board.

Upon such event, the executive would be entitled to additional severance pay in excess of the amounts described above, in each case in an amount equal to a single lump sum payment equal to 100% of the applicable executive's then current annual base salary for Mr. Lambert and 200% of the applicable executive's then current annual base salary for Mr. Wulff. In addition, in such event, the vesting of all outstanding equity based awards then held by the applicable executive would automatically accelerate and all equity based awards would continue to be exercisable for 12 months, but in no event beyond the maximum permitted expiration date.

The employment agreements with each of Messrs. Lambert and Wulff also provides that the Company could, in certain

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circumstances and in order to avoid incurring fines or penalties under applicable law (including recently enacted federal healthcare legislation), elect to pay cash payments equivalent to value of the monthly premiums the Company would otherwise pay to provide for the continuation of health and dental insurance for such executives and their eligible dependents following each such executive's termination without Cause or resignation for Good Reason.

**Henry Lambert RSU Awards:** On October 23, 2013, we granted Mr. Lambert an award consisting of five hundred thousand (500,000) RSUs. The award was not granted pursuant to any compensatory, bonus, or similar plan maintained or otherwise sponsored by the Company. Sixty percent (60%) of the RSUs vested on September 10, 2014 and the vesting of the remaining forty percent (40%) depend on the achievement of certain quarterly sales goals over a two year period. The shares of our common stock will be settled and delivered to Mr. Lambert six months after the vesting date of September 10, 2014 and immediately after the vesting upon achievement of certain quarterly sales goals, referenced above. Additionally, 100% of the restricted stock units subject to the time-based vesting would vest upon a termination without Cause or resignation for Good Reason, upon a Change in Control, or upon grantee's death or complete disability. 100% of the restricted stock units subject to the vesting based on achievement of certain sales goals would vest upon a termination without Cause or resignation for Good Reason, upon a Change in Control, or upon grantee's death or complete disability, so long as such condition occurred prior to October 31, 2015. At vesting, if grantee is an employee, the Company is obligated to withhold FICA amount due with respect to the vested units and the Company is also obligated to pay grantee an amount equal to the FICA amount withheld plus a tax gross-up payment for taxes payable by the grantee with respect to the FICA amount. At settlement, the Company shall allow grantee to satisfy all or any portion of the Company's tax withholding obligations by having the Company deduct from the shares of stock otherwise deliverable to the grantee in settlement of the restricted stock units a number of whole shares having a fair market value not in excess of the amount of such tax withholding obligations determined by the applicable minimum statutory withholding rates.

**Peter Wulff RSU Awards:** On October 23, 2013, we granted Mr. Wulff an award consisting of one million (1,000,000) RSUs. The award was not granted pursuant to any compensatory, bonus, or similar plan maintained or otherwise sponsored by the Company. Twenty five percent (25%) of the RSUs vested on March 15, 2014, twenty five percent (25%) of the RSUs vest on March 15, 2015 and fifty percent (50%) of the RSUs vest on March 15, 2016. The shares of our common stock will be settled and delivered to Mr. Wulff six months after each applicable vesting date referenced above. Additionally, 100% of the restricted stock units would vest upon a termination without Cause or resignation for Good Reason, upon a Change in Control, or upon grantee's death or complete disability. At vesting, if grantee is an employee, the Company is obligated to withhold FICA amount due with respect to the vested units and the Company is also obligated to pay grantee an amount equal to the FICA amount withheld plus a tax gross-up payment for taxes payable by the grantee with respect to the FICA amount. At settlement, the Company shall allow grantee to satisfy all or any portion of the Company's tax withholding obligations by having the Company deduct from the shares of stock otherwise deliverable to the grantee in settlement of the restricted stock units a number of whole shares having a fair market value not in excess of the amount of such tax withholding obligations determined by the applicable minimum statutory withholding rates.

The foregoing descriptions of the employment agreements and RSUs do not purport to be complete and are qualified in their entirety by the terms and conditions of such employment agreements and RSUs filed as Exhibits 10.33, 10.33, 10.37 and 10.38 to the Annual Report on Form 10-K for the year ended July 31, 2013 filed with the SEC on October 24, 2013.

*Chairman Agreements*

On August 13, 2013, we appointed Dave J. Pfanzelter to serve as Chairman of the Board. On October 23, 2013, we entered into a Chairman Agreement with Mr. Pfanzelter (the "Chairman Agreement"). The Chairman Agreement

provides that Mr. Pfanzelter is to serve as Chairman of the Board, effective as of August 13, 2013, until his earlier resignation or removal. The Chairman Agreement provides that for the period beginning on August 13, 2013 and ending November 13, 2013, we were to pay Mr. Pfanzelter an amount of approximately \$41,700 per month for his services as Chairman of the Board, and thereafter we are to pay Mr. Pfanzelter the amount of \$12,500 per month for his services as Chairman of the Board, payable on a quarterly basis (collectively Chairman Compensation ). Mr. Pfanzelter is also eligible to receive annual and periodic bonuses in the discretion of the Board. Additionally, pursuant to the terms of the Chairman Agreement, we granted Mr. Pfanzelter a restricted stock unit for 2,800,000 shares of our common stock. We consider Mr. Pfanzelter an executive officer.

The Chairman Agreement provides for certain compensation to be paid to Mr. Pfanzelter if he is removed by the Board without Cause or Mr. Pfanzelter resigns for Good Reason. In summary, Cause is the commission by Mr. Pfanzelter of an act of fraud or another felony, or gross misconduct resulting in a material adverse effect on the Company; refusal by Mr. Pfanzelter to perform his or her duties under the Chairman Agreement or to otherwise breach the Chairman Agreement, or a material breach by Mr. Pfanzelter of Company policy or the Chairman Agreement or other agreements between the Company and Mr. Pfanzelter. Good Reason is a material reduction of Mr. Pfanzelter's compensation; a material reduction by the Board of Mr. Pfanzelter's authority, duties or responsibilities; or a material breach of the Chairman Agreement by the Company.

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Upon such event, Mr. Pfanzelter, upon signing a release in favor of the Company, would be entitled to severance pay in the form of continued payments. Mr. Pfanzelter would be entitled to receive his Chairman Compensation then in effect for a period of 12 months following such date of removal or resignation. The Chairman Agreement additionally provides that all outstanding vested stock options held by Mr. Pfanzelter at the date of such termination would continue to be exercisable for a period of up to 90 days following such termination, but in no event beyond the maximum permitted expiration date. Additionally, 100% of Mr. Pfanzelter's restricted stock units described below would vest.

The Chairman Agreement with Mr. Pfanzelter also provides for compensation if Mr. Pfanzelter's position is terminated by the Company without Cause within twelve months following a Change in Control, or Mr. Pfanzelter resigns for Good Reason within such period. A Change in Control is the closing of the sale, transfer or other disposition of all or substantially all of the Company's assets or the exclusive license of substantially all of the intellectual property of the Company; the consummation of a merger or consolidation of the Company with or into another entity; any person (subject to certain exemptions) becomes the beneficial owner of securities of the Company representing 35% or more of the total combined voting power of the Company; or if individuals who, as of 60 days after the effective date of the agreement are members of the Board, or are nominees of such Board members, cease to constitute at least a majority of the members of the Board. Upon such event, Mr. Pfanzelter would be entitled to additional separation pay in excess of the amounts described above, in each case in an amount equal to a single lump sum payment equal to 200% of Mr. Pfanzelter's then current Chairman Compensation. Additionally, 100% of Mr. Pfanzelter's restricted stock units described above would vest.

Chairman RSU Award: On October 23, 2013, we granted Mr. Pfanzelter an award consisting of two million eight hundred thousand (2,800,000) Restricted Stock Units (RSUs). The award was not granted pursuant to any compensatory, bonus, or similar plan maintained or otherwise sponsored by the Company. Twenty-five percent (25%) of the RSUs vested on February 15, 2014, Twenty-five percent (25%) of the RSUs vest on February 15, 2015 and fifty percent (50%) of the RSUs vest on February 15, 2016. The shares of our common stock will be settled and delivered to Mr. Pfanzelter six months after each applicable vesting date referenced above. Additionally, 100% of the restricted stock units would vest upon a termination without Cause or resignation for Good Reason, upon a Change in Control, or upon grantee's death or complete disability. At vesting, if grantee is a director or consultant, the Company is obligated to pay grantee an amount equal to the sum of the taxes imposed on the vested units that are treated as self-employment income plus a tax gross-up payment for all federal, state and local taxes payable by grantee. At settlement, the Company shall allow grantee to satisfy all or any portion of the Company's tax withholding obligations by having the Company cancel the shares of stock otherwise deliverable to the grantee in settlement of the restricted stock units in an amount equal to a number of whole shares having a fair market value not in excess of the amount of such tax withholding obligations determined by the applicable minimum statutory withholding rates. Upon cancellation of the shares, the Company shall pay the fair market value of such cancelled shares to the grantee in cash so that the grantee can satisfy his tax obligations.

The foregoing descriptions of the Chairman Agreement and RSUs do not purport to be complete and are qualified in their entirety by the terms and conditions of such Chairman Agreement and RSUs filed as Exhibits 10.35 and 10.39 to the Annual Report on Form 10-K for the year ended July 31, 2013 filed with the SEC on October 24, 2013.

**Separation Agreements with Former Executive Officers and Directors**

On August 13, 2013 Michael L. Krall resigned all positions respectively held by them as officers of the Company by mutual agreement with the Company.

In connection with Mr. Krall's separation from the Company, the Company entered into a Purchase, Severance, and Release Agreement effective August 13, 2013 with Mr. Krall (the "Krall Release Agreement"). The Krall Release Agreement provides for a mutual release of all claims between Mr. Krall and the Company. Mr. Krall is also prohibited from engaging in certain competitive activities for the next four years. Pursuant to the Krall Release Agreement, Mr. Krall (i) was paid \$25,000 on August 13, 2013; and, (ii) is entitled to receive \$30,000 per month for 18-months following August 13, 2013, during which time enumerated intellectual property rights, the Company also (i) paid Mr. Krall the sum of \$125,000 on August 13, 2013; and, (ii) issued to Mr. Krall 850,000 shares of common stock on August 21, 2013 (the "Krall Shares"). The Krall Shares are subject to certain registration rights intended to register the Krall Shares. The Krall Shares are also subject to a Voting Support Agreement and Irrevocable Proxy (the "Krall Proxy"). The Krall Proxy gives our CEO the right to vote the Krall Shares for so long as Mr. Krall owns the Krall Shares.

In connection with Ms. Singer's separation from the Company, we entered into a Purchase, Severance, and Release Agreement effective August 13, 2013 with Ms. Singer (the "Singer Release Agreement"). The Singer Release Agreement provides for a mutual release of all claims between Ms. Singer and the Company. Ms. Singer is also prohibited from engaging in certain competitive activities until August 2017. Pursuant to the Singer Release Agreement, Ms. Singer (i) was paid \$45,000 on August 13, 2013; (ii) is due the amount of her continued health insurance coverage until August 2014; and, (iii) was

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entitled to \$17,000 per month for 12-months following August 13, 2013, during which time Ms. Singer was to provide consulting services to the Company. In consideration of Ms. Singer's transfer to the Company of certain enumerated intellectual property rights, the Company also issued to Ms. Singer 300,000 shares of common stock on August 21, 2013 (the Singer Shares). The Singer Shares are subject to certain registration rights intended to register the Singer Shares. The Singer Shares are also subject to a Voting Support Agreement and Irrevocable Proxy (the Singer Proxy). The Singer Proxy gives our CEO the right to vote the Singer Shares for so long as Ms. Singer owns the Singer Shares.

## **Code Section 162(m) Provisions**

Section 162(m) of the U.S. Internal Revenue Code, or the Code, generally disallows a tax deduction to public companies for compensation in excess of \$1 million paid to the Chief Executive Officer or any of the four most highly compensated officers. Performance-based compensation arrangements may qualify for an exemption from the deduction limit if they satisfy various requirements under Section 162(m). Although we consider the impact of this rule when developing and implementing our executive compensation programs, we believe it is important to preserve flexibility in designing compensation programs. Accordingly, we have not adopted a policy that all compensation must qualify as deductible under Section 162(m) of the Code. While our stock options are intended to qualify as performance-based compensation (as defined by the Code), amounts paid under our other compensation programs may not qualify as such.

## **Compensation of Directors**

For non-employee directors appointed subsequent to July 31, 2013, each director of the Company will receive cash fees from the Company for their services as members of the Board and any committee of the Board as follows:

Each non-employee director will receive an annual fee of \$60,000 payable for such director's service on the Board and each member of the Audit Committee and Compensation Committee will receive an additional annual fee of \$4,000 and \$2,500, respectively, payable for such director's service on the committee.

The Chair of the Audit Committee will receive an additional annual fee of \$10,000 for such Chair's service and the Chair of the Compensation Committee will receive an additional annual fee of \$5,000 for such Chair's service.

Annual fees will be paid to each non-employee director in four equal installments on a quarterly basis. Any non-employee directors serving a portion of the year will be entitled to receive such fees on a pro rata basis based on their length of service during the year.

New non-employee directors will receive an initial grant of 200,000 restricted stock units. Currently, all non-employee director grants of restricted stock units vest fifty percent (50%) on the earlier of (i) the date of the annual meeting in 2015 or (ii) January 15, 2015 and fifty percent (50%) on the earlier of (i) the date of the annual meeting in 2016 or (ii) January 15, 2016.

The following table sets forth compensation earned in the year ended July 31, 2014 by each of our directors who are not named executive officers.

Name(1)	Fees Earned or			All Other Compensation (\$)	Total Compensation (\$)
	Paid in Cash (\$)	Stock Awards (\$)(2)(3)	Option Awards (\$)(4)		
Gary D. Cohee	\$ 67,692	\$ 280,000		\$ 536,000 (5)	\$ 883,692
David Theno, Jr., PhD	\$ 54,107	\$ 280,000			\$ 334,107
William Otis	\$ 52,044	\$ 280,000			\$ 332,044
Craig C. Culver(6)	\$ 33,750	\$ 280,000			\$ 313,750
Dennis Brovarone(7)				\$ 13,944	\$ 13,944

- (1) Director Henry R. Lambert, our Chief Executive Officer, is not included on this table as he received no compensation for his service as a director. The executive compensation received by Mr. Lambert is shown in the Summary Compensation table above. The compensation for Chairman Dave J. Pfanzelter is included in the Summary Compensation table above.
- (2) Amounts for the year ended July 31, 2014 reflect the grant date fair value for financial statement reporting purposes with respect to restricted stock units granted during the fiscal year, calculated in accordance with authoritative guidance.
- (3) During the year ended July 31, 2014, we granted Messrs. Cohee, Culver, Otis and Dr. Theno, awards consisting 200,000 RSUs, respectively. The RSUs vest (i) 50% on the earlier of the date of the annual meeting in 2015 or January 15, 2015 and (ii) 50% on the earlier of the date of the annual meeting in 2016 or January 15, 2016. On April 9, 2014, Mr. Culver resigned from our board of directors. As a result, Mr. Culver's 200,000 RSU award was forfeited.
- (4) There were no option awards granted during the year ended July 31, 2014.

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- (5) During the year ended July 31, 2014, we paid approximately \$160,000, and issued 415,643 shares of common stock, to Gary D. Cohee and/or his affiliates for investor relations and financial advisor services, valued at \$376,000, pursuant to the terms of the director service agreement with Mr. Cohee.
- (6) Craig Culver resigned from the Board on April 9, 2014.
- (7) The amounts reflected above relate to Mr. Brovarone's release agreement, which the Company entered into August 13, 2013 in connection with his resignation as director and separation from the Company.

In the past, our Board has approved each year, generally in the second calendar quarter of the year, an annual option or stock grant for our non-employee directors. Any such grant is at the discretion of the Board, which considers the recommendation of our Compensation Committee. Upon the Board's approval of any such grant, each non-employee director generally may elect whether to receive the grant as an option or stock award.



**Table of Contents****Item 12. Security Ownership of Certain Beneficial Owners and Management**

The following table provides information regarding the beneficial ownership of our common stock as of October 24, 2014, or the Evaluation Date, by: (i) each of our current directors, (ii) each of our named executive officers as set forth in Item 11 of this Annual Report, and (iii) all such directors and executive officers as a group. We know of no other person or group of affiliated persons who beneficially own more than five percent of our common stock. The table is based upon information supplied by our officers, directors and principal stockholders and a review of Schedules 13D and 13G, if any, filed with the SEC. Unless otherwise indicated in the footnotes to the table and subject to community property laws where applicable, we believe that each of the stockholders named in the table has sole voting and investment power with respect to the shares indicated as beneficially owned. All information in the following table regarding share amounts of our common stock has been adjusted to reflect the application of the one-for-eight reverse stock split of our common stock that we effected on August 14, 2012, as further described elsewhere in this Annual Report, on a retroactive basis.

Applicable percentages are based on 39,780,965 shares outstanding as of the Evaluation Date, adjusted as required by rules promulgated by the SEC. These rules generally attribute beneficial ownership of securities to persons who possess sole or shared voting power or investment power with respect to those securities. In addition, the rules include shares of our common stock issuable pursuant to the exercise of stock options or warrants that are either immediately exercisable or exercisable within 60 days of the Evaluation Date. These shares are deemed to be outstanding and beneficially owned by the person holding those options for the purpose of computing the percentage ownership of that person, but they are not treated as outstanding for the purpose of computing the percentage ownership of any other person.

Name (1)	Number of Shares Beneficially Owned	Percent of Common Stock
David J. Pfanzelter	796,000 (2)	2.00%
Henry R. Lambert	342,857 (3)	*
Peter C. Wulff	500,000 (4)	1.26%
Gary D. Cohee	415,643 (5)	1.04%
David Theno, Jr., PhD	47,600 (6)	*
William Otis	31,732 (7)	*
Tom Y. Lee	3,333,813 (8)	8.25%
Michael L. Krall	850,000 (9)	2.14%
All of our named executive officers and directors as a group (8 persons)	6,317,645 (10)	15.61%

\* Indicates less than one percent of the outstanding shares of the Company's common stock.

(1) The address for each person listed in the table is c/o Pure Bioscience, Inc., 1725 Gillespie Way, El Cajon, California 92020.

(2) Consists of (a) 40,000 shares of common stock subject to options currently exercisable or exercisable within 60 days of the Evaluation Date, (b) 740,000 shares of common stock and (c) warrants to purchase 16,000 shares of common stock which are held directly by Mr. Pfanzelter.

(3) Consists of 342,857 shares of common stock held directly by Mr. Lambert.

- (4) Consists of 500,000 shares of common stock held directly by Mr. Wulff.
- (5) Consists of 415,643 shares of common stock held directly by Mr. Cohee.
- (6) Consists of 34,000 shares of common stock and warrants to purchase 13,600 shares of common stock which is currently exercisable, held directly by Dr. Theno.
- (7) Consists of 22,666 shares of common stock and warrants to purchase 9,066 shares of common stock which are currently exercisable, held directly by Mr. Otis.
- (8) Consists of 1,666,385 shares of common stock and warrants to purchase 619,999 shares of common stock which are currently exercisable, held directly by Mr. Lee and 1,047,429 shares of common stock which are held by Mr. Lee and his spouse. On October 24, 2014 Tom Y. Lee was appointed to the Board.
- (9) Consists of 850,000 shares of common stock held directly by Mr. Krall, issued pursuant to the Krall Release Agreement discussed above.
- (10) Consists of (a) 40,000 shares of common stock subject to options currently exercisable or exercisable within 60 days of the Evaluation Date, (b) warrants to purchase 658,665 shares of common stock which are currently exercisable and (c) 5,618,980 shares of common stock, held by all directors and executive officers as a group.

#### **Equity Compensation Plan Information**

The 2007 PURE Bioscience Equity Incentive Plan, or the Plan, is our only active equity incentive plan pursuant to which options to acquire common stock or restricted stock awards have been granted and are currently outstanding. Approved by our stockholders in April 2007, the Plan has a share reserve of 625,000 shares of common stock. The Plan provides for the grant of

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incentive and non-qualified stock options, as well as stock appreciation rights, common stock awards, restricted stock units, performance units and shares, and other stock-based awards. Eligible participants include employees, directors, officers and advisors, although incentive stock options generally may be granted only to employees.

All of our equity incentive plans are administered by the Compensation Committee. The exercise price for stock options is always at or above the fair market value of our common stock on the date the award is granted. Fair market value is defined by the Plan and is based on prevailing market prices of our common stock as reported by the OTCQB. The term of stock options granted and their vesting schedules are determined by the Compensation Committee, subject to any limitations defined in the Plan. The Compensation Committee also determines the vesting of other, non-option, stock awards.

The following table sets forth, as of July 31, 2014, information with respect to our equity compensation plans, and with respect to certain other options and warrants.

<b>Plan Category<sup>F</sup></b>	<b>Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)(1)</b>	<b>Weighted average exercise price of outstanding options, warrants and rights (b)</b>	<b>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)</b>
Equity compensation plans approved by stockholders	462,343	\$ 3.95	108,471
Equity compensation plans not approved by stockholders			
<b>Total</b>	<b>462,343</b>	<b>\$ 3.95</b>	<b>108,471</b>

(1) Includes options only.

**Item 13. Certain Relationships and Related Transactions, and Director Independence****Board Composition**

We are not currently listed on any national securities exchange or in an inter-dealer quotation system that has established a standard for independence. However, in evaluating the independence of our members and the composition of the committees of our Board of Directors, our Board utilizes the definition of independence as that term is defined by applicable listing standards of the NYSE MKT. As of the date of this annual report, our Board consists of three members, four of whom are considered independent as that term is defined by applicable listing standards of the NYSE MKT. Our independent directors include: Messrs. Otis, Lee and Dr. Theno.

Our directors are appointed annually, and hold office until their successors have been elected and qualified or until their earlier death, resignation, disqualification, or removal.

### **Certain Relationships and Related Transactions**

Except as described below and other than Board or employment relationships and compensation resulting from those employment relationships, no director, executive officer, 5% stockholder or immediate family member of any of the foregoing, was a party to any transaction or series of transactions since August 1, 2013 (the beginning of the year ended July 31, 2014), or is to be a party to any currently proposed transaction or series of proposed transactions, in which (i) we were or are to be a participant, (ii) the amount involved exceeds the lesser of \$120,000 or one percent of the average of our total assets at fiscal year-end for the fiscal years ended July 31, 2014 and 2013, which is \$16,605, and (iii) any director, executive officer, or immediate family member of any of the foregoing had or will have a direct or indirect material interest.

### **Transactions with Our Former Executive Officers**

Our former Director of Manufacturing and Research and Development, Richard Gumienny, is the son-in-law of Michael L. Krall, our former President, Chief Executive Officer, Interim Chief Financial Officer, and Chairman of the Board. Pursuant to

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the terms of Mr. Gumienny's employment arrangement with us, which has been in effect during the period commencing at the beginning of our fiscal year ended July 31, 2011 and continuing through July 2014, Mr. Gumienny (1) received an annual salary of \$101,100, (2) receives certain benefits that are also provided to our other similarly situated employees, which benefits have an approximate annual value of \$5,397 for Mr. Gumienny, and (3) is eligible to receive cash bonuses and equity grants at the discretion of management. In accordance with that arrangement, during the fiscal year ended July 31, 2014, Mr. Gumienny was awarded a cash bonus of \$20,000 and options to purchase up to 50,000 restricted stock units of in addition to his salary and benefits. Mr. Gumienny resigned from the Company in July 2014.

Our current Accounts Receivable and Accounts Payable Manager, Ashley Gumienny, is the daughter of Michael L. Krall, our former President, Chief Executive Officer, Interim Chief Financial Officer, and Chairman of the Board. Pursuant to the terms of Ms. Gumienny's employment arrangement with us, which has been in effect during the period commencing at the beginning of our fiscal year ended July 31, 2011 and continuing through the date of this annual report, Ms. Gumienny (1) receives an annual salary of \$50,300, (2) receives certain benefits that are also provided to our other similarly situated employees, which benefits have an approximate annual value of \$5,397 for Ms. Gumienny, and (3) is eligible to receive cash bonuses and equity grants at the discretion of management. Ms. Gumienny did not receive a cash bonus nor equity grants during the fiscal year ended July 31, 2014.

Our former director, Dennis Brovarone, provided consulting services for us as securities counsel in addition to his services as a director. Pursuant to the terms of Mr. Brovarone's consulting arrangement with us, which has been in effect during the period commencing at the beginning of our fiscal year ended July 31, 2011 and continuing through the date of this annual report, Mr. Brovarone received annual cash compensation of \$60,000 in exchange for his services as a consultant. Such amounts are in addition to the cash, equity or other compensation Mr. Brovarone received in exchange for his services as a director. Please see the table under the heading "Compensation of Directors" of this annual report for further information about Mr. Brovarone's director compensation.

**Separation Arrangements with Our Former Executive Officers and Directors**

On August 13, 2013, Michael L. Krall and Donna Singer resigned all positions respectively held by them as officers of the Company by mutual agreement with the Company. Additionally, Dennis Brovarone resigned as a director of the Company.

**Michael L. Krall:** In connection with Mr. Krall's separation from the Company, the Company entered into a Purchase, Severance, and Release Agreement effective August 13, 2013 with Mr. Krall (the "Krall Release Agreement"). The Krall Release Agreement provides for a mutual release of all claims between Mr. Krall and the Company. Mr. Krall is also prohibited from engaging in certain competitive activities for the next four years. Pursuant to the Krall Release Agreement, Mr. Krall (i) was paid \$25,000 on August 13, 2013; (ii) is entitled to receive \$30,000 per month for 18-months following August 13, 2013, during which time Mr. Krall shall provide consulting services to the Company, and (iii) is due the amount of his continued health insurance coverage until 18-months following August 13, 2013. In consideration of Mr. Krall's transfer to the Company of certain enumerated intellectual property rights, the Company also (i) paid Mr. Krall the sum of \$125,000 on August 13, 2013; and, (ii) issued to Mr. Krall 850,000 shares of common stock on August 21, 2013 (the "Krall Shares"). The Krall Shares are subject to certain registration rights intended to register the Krall Shares. The Krall Shares are also subject to a Voting Support Agreement and Irrevocable Proxy (the "Krall Proxy"). The Krall Proxy gives our CEO the right to vote the Krall Shares for so long as Mr. Krall owns the Krall Shares.

**Donna Singer:** In connection with Ms. Singer's separation from the Company, we entered into a Purchase, Severance, and Release Agreement effective August 13, 2013 with Ms. Singer (the "Singer Release Agreement"). The Singer

Release Agreement provides for a mutual release of all claims between Ms. Singer and the Company. Ms. Singer is also prohibited from engaging in certain competitive activities until August 2017. Pursuant to the Singer Release Agreement, Ms. Singer (i) was paid \$45,000 on August 13, 2013; (ii) is due the amount of her continued health insurance coverage until August 2014; and, (iii) is entitled to \$17,000 per month for 12-months following August 13, 2013, during which time Ms. Singer shall provide consulting services to the Company. In consideration of Ms. Singer's transfer to the Company of certain enumerated intellectual property rights, the Company also issued to Ms. Singer 300,000 shares of common stock on August 21, 2013 (the Singer Shares). The Singer Shares are subject to certain registration rights intended to register the Singer Shares. The Singer Shares are also subject to a Voting Support Agreement and Irrevocable Proxy (the Singer Proxy). The Singer Proxy gives our CEO the right to vote the Singer Shares for so long as Ms. Singer owns the Singer Shares.

Dennis Brovarone: In connection with Mr. Brovarone's separation from the Company, we entered into a Settlement and Release Agreement effective August 13, 2013 with Mr. Brovarone (the Brovarone Release Agreement). The Brovarone Release Agreement provides for a mutual release of all claims between Mr. Brovarone and the Company. Mr. Brovarone shall be paid \$91,332.77 (the Brovarone Amount) as follows: (i) starting November 11, 2013 the Brovarone Amount shall be subject to 2% interest per annum; (ii) starting December 11, 2013 and continuing on the same day of each month for 60-months the Company shall pay \$1,600.86; (iii) the Company shall have the right to prepay without penalty upon 30-days

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notice; and, (iv) Brovarone shall have the right to convert the then outstanding balance of the Brovarone Amount, at any time and with 10-days advance notice, into common stock at a conversion price equal to the average closing price for our common stock on the principal market on which our common stock is then listed or quoted for the ten trading days immediately preceding the date of the conversion notice.

For information with respect to the compensation paid to our executive officers and directors, see heading Executive Compensation of this annual report.

## **Arrangements Related to Board and Management Changes**

**Pillar Marketing Group, Inc.:** On August 13, 2013 we entered into a services agreement (the Pillar Services Agreement ) with Pillar Marketing Group, Inc. ( Pillar ), as amended on October 2, 2014. The Pillar Services Agreement provides, among other things, that Pillar shall serve as our exclusive provider of general advisory services regarding corporate finance, capital raising activities, merger and acquisition transactions, and other related endeavors. Pillar is to be paid the sum of \$25,000 per month plus, upon consummation of any transaction involving the acquisition, merger, or combination, or similar transaction of or with another company, we are to issue Pillar that number of our shares of our common stock which equals to three percent (3%) of our issued and outstanding shares determined on a fully diluted basis post-transaction. Additionally, pursuant to the Pillar Services Agreement and for corporate reorganization services previously provided by Pillar, we issued 550,000 shares of common stock, (300,000 shares for certain corporate reorganization services previously provided and 250,000 for general advisory services pursuant to the services agreement) with a value of \$385,000, pursuant to an exemption from registration provided by Section 4(a)(2) of the Securities Act. We also paid Pillar the amount of \$150,000 for corporate reorganization services previously provided. The reorganization services were for general corporate restructuring advice in connection with the corporate restructuring effected in August 2013. The Pillar Services Agreement provides for a term of 24 months, which renews automatically for additional 24 month terms unless either party provides prior written notice of termination. Immediately upon the renewal we are to issue to Pillar an additional two hundred fifty thousand (250,000) shares of our common stock.

**Wulff Services, Inc.:** On August 13, 2013 we issued 250,000 shares of common stock, pursuant to an exemption from registration provided by Section 4(a)(2) of the Securities Act, with a value of \$175,000, for corporate finance and restructuring activities to Wulff Services Inc. ( Wulff Services ). Wulff Services is primarily owned by our current Chief Financial Officer and Chief Operation Officer, Peter C. Wulff.

**Cohee Director Agreement:** On August 13, 2013, we appointed Mr. Cohee to serve as a member of the Board and on September 17, 2013, we entered into a letter agreement with Mr. Cohee. Mr. Cohee's letter agreement provides that his initial term will be for one year. In connection with his execution of the letter agreement, we are obligated to issue him 250,000 shares of our common stock pursuant to a restricted stock unit agreement in the form of a non-employee RSU award. Additionally, we will pay him an annual retainer fee of \$60,000, payable quarterly. Additionally, he acknowledges and agrees that in order to satisfy certain rules for public companies he may be required to serve on one or more of the Board's Audit Committee, Compensation Committee, and/or Nominating and Governance Committee, and that such committee assignments will be agreed between him and the Company, and that he will be compensated for such service. His letter agreement also provides that he will also be subject to certain confidentiality obligations. On April 24, 2014, the Company and Gary Cohee entered into an amendment to the Cohee Director Agreement to provide for a monthly consulting fee for certain investor relations activities.

Further, during the fiscal year ended July 31, 2014, we issued 415,643 shares of common stock, in exchange for previous services provided, valued at \$376,000, pursuant to an exemption from registration provided by Section 4(a)(2) of the Securities Act, and paid \$160,000 to Mr. Cohee and/or his affiliates for financial advisor

services. The shares were issued and payment made to Mr. Cohee and/or his affiliates for his services.

### **Transactions with our Director Tom Y. Lee**

Mr. Lee will receive certain benefits in accordance with the Company's non-employee director compensation program. Additionally, since August 1, 2013, Mr. Lee and the Company have entered into the following equity investment transactions:

On October 1, 2013, Mr. Lee and his spouse purchased an aggregate of 246,429 shares of Common Stock for \$172,500.

On October 1, 2013, Mr. Lee exercised an outstanding warrant for 250,000 shares of Common Stock for an aggregate exercise price of \$162,500.

On December 10, 2013, Mr. Lee and his spouse purchased an aggregate of 800,000 shares of Common Stock for \$800,000. In connection with his participation in the August 2014 Financing (as defined below), Mr. Lee and his spouse received warrants to purchase up to an aggregate of 266,666 shares of Common Stock at an exercise price of \$0.01 per share related to the shares they acquired in the December 10, 2013 financing. The Company issued the warrant to lower the cost average price Mr. Lee and his spouse paid for their shares in the December 10, 2013 financing to \$0.75 per share.

On March 3, 2014, Mr. Lee and his spouse purchased an aggregate of 100,000 shares of Common Stock for \$100,000. In connection with his participation in the August 2014 Financing, Mr. Lee and his spouse received warrants to purchase up to an aggregate of 33,333 shares of Common Stock at an exercise price of \$0.01 per share. The Company issued the warrants to lower the cost average price Mr. Lee and his spouse paid for their shares in the March 3, 2014 financing to \$0.75 per share.

On August 23, 2014, the Company completed the first closing of a private placement in which it issued Units at a purchase price of \$0.75 per Unit, with each Unit consisting of one share of common stock and a warrant to purchase 0.4 of a share of common stock with an exercise price of \$0.75 per share (the August 2014 Financing). On August 29, 2014, Mr. Lee and his spouse invested an aggregate of \$600,000 in the second closing of the August 2014 Financing, acquiring an aggregate of 800,000 shares of Common Stock and warrants to purchase up to 320,000 shares of Common Stock at an exercise price of \$0.75 per share.

### **Compensation of Our Current Directors and Executive Officers**

For information with respect to the compensation offered to our current directors and executive officers, please see the descriptions under the heading "Executive Compensation" of this annual report.

### **Related Party Transaction Policy and Procedures**

Pursuant to our Related Party Transaction and Procedures, our executive officers, directors, and principal stockholders,





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including their immediate family members and affiliates, are prohibited from entering into a related party transaction with us without the prior consent of our Audit Committee or our independent directors. Any request for us to enter into a transaction with an executive officer, director, principal stockholder, or any of such persons' immediate family members or affiliates, must first be presented to our Audit Committee for review, consideration and approval. In approving or rejecting the proposed agreement, our Audit Committee will consider the relevant facts and circumstances available and deemed relevant, including, but not limited, to the risks, costs and benefits to us, the terms of the transaction, the availability of other sources for comparable services or products, and, if applicable, the impact on a director's independence. Our Audit Committee shall approve only those agreements that, in light of known circumstances, are in, or are not inconsistent with, our best interests, as our Audit Committee determines in the good faith exercise of its discretion.

**Item 14. Principal Accounting Fees and Services****Independent Registered Public Accounting Firm's Fee Summary**

The following table provides information regarding the fees billed to us by Mayer Hoffman McCann P.C. for the years ended July 31, 2014 and 2013. Mayer Hoffman McCann P.C. leases substantially all of its personnel, who work under the control of Mayer Hoffman McCann P.C. shareholders, from wholly-owned subsidiaries of CBIZ, Inc., including CBIZ MHM, LLC, in an alternative practice structure. All fees described below were approved by the Board or the Audit Committee:

	<b>For the years ended July 31,</b>	
	<b>2014</b>	<b>2013</b>
Audit Fees (1)	\$ 124,000	\$ 152,500
Tax Fees (2)	\$ 9,300	9,000
<b>Total Fees</b>	<b>\$ 133,300</b>	<b>\$ 161,500</b>

- (1) Audit Fees include fees for services rendered for the audit and quarterly reviews of our financial statements, including our Annual Report on Form 10-K and our periodic reports, and fees incurred related to the filings of registration statements.
- (2) Tax Fees consist of amounts billed by an affiliate of our independent auditors for services in connection with the preparation of our federal and state tax returns.

**Pre-Approval Policies and Procedures**

Our Audit Committee's policy is to pre-approve all audit and permissible non-audit services provided by our independent auditors. These services may include audit services, audit-related services, tax services and other services. Pre-approval is generally provided for up to one year and any pre-approval is detailed as to the particular service or category of services. The independent auditor and management are required to periodically report to the Audit Committee regarding the extent of services provided by the independent auditor in accordance with this pre-approval. Any proposed services not included within the list of pre-approved services or any proposed services that will cause the Company to exceed the pre-approved aggregate amount requires specific pre-approval by the Audit Committee. All audit fees, audit-related fees, tax fees, and other fees listed in the table above were approved by the Audit Committee pursuant to its pre-approval policies and procedures.



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**PART IV**

**Item 15. Exhibits, Financial Statement Schedules**

- (a) (1) The list of financial statements filed in response to Part II, Item 8 is set forth at the end of this Annual Report.
- (2) Schedules are omitted because they are not applicable or the required information is shown in the financial statements or notes thereto.
- (3) The following exhibits are filed as part of this Annual Report pursuant to Item 601 of Regulation S-K:
- 2.1 Agreement and Plan of Merger, dated as of March 24, 2011, by and between Pure Bioscience and Pure Bioscience, Inc. (incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K, filed with the SEC on March 25, 2011)
  - 3.1 Certificate of Incorporation of Pure Bioscience, Inc. (incorporated by reference to Exhibit 3.1 to the Annual Report on Form 10-K, filed with the SEC on October 29, 2012)
  - 3.1.1 Certificate of Amendment to Certificate of Incorporation of Pure Bioscience, Inc. (incorporated by reference to Exhibit 3.1.1 to the Annual Report on Form 10-K, filed with the SEC on October 29, 2012)
  - 3.2 Bylaws of Pure Bioscience, Inc. (incorporated by reference to Exhibit 3.2 to the Annual Report on Form 10-K, filed with the SEC on October 29, 2012)
  - 3.2.1 Amendment to the Bylaws of Pure Bioscience, Inc. (incorporated by reference to Exhibit 3.2.1 to the Annual Report on Form 10-K, filed with the SEC on October 29, 2012)
  - 4.1 Form of Investor Warrant (incorporated by reference to Exhibit 4.5 to the Current Report on Form 8-K, filed with the SEC on May 22, 2009)
  - 4.2 Form of Investor Warrant (incorporated by reference to Exhibit 4.5 to the Current Report on Form 8-K, filed with the SEC on September 2, 2009)
  - 4.3 Wharton Capital Markets LLC Warrant (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K, filed with the SEC on March 16, 2012)
  - 4.4 Form of Underwriter's Warrant (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K, filed with the SEC on September 13, 2012)
  - 4.5 Morrison & Foerster LLP Warrant (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K, filed with the SEC on January 31, 2013)
  - 4.6 Form of Investor Warrant (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K, filed with the SEC April 23, 2013)
  - 4.7 Form of Investor Warrant (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K, filed with the SEC August 27, 2014)

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- 10.1 PURE Bioscience 2007 Equity Incentive Plan (incorporated by reference from Exhibit 10.15.8 to the Annual Report on Form 10-K, filed with the SEC on October 14, 2008)
- 10.2 # Form of Indemnification Agreement (incorporated by reference to Exhibit 10.2 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.3 Purchase Agreement, dated December 14, 2011, by and between Pure Bioscience, Inc. and Lincoln Park Capital Fund, LLC (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on December 15, 2011)
- 10.4 Purchase Agreement, dated December 15, 2011, by and between Pure Bioscience, Inc. and Lincoln Park Capital Fund, LLC (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on December 15, 2011)
- 10.5 Registration Rights Agreement, dated December 15, 2011, by and between Pure Bioscience, Inc. and Lincoln Park Capital Fund, LLC (incorporated by reference to Exhibit 10.3 of the Current Report on Form 8-K filed with the SEC on December 15, 2011)

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- 10.6 Warrant, dated February 3, 2012, issued by Pure Bioscience, Inc. to Wharton Capital Markets LLC (incorporated by reference to Exhibit 4.1 of the Quarterly Report on Form 10-Q filed with the SEC on March 16, 2012)
- 10.7 First Amendment to Purchase Agreement, dated April 5, 2012, by and between Pure Bioscience, Inc. and Lincoln Park Capital Fund, LLC (incorporated by reference to Exhibit 10.15 of the Registration Statement on Form S-1 filed with the SEC on April 10, 2012)
- 10.8 Securities Purchase Agreement, dated June 26, 2012, by and between Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on June 29, 2012)
- 10.9 Form of Common Stock Purchase Warrant (incorporated by reference to Exhibit 10.5 of the Current Report on Form 8-K filed with the SEC on June 29, 2012)
- 10.10 Securities Purchase Agreement, dated June 29, 2012, among Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on July 6, 2012)
- 10.11 Form of Common Stock Purchase Warrant (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on July 6, 2012)
- 10.12 Addendum to Transaction Documents, dated July 5, 2012, by and among Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.6 of the Current Report on Form 8-K/A filed with the SEC on July 13, 2012)
- 10.13 Settlement Agreement, effective July 9, 2012, among Pure Bioscience, Inc. Richmond Sciences, LLC, Richmond Holdings, Inc., Richmond Corporation, IV-7 Direct, LLC, and The Coalition to Save Pure (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on July 12, 2012)
- 10.14 Second Addendum to Transaction Documents, dated August 20, 2012, by and between Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on September 14, 2012)
- 10.15 Third Addendum to Transaction Documents, dated August 20, 2012, by and between Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on September 14, 2012)
- 10.16 Underwriting Agreement, dated September 11, 2012, by and between Pure Bioscience, Inc. and Aegis Capital Corp. (incorporated by reference to Exhibit 1.1 of the Current Report on Form 8-K filed with the SEC on September 13, 2012)
- 10.17 Form of Underwriter Warrant (incorporated by reference to Exhibit 4.1 of the Current Report on Form 8-K filed with the SEC on September 13, 2012)
- 10.18 Letter Agreement, dated as of January 25, 2013, between Pure Bioscience, Inc., and Morrison & Foerster LLP (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on January 31, 2013)
- 10.19 Promissory Note, dated as of January 25, 2013, in favor of Morrison & Foerster LLP (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on January 31, 2013)
- 10.20 Securities Purchase Agreement, dated as of April 16, 2013, between Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.1 of the Current

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Report on Form 8-K filed with the SEC on April 23, 2013)

- 10.21 Registration Rights Side Letter Agreement, dated as of April 16, 2013, between Pure Bioscience, Inc. and Harmony Bioscience, Inc. (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on April 23, 2013)
- 10.22 Securities Purchase Agreement, dated as of April 24, 2013, between Pure Bioscience, Inc. and each purchaser identified on the signature pages thereto (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on April 29, 2013)
- 10.23 Registration Rights Side Letter Agreement, dated as of April 23, 2013, between Pure Bioscience, Inc. and Sentinel Capital Solutions, Inc. (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on April 29, 2013)
- 10.24 Form of Common Stock Purchase Agreement dated as of August 13, 2013 (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)

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- 10.25 Services Agreement dated as of August 13, 2013, between Pure Bioscience, Inc. and Pillar Marketing Group, Inc. (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)
- 10.26 # Purchase, Severance, and Release Agreement dated as of August 13, 2013 between Pure Bioscience, Inc. and Michael L. Krall (incorporated by reference to Exhibit 10.3 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)
- 10.27 Voting Support Agreement and Irrevocable Proxy dated as of August 13, 2013 between Pure Bioscience, Inc. and Michael L. Krall (incorporated by reference to Exhibit 10.4 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)



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- 10.28 # Purchase, Severance, and Release Agreement dated as of August 13, 2013 between Pure Bioscience, Inc. and Donna Singer (incorporated by reference to Exhibit 10.5 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)
- 10.29 Voting Support Agreement and Irrevocable Proxy dated as of August 13, 2013 between Pure Bioscience, Inc. and Donna Singer (incorporated by reference to Exhibit 10.6 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)
- 10.30 # Settlement and Release Agreement dated as of August 13, 2013 between Pure Bioscience, Inc. and Dennis Brovarone (incorporated by reference to Exhibit 10.7 of the Current Report on Form 8-K filed with the SEC on August 20, 2013)
- 10.31 Subscription Agreement dated as of October 14, 2013 between Pure Bioscience, Inc. and purchaser identified on Exhibit A attached thereto (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on October 15, 2013)
- 10.32 # Director Agreement dated as of September 17, 2013 between Pure Bioscience, Inc. and Gary D. Cohee (incorporated by reference to Exhibit 10.32 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.33 # Employment Agreement dated as of October 23, 2013 between Pure Bioscience, Inc. and Henry R. Lambert (incorporated by reference to Exhibit 10.33 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.34 # Employment Agreement dated as of October 23, 2013 between Pure Bioscience, Inc. and Peter C. Wulff (incorporated by reference to Exhibit 10.34 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.35 # Chairman Agreement dated as of October 23, 2013 between Pure Bioscience, Inc. and Dave J. Pfanzelter (incorporated by reference to Exhibit 10.35 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.36 # Form of RSU Agreement between Pure Bioscience, Inc. and Non-employee directors (incorporated by reference to Exhibit 10.36 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.37 # RSU Agreement dated as of October 23, 2013 between Pure Bioscience, Inc. and Henry R. Lambert (incorporated by reference to Exhibit 10.37 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.38 # RSU Agreement dated as of October 23, 2013 between Pure Bioscience, Inc. and Peter C. Wulff (incorporated by reference to Exhibit 10.38 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.39 # RSU Agreement dated as of October 23, 2013 between Pure Bioscience, Inc. and Dave J. Pfanzelter (incorporated by reference to Exhibit 10.39 to the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.40 Form of Subscription Agreement, dated November 18, 2013 (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on November 18, 2013)
- 10.41 Form of Officer and Director Indemnification Agreement (incorporated by reference to Exhibit 10.2 of the Annual Report on Form 10-K filed with the SEC on October 24, 2013)
- 10.42 Payoff Agreement, dated as of December 18, 2013, by and between Pure Bioscience, Inc. and Morrison & Foerster LLP (incorporated by reference to Exhibit 10.2 of the Quarterly Report on Form 10-Q filed

with the SEC on March 13, 2014)

- 10.43 Strategic Collaboration Agreement, dated December 11, 2013, by and between Pure Bioscience, Inc. and Intercon Chemical Company (incorporated by reference to Exhibit 10.3 of the Quarterly Report on Form 10-Q filed with the SEC on March 13, 2014)
- 10.44 Form of Subscription Agreement, (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on April 29, 2014)
- 10.45 Amendment to Director Agreement dated as of April 24, 2014, between Pure Bioscience, Inc. and Gary D. Cohee (incorporated by reference to Exhibit 10.2 of the Quarterly Report on Form 10-Q filed with the SEC on June 10, 2014)
- 10.46 Securities Purchase Agreement, dated August 22, 2014 (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed with the SEC on August 27, 2014)
- 10.47 Registration Rights Agreement, dated August 22, 2014 (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed with the SEC on August 27, 2014)

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- 10.48 Amendment to Services Agreement, dated October 2, 2014, between Pure Bioscience, Inc. and Pillar Marketing Group, Inc. (incorporated by reference to Exhibit 10.48 of the Registration Statement on Form S-1 filed with the SEC on October 10, 2014)
- 21.1 Subsidiaries of the Registrant (incorporated by reference to Exhibit 21.1 to the Annual Report on Form 10-K, filed with the SEC on October 13, 2009)
- 23.1 \* Consent of Mayer Hoffman McCann P.C.
- 31.1 \* Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 \* Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 \* Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 \* Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 \* The following materials from the Company's Annual Report on Form 10-K for the annual period ended July 31, 2014, formatted in XBRL (eXtensible Business Reporting Language): (i) Consolidated Balance Sheets as at July 31, 2014 and 2013; (ii) Consolidated Statements of Operations for the years ended July 31, 2014 and 2013; (iii) Consolidated Statements of Stockholders' Equity for the years ended July 31, 2014 and 2013, (iv) Consolidated Statements of Cash Flows for the years ended July 31, 2014 and 2013; and (v) Notes to Consolidated Financial Statements.

\* Filed herewith

# Management contract or compensatory plan or arrangement

**Table of Contents****Signatures**

Pursuant to the requirements of Section 13 or 15(d) 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.

<b>PURE BIOSCIENCE, INC.</b>	<b>DATE</b>
/s/ HENRY R. LAMBERT Henry R. Lambert  Chief Executive Officer	October 28, 2014
/s/ PETER C. WULFF Peter C. Wulff  Chief Financial Officer / Chief Operating Officer	October 28, 2014

Pursuant to the requirements of the Securities Exchange Act of 1934, this report is signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<b>NAME</b>	<b>TITLE</b>	<b>DATE</b>
/s/ HENRY R. LAMBERT Henry R. Lambert	CEO, Director	October 28, 2014
/s/ DAVE J. PFANZELTER Dave J. Pfanzelter	Chairman, Director	October 28, 2014
/s/ GARY D. COHEE Gary D. Cohee	Director	October 28, 2014
/s/ DR. DAVID THENO, JR. Dr. David Theno, Jr.	Director	October 28, 2014
/s/ WILLIAM OTIS William Otis	Director	October 28, 2014
/s/ TOM Y. LEE Tom Y. Lee	Director	October 28, 2014

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**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Stockholders

**Pure Bioscience, Inc.**

We have audited the accompanying consolidated balance sheets of **Pure Bioscience, Inc.** ( the Company ) as of July 31, 2014 and 2013, and the related consolidated statements of operations, stockholders' equity (deficit) and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Pure Bioscience, Inc. as of July 31, 2014 and 2013, and the consolidated results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Mayer Hoffman McCann P.C.

San Diego, California

October 28, 2014

**Table of Contents****Pure Bioscience, Inc.****Consolidated Balance Sheets**

	<b>July 31, 2014</b>	<b>July 31, 2013</b>
<b>Assets</b>		
Current assets		
Cash and cash equivalents	\$ 86,000	\$ 32,000
Accounts receivable, net	47,000	18,000
Inventories, net	249,000	365,000
Prepaid expenses	96,000	71,000
<b>Total current assets</b>	<b>478,000</b>	<b>486,000</b>
Property, plant and equipment, net	36,000	146,000
Patents, net	1,345,000	1,430,000
<b>Total assets</b>	<b>\$ 1,859,000</b>	<b>\$ 2,062,000</b>
<b>Liabilities and stockholders equity (deficit)</b>		
Current liabilities		
Accounts payable	\$ 1,096,000	\$ 1,134,000
Restructuring liability	323,000	
Note payable, current		368,000
Accrued liabilities	401,000	600,000
Derivative liability	9,000	51,000
<b>Total current liabilities</b>	<b>1,829,000</b>	<b>2,153,000</b>
Note payable, less current portion		887,000
Deferred rent	13,000	13,000
<b>Total liabilities</b>	<b>1,842,000</b>	<b>3,053,000</b>
Commitments and contingencies (See Note 7)		
Stockholders equity (deficit)		
Preferred stock, \$0.01 par value: 5,000,000 shares authorized, no shares issued		
Common stock, \$0.01 par value: 100,000,000 shares authorized, 29,394,940 shares issued and outstanding at July 31, 2014, and 12,569,503 shares issued and outstanding at July 31, 2013		
	295,000	126,000
Additional paid-in capital	80,943,000	69,054,000
Accumulated deficit	(81,221,000)	(70,171,000)
<b>Total stockholders equity (deficit)</b>	<b>17,000</b>	<b>(991,000)</b>
<b>Total liabilities and stockholders equity (deficit)</b>	<b>\$ 1,859,000</b>	<b>\$ 2,062,000</b>

*See accompanying notes.*

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**Table of Contents****Pure Bioscience, Inc.****Consolidated Statements of Operations**

	<b>Year Ended</b>	
	<b>July 31,</b>	
	<b>2014</b>	<b>2013</b>
Net product sales	\$ 550,000	\$ 820,000
Operating costs and expenses		
Cost of goods sold	344,000	565,000
Selling, general and administrative	5,056,000	5,154,000
Research and development	1,032,000	1,169,000
Share-based compensation	2,958,000	720,000
Other share-based expenses	308,000	
Restructuring costs	2,754,000	
Impairment of patents		551,000
Total operating costs and expenses	12,452,000	8,159,000
Loss from operations	(11,902,000)	(7,339,000)
Other income (expense)		
Change in derivative liability	(55,000)	268,000
Interest expense, net	(10,000)	(593,000)
Gain on extinguishment of debt	727,000	
Other income (expense), net	190,000	(7,000)
Total other income (expense)	852,000	(332,000)
Net loss	\$ (11,050,000)	\$ (7,671,000)
Basic and diluted net loss per share	\$ (0.43)	\$ (0.71)
Shares used in computing basic and diluted net loss per share	25,609,548	10,838,140

*See accompanying notes.*

**Table of Contents****Pure Bioscience, Inc.****Consolidated Statements of Stockholders Equity (Deficit)**

	Common Stock		Additional Paid-In Capital	Accumulated Deficit	Total Stockholders Equity (Deficit)
	Shares	Amount			
Balance, July 31, 2012	6,644,555	67,000	63,251,000	(62,500,000)	818,000
Issuance of common stock in a registered offering, net	4,341,615	43,000	4,184,000		4,227,000
Issuance of common stock in a private placement, net	1,183,333	12,000	427,000		439,000
Share-based compensation expense - stock options			701,000		701,000
Share-based compensation expense - restricted stock			19,000		19,000
Warrants issued in connection with note payable			245,000		245,000
Issuance of common stock for consulting agreements	400,000	4,000	227,000		231,000
Net loss				(7,671,000)	(7,671,000)
Balance, July 31, 2013	12,569,503	\$ 126,000	\$ 69,054,000	\$ (70,171,000)	\$ (991,000)
Issuance of common stock in private placements, net	12,082,194	123,000	6,494,000		6,617,000
Shares issued in connection with financings	415,643	4,000	(4,000)		
Share-based compensation expense - stock options			80,000		80,000
Share-based compensation expense - restricted stock units			2,878,000		2,878,000
Shares issued in connection with severance agreements	1,165,000	11,000	814,000		825,000
Stock issued to investors to amend subscription agreements	218,938	2,000	283,000		285,000
Stock issued for services	20,000		25,000		25,000
Issuance of common stock for consulting agreements	1,100,000	11,000	759,000		770,000
Issuance of common stock for the cashless exercise of warrants	100,662	1,000	(1,000)		
Settlement of warrant liability			97,000		97,000
Issuance of common stock upon vesting of restricted stock units	1,205,000	12,000	(12,000)		
Issuance of penalty warrants			23,000		23,000
Warrants issued for services provided			121,000		121,000

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Issuance of common stock upon exercise of warrants	518,000	5,000	332,000		337,000
Net loss				(11,050,000)	(11,050,000)
Balance, July 31, 2014	29,394,940	\$ 295,000	\$ 80,943,000	\$ (81,221,000)	\$ 17,000

*See accompanying notes.*

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**Table of Contents****Pure Bioscience, Inc.****Consolidated Statements of Cash Flows**

	<b>Year Ended July 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Operating activities</b>		
Net loss	\$ (11,050,000)	\$ (7,671,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Share-based compensation	2,958,000	720,000
Stock issued for services	25,000	
Warrants issued for services	121,000	
Amortization of stock issued for services	679,000	255,000
Stock issued under severance agreements	825,000	
Stock issued to investors to amend subscription agreements	285,000	
Settlement of vendor payables	182,000	
Fair value of penalty warrants issued	23,000	
Gain on extinguishment of debt	(727,000)	
Gain on fixed asset sale	(7,000)	
Depreciation and amortization	248,000	311,000
Change in fair value of derivative liability	55,000	(268,000)
Inventory reserve	128,000	347,000
Impairment of patents		551,000
Troubled debt restructuring loss		25,000
Amortization of deferred financing costs		215,000
Amortization of debt discount		371,000
Changes in operating assets and liabilities:		
Accounts receivable	(29,000)	82,000
Inventories	(12,000)	149,000
Prepaid expenses	66,000	37,000
Accounts payable and accrued liabilities	(96,000)	962,000
Deferred rent		10,000
Net cash used in operating activities	(6,326,000)	(3,904,000)
<b>Investing activities</b>		
Investment in patents	(91,000)	(219,000)
Proceeds from sale of fixed assets	66,000	
Purchases of property, plant and equipment	(21,000)	(12,000)
Net cash used in investing activities	(46,000)	(231,000)
<b>Financing activities</b>		
Net proceeds from the sale of common stock	6,617,000	4,666,000
Net proceeds from the exercise of warrants	337,000	
Payment of Bridge Loan		(1,333,000)

Payment on note payable	(528,000)	(43,000)
Net cash provided by financing activities	6,426,000	3,290,000
Net increase (decrease) in cash and cash equivalents	54,000	(845,000)
Cash and cash equivalents at beginning of year	32,000	877,000
Cash and cash equivalents at end of year	\$ 86,000	\$ 32,000

**Supplemental disclosure of cash flow information**

Cash paid for taxes	\$ 4,000	\$ 1,600
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**Supplemental disclosure of non-cash investing and financing activities**

Common stock issued for prepaid services	\$ 175,000	\$ 231,000
Common stock issued in connection with financing	\$ 376,000	\$
Settlement of warrant liability	\$ 97,000	\$
Issuance of common stock for the cashless exercise of warrants	\$ 1,000	\$

During the fiscal year ended July 31, 2013, we recorded a reduction of approximately

\$1,519,000 in accounts payable in exchange for a note payable of \$1,125,000, accrued interest of \$174,000, and warrants valued at \$245,000, with a resulting \$25,000 restructuring loss.

*See accompanying notes.*

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**Pure Bioscience, Inc.**

**Notes to Consolidated Financial Statements**

**1. Organization and Business**

All references to PURE, we, our, and us refer to Pure Bioscience, Inc. and our wholly owned subsidiary.

Pure Bioscience, Inc. is focused on developing and commercializing our proprietary antimicrobial products that provide solutions to the health and environmental challenges of pathogen and hygienic control. Our technology platform is based on patented stabilized ionic silver, and our initial products contain silver dihydrogen citrate, or SDC. SDC is a broad-spectrum, non-toxic antimicrobial agent that is manufactured as a liquid delivered in various concentrations. We currently distribute and contract the manufacture and distribution of, our SDC-based disinfecting and sanitizing products, which are registered by the Environmental Protection Agency, or EPA. We also contract manufacture and sell SDC-based formulations to manufacturers for use as a raw material ingredient in the production of personal care products. We believe our technology platform has potential application in a number of industries. We intend to focus our current resources on providing food safety solutions to the food industry

We were incorporated in the state of California in August 1992 as Innovative Medical Services. In September 2003, we changed our name to Pure Bioscience. In March 2011, we reincorporated in the state of Delaware. We operate in one business segment.

Effective on August 14, 2012 and commencing with the opening of trading on August 15, 2012, we effected a reverse stock split of our issued and outstanding common stock, \$0.01 par value per share, at a ratio of one-for-eight, with each eight (8) issued and outstanding shares of our common stock automatically combined and converted into one (1) issued and outstanding share of our common stock. The reverse stock split was approved by stockholders holding a majority of our outstanding voting power at our annual meeting of stockholders held on July 31, 2012. All information in our consolidated financial statements and the notes thereto regarding share amounts of our common stock and prices per share of our common stock has been adjusted to reflect the application of the reverse stock split on a retroactive basis.

**Liquidity**

Since our inception, we have financed our operations primarily through public and private offerings of securities, debt financings, and revenue from product sales and license agreements. We have a history of recurring losses, and as of July 31, 2014 we have incurred a cumulative net loss of \$81,221,000.

As of July 31, 2014, we had \$86,000 in cash and cash equivalents, and \$1,829,000 of current liabilities. As of July 31, 2014, we had no long term debt.

Subsequent to July 31, 2014, we received approximately \$7.49 million in connection with private placements (see Note 13).

Our future capital requirements depend on numerous forward-looking factors. These factors may include, but are not limited to, the following: the acceptance of, and demand for, our products; our success and the success of our partners in selling our products; our success and the success of our partners in obtaining regulatory approvals to sell our products; the costs of further developing our existing products and technologies; the extent to which we invest in new product and technology development; and the costs associated with the continued operation, and any future growth, of

our business. The outcome of these and other forward-looking factors will substantially affect our liquidity and capital resources.

We expect that we will need to increase our liquidity and capital resources by one or more measures. These measures may include, but are not limited to, the following: reducing operating expenses; obtaining financing through the issuance of equity, debt, or convertible securities; entering into partnerships, licenses, or other arrangements with third parties; and reducing the exercise price of outstanding warrants. Any one of these measures could substantially reduce the value to us of our technology and its commercial potential. If we issue equity, debt or convertible securities to raise additional funds, our existing stockholders may experience dilution, and the new equity, debt or convertible securities may have rights, preferences and privileges senior to those of our existing stockholders. There is no guarantee that we would be able to obtain capital on terms acceptable to us, or at all.

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If we are unable to obtain sufficient capital, it would have a material adverse effect on our business and operations. It could cause us to fail to execute our business plan, fail to take advantage of future opportunities, or fail to respond to competitive pressures or customer requirements. It also may require us to delay, scale back or eliminate some or all of our research and development programs, to license to third parties the right to commercialize products or technologies that we would otherwise commercialize ourselves, or to reduce or cease operations. If adequate funds are not available when needed, we may be required to significantly modify our business model and operations to reduce spending to a sustainable level.

We believe our available cash received from financings subsequent to our year ended July 31, 2014, our current efforts to market and sell our products, and our ability to significantly reduce expenses, will provide sufficient cash resources to satisfy our needs over the next 12 months. However, we do not yet have, and we may never have, significant cash inflows from product sales or from other sources of revenue to offset our ongoing and planned investments in, research and development projects, regulatory submissions, business development activities, and sales and marketing, among other investments. Some or all of our ongoing or planned investments may not be successful. In addition, irrespective of our cash resources, we may be contractually or legally obligated to make certain investments which cannot be postponed.

## **Recent Corporate Developments**

### ***New Board of Directors and Management Team***

On August 13, 2013, the following managerial and corporate governance changes occurred to create a new Board of Directors, or Board, and management team:

Michael L. Krall, Donna Singer, and Dennis Brovarone resigned as members of the Board;

Michael L. Krall, Donna Singer, and Dennis Atchley resigned all positions respectively held by them as officers of the Company;

Dave J. Pfanzelter was appointed by the Board to be the Chairman of the Board;

Dave J. Pfanzelter was appointed by the Board to serve as Interim Chief Executive Officer;

Gary D. Cohee was appointed by the Board to serve as a member of the Board; and

Peter C. Wulff was appointed by the Board to serve as Chief Financial Officer, Chief Operating Officer, and Corporate Secretary.

On July 22, 2013, Jon Carbone and Paul Maier resigned as directors of the Company and as members of the Audit and Compensation Committees.



On September 10, 2013, the Board appointed Henry R. Lambert to serve as Chief Executive Officer and a member of the Board. In connection with the hiring of Henry R. Lambert to serve as our Chief Executive Officer, Dave J. Pfanzelter resigned his position as our Interim Chief Executive Officer. Mr. Pfanzelter continues to render significant services to us and continues to serve as our Chairman of the Board.

In October 2013, we appointed three additional members to the Board; Dr. David Theno, Jr., Craig Culver and William Otis. On April 9, 2014, Craig Culver resigned from the Board.

On October 24, 2014, we appointed Tom Y. Lee, CPA, to the Board. The Board now consists of six members who provide professional experience in business and finance; food science and food safety; and foodservice and food manufacturing.

## **2. Summary of Significant Accounting Policies**

### ***Basis of Presentation***

The accompanying consolidated financial statements include the consolidated accounts of Pure Bioscience, Inc. and its wholly owned subsidiary, ETIH2O Corporation, a Nevada corporation. ETIH2O Corporation has no business and no material assets or liabilities and there have been no significant transactions related to ETIH2O during the periods presented in the consolidated financial statements. All inter-company balances and transactions have been eliminated.

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### **Use of Estimates**

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, or GAAP, requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements, and the disclosures made in the accompanying notes to the consolidated financial statements. Actual results could differ materially from those estimates.

### **Reclassification**

Certain reclassifications have been made to prior period amounts to conform to current period presentation. These reclassifications did not have an impact on our results of operations or financial condition as of and for the years ended July 31, 2014 and 2013.

### **Cash and Cash Equivalents**

Cash and cash equivalents consist of cash and highly liquid investments with original maturities from purchase date of three months or less.

### **Fair Value of Financial Instruments**

Certain of our financial instruments including cash and cash equivalents, accounts receivable, inventories, prepaid expenses, accounts payable, accrued liabilities, note payable and deferred rent are carried at cost, which is considered to be representative of their respective fair values because of the short-term nature of these instruments. Our loan payable and derivative liabilities are carried at estimated fair value (see Note 5 and 6).

### **Derivative Financial Instruments**

We do not use derivative instruments to hedge exposures to cash flow or market or foreign currency risks.

We review the terms of the common stock, warrants and convertible debt we issue to determine whether there are derivative instruments, including embedded conversion options that are required to be bifurcated and accounted for separately as derivative financial instruments. In circumstances where the host instrument contains more than one embedded derivative instrument, including a conversion option, that is required to be bifurcated, the bifurcated derivative instruments are accounted for as a single, compound derivative instrument.

Derivatives are initially recorded at fair value and are then revalued at each reporting date with changes in the fair value reported as non-operating income or expense. When the equity or convertible debt instruments contain embedded derivative instruments that are to be bifurcated and accounted for as liabilities, the total proceeds received are first allocated to the fair value of all the bifurcated derivative instruments. The remaining proceeds, if any, are then allocated to the host instruments themselves, usually resulting in those instruments being recorded at a discount from their face value.

The discount from the face value of any convertible debt, together with the stated interest on the instrument, is amortized over the life of the instrument through periodic charges to interest expense, using the effective interest method.

### **Accounts Receivable**

Trade accounts receivable are recorded net of allowances for doubtful accounts. Estimates of allowances for doubtful accounts are determined based on historical payment patterns and individual customer circumstances. The allowance for doubtful accounts was zero at July 31, 2014 and 2013.

Inventories

Inventories are stated at the lower of cost or net realizable value, and net of a valuation allowance for potential excess or obsolete material. Cost is determined using the average cost method.

Property, Plant and Equipment

Property, plant and equipment is stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets. The estimated useful lives of our property, plant, and equipment range from three to ten years. Capitalized costs associated with leasehold improvements are depreciated over the lesser of the useful life of the asset or the remaining life of the lease. Depreciation is generally included in selling, general and administrative expense. Depreciation related to manufacturing is systematically allocated to inventory produced, and expensed through cost of goods sold at the time inventory is sold.

Patents

We have filed a number of patent applications with the United States Patent and Trademark Office and in foreign countries. Certain legal and related costs incurred in connection with pending patent applications have been capitalized. Costs related to successful patent applications are amortized over the lesser of the remaining useful life of the related technology or the remaining patent life, commencing on the date the patent is issued. Capitalized costs related to patent applications are expensed in the period in which a determination is made not to pursue such applications.

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### **Impairment of Long-Lived Assets**

In accordance with GAAP, if indicators of impairment exist, we assess the recoverability of the affected long-lived assets by determining whether the carrying value of such assets can be recovered through undiscounted future operating cash flows. If impairment is indicated, we measure the amount of such impairment by comparing the carrying value of the asset to the fair value of the asset and we record the impairment as a reduction in the carrying value of the related asset and a charge to operating results. Estimating the undiscounted future cash flows associated with long-lived assets requires judgment, and assumptions could differ materially from actual results. During the year ended July 31, 2013 we incurred \$551,000 of expense relating to the impairment of long-lived assets (See Note 3). No impairment expense was recorded during the year ended July 31, 2014.

### **Revenue Recognition**

We sell our products to distributors and end users. We record revenue when we sell products to our customers, rather than when our customers resell products to third parties. When we sell products to our customers, we reduce the balance of our inventory with a corresponding charge to cost of goods sold. We do not currently have any consignment sales.

Terms of our product sales are generally FOB shipping point. Product sales are recognized when delivery of the products has occurred (which is generally at the time of shipment), title has passed to the customer, the selling price is fixed or determinable, collectability is reasonably assured and we have no further obligations. Any amounts received prior to satisfying these revenue recognition criteria are recorded as deferred revenue. We record product sales net of discounts at the time of sale and report product sales net of such discounts.

We also license our products and technology to development and commercialization partners. Upfront product and technology license fees under multiple-element arrangements are deferred and recognized over the period of such services or performance, if such arrangements require on-going services or performance. Non-refundable amounts received for substantive milestones are recognized upon achievement of the milestone. Any amounts received prior to satisfying these revenue recognition criteria are recorded as deferred revenue.

### **Shipping and Handling Costs**

Shipping and handling costs incurred by us for product shipments are included in cost of goods sold and were minimal for the years ended July 31, 2014 and 2013.

### **Research and Development Costs**

Research and development costs are expensed as incurred.

### **Share-Based Compensation**

We grant equity-based awards under share-based compensation plans. We estimate the fair value of share-based payment awards using the Black-Scholes option valuation model. This fair value is then amortized over the requisite service periods of the awards. The Black-Scholes option valuation model requires the input of subjective assumptions, including price volatility of the underlying stock, risk-free interest rate, dividend yield, and expected life of the option. Share-based compensation expense is based on awards ultimately expected to vest, and therefore is reduced by expected forfeitures.

Other Income (Expense)

We record interest income, interest expense, change in derivative liabilities, as well as other non-operating transactions, as other income (expense) on our consolidated statements of operations.

During the year ended July 31, 2014, the Company recorded other income of approximately \$182,000 related to accounts payable vendor settlements, which is included in other income (expense).

Comprehensive Loss

Comprehensive loss is defined as the change in equity during a period from transactions and other events and circumstances from non-owner sources, including unrealized gains and losses on marketable securities and foreign currency translation adjustments. For the years ended July 31, 2014 and 2013, our comprehensive loss consisted only of net loss.

Income Taxes

We recognize deferred tax assets and liabilities for temporary differences between the tax basis of assets and liabilities and the amounts at which they are carried in the financial statements based upon the enacted tax rates in effect for the year in which the differences are expected to reverse. A valuation allowance is established to reduce deferred tax assets to the amount expected to be realized.

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**Table of Contents****Net Loss Per Share**

Basic net loss per common share is computed as net loss divided by the weighted average number of common shares outstanding for the period. Our diluted net loss per common share is the same as our basic net loss per common share because we incurred a net loss during each period presented, and the potentially dilutive securities from the assumed exercise of all outstanding stock options, restricted stock units, and warrants would have an antidilutive effect. As of July 31, 2014 and 2013, the number of shares issuable upon the exercise of stock options, the vesting of restricted stock units, and the exercise of warrants, none of which are included in the computation of basic net loss per common share, was 6,136,355 and 1,877,876 respectively.

**Recent Accounting Pronouncements**

In May 2014, the Financial Accounting Standards Board ( FASB ) issued Accounting Standard Update No. 2014-09, Revenue from Contracts with Customers, ( ASU 2014-09 ) an updated standard on revenue recognition. ASU 2014-09 provides enhancements to the quality and consistency of how revenue is reported by companies while also improving comparability in the financial statements of companies reporting using International Financial Reporting Standards or GAAP. The main purpose of the new standard is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which a company expects to be entitled in exchange for those goods or services. The new standard also will result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively and improve guidance for multiple-element arrangements. ASU 2014-09 will be effective for the Company in the first quarter of fiscal year 2018 and may be applied on a full retrospective or modified retrospective approach. The Company is currently evaluating the potential impact that adoption of this standard may have on its financial statements.

In June 2014, the Financial Accounting Standards Board issued Accounting Standards Update, or ASU, No. 2014-12 Compensation Stock Compensation (Topic 718). The ASU provides guidance for accounting for share-based payments when the terms of an award provide that a performance target could be achieved after the requisite service period. That is the case when an employee is eligible to retire or otherwise terminate employment before the end of the period in which a performance target could be achieved and still be eligible to vest in the award if and when the performance target is achieved. The amendment requires a performance target that affects vesting and that could be achieved after requisite service period be treated as a performance condition. Compensation cost should be recognized in the period in which it becomes probable that such performance condition would be achieved and should represent the compensation cost attributable to the periods for which the requisite service has already been rendered. Those amendments are effective for annual reporting periods beginning after December 15, 2015, and interim periods therein. The Company is currently evaluating the potential impact that adoption of this standard may have on its financial statements.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern, which is intended to define management's responsibility to evaluate whether there is substantial doubt about an organization's ability to continue as a going concern and to provide related footnote disclosures. This ASU provides guidance to an organization's management, with principles and definitions that are intended to reduce diversity in the timing and content of disclosures that are commonly provided by organizations today in the financial statement footnotes. The amendments are effective for annual periods ending after December 15, 2016, and interim periods within annual periods beginning after December 15, 2016. Early application is permitted for annual or interim reporting periods for which the financial statements have not previously been issued. The Company does not intend to early adopt this standard. The Company does not expect the adoption of this standard to have an impact on its financial statements.

**3. Balance Sheet Details**

Inventories consist of the following:

	<b>July 31,</b>	
	<b>2014</b>	<b>2013</b>
Raw materials	\$ 102,000	\$ 70,000
Finished goods	147,000	295,000
	\$ 249,000	\$ 365,000

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During the fiscal year ended July 31, 2014, we established a reserve of \$128,000 for slow moving finished goods inventory that was manufactured in prior years. During the fiscal year ended July 31, 2013, we established an inventory reserve of \$347,000. The majority of the reserve related to components such as, plastic bottles, spray triggers, miscellaneous plastics, and numerous corrugated cardboard configurations.

In addition, during the fiscal year ended July 31, 2014, we received \$20,000 from the sale of inventory which was previously reserved during the fiscal year ended July 31, 2013. During the fiscal year ended July 31, 2013, we received \$58,000 from the sale of silver held in inventory. At the time of sale, the silver had a book value of \$40,000. The \$20,000 gain on sale of inventory sold during the current fiscal year and the \$18,000 gain on sale of silver sold during the prior fiscal year is reflected in the other income (expense) section of the consolidated statement of operations.

Property, plant, and equipment consist of the following:

	<b>July 31,</b>	
	<b>2014</b>	<b>2013</b>
Computers and equipment	\$ 508,000	\$ 921,000
Furniture and fixtures	21,000	21,000
Leasehold improvements	622,000	622,000
	1,151,000	1,564,000
Less accumulated depreciation	(1,115,000)	(1,418,000)
	\$ 36,000	\$ 146,000

Depreciation expense was \$71,000 and \$123,000 for the years ended July 31, 2014 and 2013, respectively.

Patents consist of the following:

	<b>July 31,</b>	
	<b>2014</b>	<b>2013</b>
Patents	\$ 3,482,000	\$ 3,389,000
Less accumulated amortization	(2,137,000)	(1,959,000)
	\$ 1,345,000	\$ 1,430,000

Due to the significant changes in our strategic business objectives and utilization of our assets, we have determined cost associated with the pending patent applications in numerous foreign geographic locations have been impaired. As a result, during the year ended July 31, 2013, we reduced the carrying value of our patents and recorded a \$551,000 patent impairment. There were no patent impairments during our fiscal year ended July 31, 2014.

Patent amortization expense was \$177,000 and \$188,000 for the years ended July 31, 2014 and 2013, respectively. At July 31, 2014, the weighted average remaining amortization period for all patents was approximately eight years. The



annual patent amortization expense for the next five years is estimated to be approximately \$183,000 per year.

#### **4. Promissory Note**

On January 25, 2013, we entered into a Letter Agreement (the Agreement ) with Morrison & Foerster LLP ( Morrison ). Under the terms of the Agreement, we issued a Promissory Note (the Note ) in favor of Morrison in the principal amount of \$1,125,000. In consideration for the Note, Morrison agreed to waive \$1,519,000 of amounts due and payable to Morrison for legal services rendered. The Note bore interest at the rate of 7.5% per annum, but the then outstanding balance would accrue interest at the rate of 10% per annum upon the occurrence of an event of default (as defined in the Note). Beginning March 31, 2013, and on or before the last business day of each calendar month thereafter, we were required to pay all accrued but unpaid interest on the then unpaid amount of outstanding principal. Beginning on February 28, 2014, we were required to pay equal monthly principal installments of approximately \$47,000, plus interest. We could prepay the

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outstanding balance under the Note in full or in part at any time, which would result in a discount of the then outstanding balance. The Note was to mature on February 28, 2016, unless accelerated pursuant to an event of default or upon the consummation of a change of control. As a result of the Agreement, we reclassified the amount due and payable to Morrison from accounts payable to note payable during the fiscal year ended July 31, 2013.

In consideration for Morrison's acceptance of the Note, we issued Morrison a warrant to purchase 375,000 shares of our common stock at an exercise price of \$0.83 per share. The warrant was exercisable immediately and expires on January 24, 2018. The warrant may be exercised by Morrison with a cash payment or, in lieu thereof, at its election, through a net exercise, as set forth in the warrant agreement. Neither the warrant nor the shares to be issued upon exercise thereof are registered for sale or resale under the Securities Act of 1933, as amended (the Securities Act), and have been or will be issued in reliance on an exemption from registration under the Securities Act pursuant to Section 4(a)(2) thereof based on the offering of such securities to one investor and the lack of any general solicitation or advertising in connection with such issuance. We determined that the warrants issued in connection with the Note were equity instruments and did not represent derivative instruments. The fair value of the warrants issued to Morrison was \$245,000, based on the Black-Scholes valuation method assuming no dividend yield, volatility of 134%, a risk-free interest rate of 0.35%, and an expected life of 5 years.

This transaction was accounted for as a troubled debt restructuring. During the year ended July 31, 2013, we recorded \$25,000 of other expense resulting from the excess of the total cash outflows under the troubled debt restructuring, plus the expense related to the fair value of the warrant issued in conjunction with the debt, over the carrying amount of the Morrison payables prior to the restructuring. In accordance with the applicable guidance, interest to be paid under the Note of approximately \$174,000 was added to the carrying amount of the Note, and future payments of interest were to be reflected as a reduction to the carrying amount of the debt.

During the fiscal year ended July 31, 2014, we entered into a Promissory Note Payoff Agreement ( Payoff Agreement ) with Morrison. Under the Payoff Agreement, we paid \$500,000 in cash to Morrison to extinguish \$1,227,000 in unsecured debt owed to Morrison under the Note, dated January 25, 2013. We have no further obligations or liability under the Note. As a result of the Payoff Agreement, we recorded a gain of \$727,000 that is reflected in the other income (expense) section of the consolidated statement of operations.

During the fiscal year ended July 31, 2014, prior to the Payoff Agreement, we paid \$28,000 under the terms of the Note. During the fiscal year ended July 31, 2013, we paid \$43,000 under the terms of the Note.

**5. Convertible Note and Derivative Liability**

On June 26, 2012 and July 10, 2012 we received an aggregate of \$1,200,000 in cash consideration from nine lenders in exchange for our issuance to such lenders of secured convertible promissory notes, or the Convertible Notes, in an aggregate principal amount of \$1,333,000 and certain other consideration (including shares of our common stock and warrants to acquire shares of our common stock). We refer to such transaction as the Bridge Loan. Pursuant to the terms of the Convertible Notes and the other agreements entered in connection with the Bridge Loan, all amounts owed thereunder became due and payable upon the closing of our underwritten public offering on September 17, 2012 (See Note 8), and accordingly all such amounts were repaid during the year ended July 31, 2013. Due to the repayment of the Bridge Loan the debt discounts and deferred financing costs related to the Bridge Loan of \$371,000 and \$215,000, respectively, were recorded as interest expense during the year ended July 31, 2013.

While outstanding, the Convertible Notes were secured by a lien on all of our assets pursuant to a security agreement entered in connection with the Bridge Loan, and 575,000 shares of our common stock (later reduced to 500,000 shares pursuant to an amendment effective September 6, 2012), were issued in the name of an escrow agent as additional

collateral for the timely repayment of the Notes which were cancelled pursuant to our full repayment of the Bridge Loan. Additionally, the Convertible Notes could have been converted into shares of our common stock if the entire balance owed thereunder was not repaid by December 26, 2012 or an earlier event of default occurred. The conversion price of the Convertible Notes as of July 31, 2012 was \$3.28 per share, subject to adjustment as set forth in the Notes, including adjustment of the conversion price to the sale price to the public of shares of our common stock issued in a registered public offering, if lower, closed within the 60-day period commencing on June 26, 2012, if any. We analyzed the nature of the conversion terms of the Convertible Notes and determined that the conversion feature required derivative liability classification in accordance with authoritative guidance (See Note 6). At issuance, the fair value of the conversion feature totaled \$33,000. Due to the repayment of the Bridge Loan in September 2012, the derivative liability related to the conversion feature was settled during the year ended July 31, 2013 and, as such, there is no related liability as of July 31, 2013 and 2014. The change in fair value of \$33,000 was recorded as a change in derivative liability in the consolidated statement of operations in 2013.

We accounted for the 132,420 warrants issued in connection with the Bridge Loan in accordance with the accounting guidance

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for derivatives. The applicable accounting guidance sets forth a two-step model to be applied in determining whether a financial instrument is indexed to an entity's own stock, which would qualify such financial instruments for a scope exception. This scope exception specifies that a contract that would otherwise meet the definition of a derivative financial instrument would not be considered as such if the contract is both (i) indexed to the entity's own stock and (ii) classified in the stockholders' equity section of the entity's balance sheet. We determined the warrants were ineligible for equity classification due to anti-dilution provisions set forth therein.

We recorded the fair value of the warrants issued in connection with the Bridge Loan as a warrant liability due to anti-dilution provisions requiring the strike price of the warrants to be adjusted if we subsequently issue common stock at a lower stock price. The Company revalues the warrants at the end of each reporting period. The fair value of the warrants at July 31, 2014 and July 31, 2013 was \$9,000 and \$51,000, respectively. The change in fair value of the warrant liability for the fiscal years ended July 31, 2014 and 2013 was a decrease of \$55,000, and an increase of \$268,000, respectively, which was recorded as a change in derivative liability in the consolidated statements of operations.

During the fiscal year ended July 31, 2014, there were net exercises on an aggregate of 122,711 of the warrants issued in connection with the Bridge Loan, which resulted in the issuance of 100,662 shares of our common stock. As these warrants were net exercised, as permitted under the respective warrant agreements, we did not receive any cash proceeds. The warrants were revalued as of the settlement dates, and the change in fair value was recognized to earnings. The Company also recognized a reduction in the warrant liability based on the fair value as of the settlement date for the warrants exercised, with a corresponding increase in additional paid-in capital. As of July 31, 2014, there are 9,709 warrants outstanding that were issued in connection with the Bridge Loan.

The estimated fair value of the derivative liability was computed using a Monte Carlo option pricing model based the following assumptions:

	<b>July 31, 2014</b>	<b>July 31, 2013</b>
Volatility	163.5%	144.5%
Risk-free interest rate	0.98%	0.97%
Dividend yield	0.0%	0.0%
Expected life	2.4 years	3.4 years

**6. Fair Value of Financial Instruments**

Fair value is defined as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering such assumptions, the authoritative guidance establishes a three-tier value hierarchy, which prioritizes the inputs used in measuring fair value as follows:

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

Level 2 Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

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

In connection with the Bridge Loan, we issued warrants and convertible notes that have been accounted for as derivative liabilities.

We used Level 3 inputs for the valuation methodology of the derivative liabilities. The estimated fair values were computed using a Monte Carlo option pricing model based on various assumptions. Our derivative liabilities are adjusted to reflect estimated fair value at each period end, with any decrease or increase in the estimated fair value being recorded in other income or expense accordingly, as adjustments to the fair value of the derivative liabilities.

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The following table provides a reconciliation of the beginning and ending balances of the derivative liabilities for the years ended July 31, 2014 and 2013:

**Fair Value of Significant Unobservable Inputs (Level 3)**

	<b>Warrant Liability</b>	<b>Conversion Feature Liability</b>	<b>Total</b>
Balance at July 31, 2012	\$ 286,000	\$ 33,000	\$ 319,000
Issuances			
Settlement of conversion feature liability		(33,000)	(33,000)
Adjustments to estimated fair value	(235,000)		(235,000)
Balance at July 31, 2013	\$ 51,000	\$	\$ 51,000
Issuances			
Settlement of warrant liability	(97,000)		(97,000)
Adjustments to estimated fair value	55,000		55,000
Balance at July 31, 2014	\$ 9,000	\$	\$ 9,000

**7. Commitments and Contingencies****Severance Agreements**

In connection with Mr. Krall's separation from the Company (See Note 1), the Company entered into a Purchase, Severance, and Release Agreement effective August 13, 2013 with Mr. Krall (the "Krall Release Agreement"). The Krall Release Agreement provides for a mutual release of all claims between Mr. Krall and the Company. Mr. Krall is also prohibited from engaging in certain competitive activities until July 2017. Pursuant to the Krall Release Agreement, Mr. Krall (i) was paid \$25,000 on August 13, 2013; and, (ii) is entitled to receive \$30,000 per month for 18-months following August 13, 2013, during which time Mr. Krall shall provide consulting services to the Company. In consideration of Mr. Krall's transfer to the Company of certain enumerated intellectual property rights, the Company also (i) paid Mr. Krall the sum of \$125,000 on August 13, 2013; and, (ii) issued to Mr. Krall 850,000 shares of common stock on August 21, 2013 (the "Krall Shares"). The Krall Shares are subject to certain registration rights intended to register the Krall Shares. The Krall Shares are also subject to a Voting Support Agreement and Irrevocable Proxy (the "Krall Proxy"). The Krall Proxy gives our CEO the right to vote the Krall Shares for so long as Mr. Krall owns the Krall Shares. Mr. Krall will also continue to receive health insurance coverage over the term of the severance period, which will cost the Company \$20,000.

In connection with Ms. Singer's separation from the Company (See Note 1), we entered into a Purchase, Severance, and Release Agreement effective August 13, 2013 with Ms. Singer (the "Singer Release Agreement"). The Singer Release Agreement provides for a mutual release of all claims between Ms. Singer and the Company. Ms. Singer is also prohibited from engaging in certain competitive activities until August 2017. Pursuant to the Singer Release Agreement, Ms. Singer (i) was paid \$45,000 on August 13, 2013; (ii) is due the amount of her continued health insurance coverage until August 2014; and, (iii) is entitled to \$17,000 per month for 12-months following August 13, 2013, during which time Ms. Singer shall provide consulting services to the Company. In consideration of Ms. Singer's transfer to the Company of certain enumerated intellectual property rights, the Company also issued to Ms. Singer

300,000 shares of common stock on August 21, 2013 (the Singer Shares ). The Singer Shares are subject to certain registration rights intended to register the Singer Shares. The Singer Shares are also subject to a Voting Support Agreement and Irrevocable Proxy (the Singer Proxy ). The Singer Proxy gives our CEO the right to vote the Singer Shares for so long as Ms. Singer owns the Singer Shares. Ms. Singer will also continue to receive health insurance coverage over the term of the severance period, which will cost the Company \$18,000.

In connection with Mr. Brovarone s separation from the Company (See Note 1), we entered into a Severance and Release Agreement effective August 13, 2013 with Mr. Brovarone (the Brovarone Release Agreement ). The Brovarone Release Agreement provides for a mutual release of all claims between Mr. Brovarone and the Company. In addition, Mr. Brovarone will receive \$91,000, payable in 60 monthly installments of \$1,600, commencing 120 days after the separation date for amounts previously accrued as of July 31, 2013.

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On January 23, 2014, we entered into a General Release and Settlement Agreement with a former employee ( Employee Settlement ). Under the terms of the Employee Settlement, we will pay \$50,000 over a six-month period with payments commencing in March 2014, and issue 15,000 shares of common stock.

During the fiscal year ended July 31, 2014, the Company expensed approximately \$1,859,000, related to the Employee Settlement and the Purchase, Severance, and Release Agreements for Mr. Krall, Ms. Singer, and Mr. Brovarone. Approximately \$323,000 remains payable under the severance agreements and is included in the accrued restructuring liability section of the consolidated balance sheet as of July 31, 2014.

**Operating Leases**

During May 2014, we amended the lease of our primary facility in El Cajon, California under a noncancelable operating lease that now expires in December 2016. Per the terms of the agreement, our occupancy costs have decreased by approximately 60%. This facility includes our corporate offices, research and development laboratory, and warehouse. Rent expense including common area maintenance, was \$174,000 and \$286,000 for the years ended July 31, 2014 and 2013, respectively.

Future minimum annual lease payments for our primary facility as of July 31, 2014 are as follows:

2015	\$ 83,000
2016	84,000
2017	36,000
	\$ 203,000

**8. Stockholders Equity****Preferred Stock**

As of July 31, 2014, the Company's Board of Directors is authorized to issue 5,000,000 shares of preferred stock with a par value of \$0.01 per share, in one or more series. As of July 31, 2014 and 2013, there were no shares of preferred stock issued and outstanding.

**Common Stock**

As of July 31, 2014, 100,000,000 shares of common stock with a par value of \$0.01 per share are authorized for issuance.

**Private Placements**

In August 2013, we completed a private placement pursuant to which we sold 5,500,000 shares of our common stock. The shares were sold at a per share purchase price of \$0.20, resulting in approximately \$1,100,000 in aggregate gross proceeds to the Company. After deducting fees of \$43,000, the net proceeds to us were \$1,057,000.

On October 14 and October 16, 2013, we completed private placements pursuant to which we sold 2,441,270 shares of our common stock. The shares were sold at a per share purchase price of \$0.75 per share, resulting in



approximately \$1,831,000 in aggregate gross proceeds to the Company. After deducting fees of \$49,000, the net proceeds to us were \$1,782,000. In addition, between October 17, 2013 and October 31, 2013, we sold 442,667 shares of our common stock in private placements. The shares were sold at a per share purchase price of \$0.75 per share, resulting in approximately \$332,000 in aggregate gross proceeds to the Company. After deducting fees of \$8,000, the net proceeds to us were \$324,000. During December 2013, we amended the subscription agreements for investor who participated in the \$0.75 private placements. As a result, the per share purchase price of \$0.75 was reduced to \$0.70 per share, resulting in the issuance of an additional 218,938 shares of common stock. We recorded \$285,000 of expense associated with the price adjustment in the other share-based expenses section of the consolidated statement of operations. After the purchase price adjustment to \$0.70 per share, the total shares issued under the October private placements was 3,102,875, for aggregate net proceeds of \$2,106,000.

During the three months ended January 31, 2014, we completed private placements pursuant to which we sold 1,611,817 shares of our common stock, resulting in approximately \$1,514,000 in aggregate gross proceeds to the Company. After deducting fees of \$13,000, the net proceeds to us were \$1,501,000.

During the three months ended April 30, 2014, we completed private placements pursuant to which we sold 1,575,000 shares of our common stock, resulting in approximately \$1,545,000 in aggregate gross proceeds to the Company. After deducting fees of \$47,000, the net proceeds to us were \$1,498,000.

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During the three months ended July 31, 2014, we completed private placements pursuant to which we sold 511,440 shares of our common stock, resulting in net proceeds of \$455,000.

During the year ended July 31, 2014, the shares of common stock issued under the private placements were offered and sold without registration under the Securities Act, or state securities laws, in reliance on the exemptions provided by Section 4(a)(2) of the Securities Act and Regulation D promulgated thereunder and in reliance on similar exemptions under applicable state laws, based on the lack of any general solicitation or advertising in connection with the sale of the securities; the representation of each investor to the Company that it is an accredited investor (as that term is defined in Rule 501 of Regulation D) and that it was purchasing the securities for its own account and without a view to distribute them. The securities may not be offered or sold in the United States without an effective registration statement or pursuant to an exemption from applicable registration requirements.

On September 17, 2012, we closed an underwritten public offering of an aggregate of 4,341,615 shares of our common stock, including shares issued pursuant to the exercise of the underwriter's overallotment option, at a price to the public of \$1.10 per share. The gross proceeds from the offering were approximately \$4,776,000 and, after deducting \$549,000 for transaction costs, including discounts, commissions, and other offering expenses, such as legal and accounting fees, the net proceeds to us from the offering were approximately \$4,227,000. We used \$1,333,000 of the net proceeds from the offering to pay the full amount of the indebtedness we incurred in connection with the Bridge Loan, described in further detail under Note 5 above.

On April 17 and April 24, 2013, we completed the initial and second closings of a private placement pursuant to which we sold an aggregate of 1,000,000 shares of our common stock and warrants to purchase an aggregate of 500,000 shares of our common stock. The shares were sold at a per share purchase price of \$0.40, resulting in approximately \$400,000 in aggregate proceeds to us. After deducting fees of \$16,000, the net proceeds to us were \$384,000. The warrants have a term of three years from the initial exercise date, become exercisable six months after the date of issuance, and have an exercise price of \$0.65 per share. We determined that the warrants issued in connection with this private placement were equity instruments and did not represent derivative instruments. For the warrants issued in connection with the initial closing on April 17th, a fair value of \$119,000 was estimated for the warrants using the Black-Scholes valuation method using a volatility of 140.63%, an interest rate of 0.44% and a dividend yield of zero. For the warrants issued in connection with the second closing on April 24th, a fair value of \$100,000 was estimated for the warrants using the Black-Scholes valuation method using a volatility of 140.75%, an interest rate of 0.43% and a dividend yield of zero. As part of this financing, the Company granted certain registration rights, under which the Company agreed to file a registration statement covering the resale of the shares of common stock sold in this financing, as well as those shares issuable upon exercise of the warrant. In the event that we have not filed to register for resale the shares and warrant shares issued as part of the April 24, 2013 private placement, within 45 days of the closing date, the Company will issue 100 warrant shares for each day that such filing is not completed, not to exceed 18,000 warrant shares. As of April 30, 2014, the shares and warrant shares, issued in connection with the April 24, 2013 private placement, had not been registered for resale. As a result, the private placement participant received the entire 18,000 warrant shares as of April 30, 2014. The expense associated with the warrants was \$23,000 and is included in the other share-based expenses section of the consolidated statement of operations.

On June 26 and July 10, 2013, we completed the initial and second closings of a private placement pursuant to which we sold an aggregate of 183,333 shares of our common stock and warrants to purchase an aggregate of 91,667 shares of our common stock. The shares were sold at a per share purchase price of \$0.30, resulting in approximately \$55,000 in aggregate proceeds to us. The warrants have a three-year term, are immediately exercisable, and have an exercise price of \$0.50 per share. We determined that the warrants issued in connection with this private placement were equity instruments and did not represent derivative instruments. For the warrants issued in connection with the initial closing on June 26th, a fair value of \$13,000 was estimated for the warrants using the Black-Scholes valuation method using a

volatility of 146.80%, an interest rate of 0.69% and a dividend yield of zero. For the warrants issued in connection with the second closing on July 10th, a fair value of \$13,000 was estimated for the warrants using the Black-Sholes valuation method using a volatility of 146.89%, an interest rate of 0.73% and a dividend yield of zero. As part of this financing, the Company granted certain registration rights, under which the Company agreed to file a registration statement covering the resale of the shares of common stock sold in this financing, as well as those shares issuable upon exercise of the warrant. There are no penalties associated with the registration of shares and warrant shares.

During the year ended July 31, 2013, the shares of common stock issued under the private placements were offered and sold without registration under the Securities Act, or state securities laws, in reliance on the exemptions provided by Section 4(a)(2) of the Securities Act and Regulation D promulgated thereunder and in reliance on similar exemptions under applicable state laws, based on the lack of any general solicitation or advertising in connection with the sale of the securities; the representation of each investor to the Company that it is an accredited investor (as that term is defined in Rule 501 of

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Regulation D) and that it was purchasing the securities for its own account and without a view to distribute them. The securities may not be offered or sold in the United States without an effective registration statement or pursuant to an exemption from applicable registration requirements.

**Corporate Governance Restructuring Activity**

The following transactions occurred on August 13, 2013:

We entered into a two-year service agreement with Pillar Marketing Group, Inc. for general advisory services with respect to corporate finance and capital raising activities, merger and acquisition transactions, and other related endeavors. In accordance with the agreement with Pillar we issued 250,000 shares of common stock, with a value of \$175,000. The value was capitalized to prepaid expense and is being amortized over the term of the agreement. During the fiscal year ended July 31, 2014, we recognized \$85,000 of expense related to these services. We also issued 300,000 shares of registered common stock to the principal of Pillar for certain corporate reorganization services, valued at \$210,000. Pillar also received a onetime payment of \$150,000 for certain corporate reorganization activities previously provided. The fair value of the stock issued and the onetime payment was expensed to restructuring costs.

We issued 300,000 shares of common stock to Bibicoff & McInnis for investor relations services related to restructuring activities, valued at \$210,000. On issuance, the \$210,000 was expensed to restructuring costs.

We issued 250,000 shares of common stock, with a value of \$175,000, for corporate finance and restructuring activities to Wulff Services, Inc. Wulff Services, Inc. is primarily owned by our current Chief Financial Officer / Chief Operation Officer, Peter C. Wulff. In addition, Wulff Services, Inc. received a onetime payment of \$75,000 related to the corporate finance and restructuring efforts. The fair value of the stock issued and the onetime payment was expensed to restructuring costs.

We issued 300,000 shares of common stock, with a value of \$210,000, to Donna Singer, per Ms. Singer's separation agreement, pursuant to an exemption from registration provided by Section 4(a)(2) of the Securities Act. Ms. Singer was the Company's Executive Vice President and served as a member of the Board. Additionally, as part of this issuance, we granted certain registration rights with respect to the shares issued to Ms. Singer. On issuance, the \$210,000 was expensed to restructuring costs.

We issued 850,000 shares of common stock, with a value of \$595,000, to Michael L. Krall, per Mr. Krall's separation agreement, pursuant to an exemption from registration provided by Section 4(a)(2) of the Securities Act. Mr. Krall was the Company's Chief Executive Officer and served as a member of the Board. Additionally, as part of this issuance, we granted certain registration rights with respect to the shares issued to Mr. Krall. On issuance, the \$595,000 was expensed restructuring costs.

**Other Activity**

During the fiscal year ended July 31, 2014, we paid approximately \$160,000, and issued 415,643 shares of common stock, to Gary D. Cohee and/or his affiliates for investor relations and financial advisor services, valued at \$376,000,

pursuant to the terms of the director service agreement with Mr. Cohee. The amounts paid and the fair value of the stock issued were offset to additional paid-in capital. Mr. Cohee is a member of our Board.

In addition, during the fiscal year ended July 31, 2014, we issued 15,000 shares of common stock to a former employee, valued at \$20,000, and issued 20,000 shares of common stock, valued at \$25,000, based on a Settlement Agreement with a former director, for services previously provided.

On March 1, 2013, we entered into a one-year service agreement for investor relations services. We issued 250,000 shares of our common stock, with a value of \$160,000, for these services. The value was capitalized to prepaid expenses and was being amortized over the term of the agreement, however, the agreement has since been terminated and, as such, the entire amount was recognized as expense during the year ended July 31, 2013. As part of this agreement, the Company granted certain registration rights, under which the Company agreed to file a registration statement covering the resale of the shares of common stock issued in accordance with this agreement.

On May 23, 2013 we issued common stock as a settlement for past investor relations services and in exchange for services through July 31, 2013. We issued 150,000 shares of common stock, with a value of \$71,000, for these services. The entire value was expensed during the year ended July 31, 2013. As part of this agreement, the Company granted certain registration rights, under which the Company agreed to file a registration statement covering the resale of the shares of common stock issued in accordance with this agreement.

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During the fiscal year ended July 31, 2014, we issued 100,000 warrants in exchange for investor relations services, valued at \$121,000 (based on the Black-Scholes Option Pricing Model, assuming no dividend yield, volatility of 154.07% and a risk free interest rate of 0.79%). The warrants vest immediately and were expensed on issuance. The warrants were classified as equity instruments because they do not contain any anti-dilution provisions.

During the fiscal year ended July 31, 2014, we received \$337,000 from the exercise of warrants to purchase 518,000 shares of our common stock. There were no warrants exercised during the fiscal year ended July 31, 2013.

In addition, during the fiscal year ended July 31, 2014, there were net exercises on an aggregate of 122,711 warrants, which resulted in the issuance of 100,662 shares of our common stock. As these warrants were net exercised, as permitted under the respective warrant agreements, we did not receive any cash proceeds.

A summary of our warrant activity and related data is as follows:

	<b>Shares</b>
Outstanding at July 31, 2012	427,312
Issued	1,080,187
Exercised	
Expired	(73,378)
Outstanding at July 31, 2013	1,434,121
Issued	118,000
Exercised	(640,711)
Expired	(62,398)
Outstanding at July 31, 2014	849,012

The following table summarizes information related to warrants outstanding at July 31, 2014:

<b>Expiration Date</b>	<b>Exercise Price</b>	<b>Shares</b>
03/03/15	\$ 16.80	52,836
01/13/16	\$ 3.52	81,280
06/26/16	\$ 0.50	41,667
07/10/16	\$ 0.50	50,000
12/14/16	\$ 3.61	25,000
12/24/16	\$ 0.20	9,709
02/24/17	\$ 1.00	100,000
09/17/17	\$ 1.38	113,520
01/24/18	\$ 0.83	375,000
		849,012

*Restricted Stock Units*

During the fiscal year ended July 31, 2014, we issued 1,205,000 shares of common stock to employees for restricted stock units that vested, based on performance and service conditions (See Note 9)

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A summary of our restricted stock unit activity and related data is as follows:

	<b>Shares</b>
Outstanding at July 31, 2012	
Granted	
Vested	
Forfeited	
Outstanding at July 31, 2013	
Granted	6,230,000
Vested	(1,205,000)
Forfeited	(200,000)
Outstanding at July 31, 2014	4,825,000

**Stock Options**

In 2007, we adopted the PURE Bioscience 2007 Equity Incentive Plan, or the Plan, which provides for the grant of incentive and non-qualified stock options, as well as other share-based payment awards, to our employees, directors, consultants and advisors. These awards have up to a 10-year contractual life and are subject to various vesting periods, as determined by the Compensation Committee or the Board of Directors. The Plan is the only active plan pursuant to which options to acquire common stock or restricted stock awards can be granted and are currently outstanding. As of July 31, 2014, there were approximately 108,471 shares of our common stock available for issuance under the Plan.

A summary of our stock option activity and related data is as follows:

	<b>Shares</b>	<b>Weighted- Average Exercise Price</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at July 31, 2012	348,463	\$ 19.26	\$
Granted	273,000	\$ 0.83	
Exercised		\$	
Cancelled	(177,708)	\$ 15.28	
Outstanding at July 31, 2013	443,755	\$ 9.52	\$
Granted	300,000	\$ 1.40	
Exercised		\$	
Cancelled	(281,412)	\$ 10.01	
Outstanding at July 31, 2014	462,343	\$ 3.95	\$ 22,000

The weighted-average remaining contractual term of options outstanding at July 31, 2014 was approximately 4.08 years.



At July 31, 2014, 254,010 options were exercisable. These options had a weighted-average exercise price of \$6.05, an aggregate intrinsic value of \$22,000, and a weighted average remaining contractual term of approximately 5.5 years.

The weighted-average grant date fair value of equity options granted during the years ended July 31, 2014 and 2013 was \$0.76 and \$0.69, respectively.

## 9. Share-Based Compensation

### Stock Options

We recognize compensation expense for stock option awards on a straight-line basis over the applicable service period of the award. The service period is generally the vesting period, with the exception of options granted subject to a consulting agreement, whereby the option vesting period and the service period defined pursuant to the terms of the consulting agreement may be different. Stock options issued to consultants are revalued quarterly until fully vested, with any change in fair value expensed. The following weighted-average assumptions were used to calculate share based compensation for the years ended July 31, 2014 and 2013:

	<b>For the years ended July 31,</b>	
	<b>2014</b>	<b>2013</b>
Volatility	108.00%	134.80%
Risk-free interest rate	0.45%	85.00%
Dividend yield	0.0%	0.0%
Expected life	2.32 years	5.06 years

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Volatility is the measure by which our stock price is expected to fluctuate during the expected term of an option. Volatility is derived from the historical daily change in the market price of our common stock, as we believe that historical volatility is the best indicator of future volatility.

The risk-free interest rates used in the Black-Scholes calculations are based on the prevailing U.S. Treasury yield as determined by the U.S. Federal Reserve.

We have never paid dividends on our common stock and do not anticipate paying dividends on our common stock in the foreseeable future. Accordingly, we have assumed no dividend yield for purposes of estimating the fair value of our share-based compensation.

The expected life of our options is determined following the guidance of Staff Accounting Bulletin No. 107 and Staff Accounting Bulletin No. 110. We follow the simplified method to determine the expected term of options issued to employees and directors. Under the simplified method, the expected term is presumed to be the mid-point between the vesting date and the end of the contractual term. The expected term for options issued to consultants is the contractual term. We periodically evaluate our historical data as a basis for determining the expected terms of such options.

Stock-based compensation expense is based on awards ultimately expected to vest, and therefore is reduced by expected forfeitures.

Total stock option expense recognized during the fiscal year ended July 31, 2014 and 2013, was \$80,000 and \$701,000, respectively.

As of July 31, 2014, there was \$142,000 of unrecognized non-cash compensation cost related to unvested options, which will be recognized over a weighted average period of 2.38 years.

## Restricted Stock Units

During the fiscal year ended July 31, 2014, the Board of Directors authorized the issuance of 5,100,000 Restricted Stock Units ( RSUs ) to our directors and officers. Each RSU represents the right to receive one share of common stock, issuable at the time the RSU vests, as set forth in the Restricted Stock Unit Agreement. The breakdown is as follows:

**Chairman RSU Award:** We granted Mr. Pfanzelter an award consisting of two million eight hundred thousand (2,800,000) RSUs. The RSUs vest 25% on February 15, 2014, 25% on February 15, 2015 and 50% on February 15, 2016.

**Henry R. Lambert RSU Award:** We granted Mr. Lambert an award consisting of five hundred thousand (500,000) RSUs. The RSUs vest 60% on September 10, 2014 and the vesting of the remaining 40% depends on the achievement of certain quarterly sales goals over a two year period. If the sales goals are not achieved, 40% of the award will be forfeited.

**Peter C. Wulff RSU Award:** We granted Mr. Wulff an award consisting of one million (1,000,000) RSUs. The RSUs vest 25% on March 15, 2014, 25% on March 15, 2015 and 50% on March 15, 2016.

Director RSU Awards: We granted Messrs. Cohee, Culver, Otis and Dr. Theno, awards consisting of two hundred thousand (200,000) RSUs, respectively. The RSUs vest (i) 50% on the earlier of the date of the annual meeting in 2015 or January 15, 2015 and (ii) 50% on the earlier of the date of the annual meeting in 2016 or January 15, 2016.

None of the RSUs granted to our directors and officers were granted pursuant to any compensatory, bonus, or similar plan maintained or otherwise sponsored by the Company.

On April 9, 2014, Mr. Culver resigned from our board of directors. As a result, Mr. Culver's 200,000 RSU award was forfeited and \$59,000 of pre-vest expense associated with the RSU award was reversed.

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During the fiscal year ended July 31, 2014, we issued 1,130,000 RSUs to key employees. The RSUs vest based on performance and service conditions. If the performance conditions are not met or expected to be met, no compensation cost will be recognized on the underlying RSUs. In addition, if the performance conditions are not achieved, then the corresponding RSUs will be forfeited.

During the fiscal year ended July 31, 2014, 1,205,000 restricted stock units vested, based on performance and service conditions, which were satisfied during the year. Of the RSUs awarded during the fiscal year ended July 31, 2014 that remain outstanding as of year end, we currently expect 3,765,000 to vest.

Total expense recognized for RSUs granted during the fiscal year ended July 31, 2014 was \$2,878,000. No RSUs were outstanding during the prior year; however, we did recognize \$19,000 of expense related to restricted stock. As of July 31, 2014, there was \$4,059,000 of unrecognized non-cash compensation cost related to the RSUs, which will be recognized over a weighted average period of 1.47 years

## **10. Related Party Transactions**

The following related party transactions occurred during our fiscal year ended July 31, 2014:

We issued 250,000 shares of common stock, with a value of \$175,000, for corporate finance and restructuring activities to Wulff Services, Inc. Wulff Services, Inc. is primarily owned by our current Chief Financial Officer / Chief Operation Officer, Peter C. Wulff. In addition, Wulff Services, Inc. received a onetime payment of \$75,000 related to the corporate finance and restructuring efforts.

We paid approximately \$160,000, and issued 415,643 shares of common stock, to Gary D. Cohee and/or his affiliates for investor relations and financial advisor services, valued at \$376,000, pursuant to the terms of the director service agreement with Mr. Cohee. Mr. Cohee is a member of our Board.

On December 11, 2013, the Company entered into a five-year strategic collaboration agreement with St. Louis-based Intercon Chemical Company (ICC). The agreement consists of a multi-prong approach to accelerate the commercialization of PURE's unique and proprietary SDC-based products. The strategic collaboration agreement provides:

ICC licenses from PURE its patents and technology know-how for the exclusive manufacture of our SDC-based products.

ICC will invest in plant improvements to allow for expanded SDC production.

ICC's R&D team will collaborate on SDC product line development.

ICC licenses the distribution rights for SDC-based products into its core businesses of institutional cleaning and sanitation products.

ICC will also develop a new initiative focused on US hospital, healthcare and medical facilities.

PURE earns royalty income on SDC-products sold by ICC and its affiliates.

The agreement may be terminated by mutual written consent, or by either party upon the material breach of the terms of the agreement by the other party.

During the year ended July 31, 2014, we entered into an asset purchase agreement with ICC. Based on the terms of the agreement we received approximately \$58,000 for our manufacturing assets. The assets were sold at book value. As a result, no gain was recorded. ICC is a current customer of the Company and the president of ICC is a shareholder of the Company.

### **11. Sales Concentration**

Net product sales were \$550,000 and \$820,000 for the years ended July 31, 2014 and 2013, respectively. For the year ended July 31, 2014, two customers accounted for 66% of our net product sales. No other individual customer accounted for 10% or more of our net product sales. The geographic breakdown of net product sales was as follows: 100% U.S. For the year ended July 31, 2013, three customers accounted for 69% of our net product sales. No other individual customer accounted for 10% or more of our net product sales. The geographic breakdown of net product sales was as follows: 86% U.S. and 14% foreign.

**Table of Contents****12. Income Taxes**

We file federal and California consolidated tax returns with our subsidiaries. Our income tax provision for the year ended July 31, 2014 and 2013 was \$1,600; the minimum state franchise taxes we pay regardless of income or loss.

At July 31, 2014, we had federal and California tax net operating loss carry-forwards of approximately \$83.6 million and \$71.8 million, respectively. Included in these net operating loss carry-forwards is \$17.3 million related to a deduction for income tax purposes for which the Company has not realized a tax benefit. In future periods an adjustment would be recorded to Additional Paid in Capital at the time that these net operating losses may be utilized and reduce income tax. At July 31, 2013, we had federal and California tax net operating loss carry-forwards of approximately \$75.2 million and \$64.9 million, respectively. Utilization of the net operating loss carry-forwards may be subject to a substantial annual limitation due to ownership change limitations that may have occurred or that could occur in the future, as required by Section 382 of the Internal Revenue Code as well as similar state provisions. These ownership changes may limit the amount of net operating loss carry-forwards that can be utilized annually to offset future taxable income and tax, respectively. In general, an ownership change, as defined by Section 382 of the Internal Revenue Code results from a transaction or series of transactions over a three-year period resulting in an ownership change of more than 50 percentage points of the outstanding stock of a company by certain stockholders or public groups. Since our formation, we have raised capital through the issuance of capital stock on several occasions (both before and after our initial public offering in 1996) which, combined with the purchasing stockholders' subsequent disposition of those shares, may have resulted in such an ownership change, or could result in an ownership change in the future upon subsequent disposition. While we do not believe that we have experienced an ownership change, the pertinent tax rules related thereto are complex and subject to varying interpretations, and thus complete assurance cannot be provided that the taxing authorities would not take an alternative position.

Our current federal tax loss carry-forwards begin expiring in the year ended July 31, 2019 and, unless previously utilized, will completely expire in the year ending July 31, 2034. Our California tax loss carry-forwards will begin to expire in the year ending July 31, 2015, and will completely expire in the year ending July 31, 2034.

Significant components of our deferred tax assets are as follows:

	<b>July 31,</b>	
	<b>2014</b>	<b>2013</b>
Net operating loss carry-forward	\$ 25,740,000	\$ 22,482,000
Stock options and warrants	1,720,000	1,915,000
Other temporary differences	310,000	252,000
Total deferred tax assets	27,770,000	24,649,000
Valuation allowance for deferred tax assets	(27,770,000)	(24,649,000)
Net deferred tax assets	\$	\$

Realization of our deferred tax assets, which relate to operating loss carry-forwards and timing differences, is dependent on future earnings, among other factors. The timing and amount of future earnings are uncertain and therefore a valuation allowance has been established. The increase in the valuation allowance on the deferred tax asset during the year ended July 31, 2014 was \$3,121,000.

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A reconciliation of income taxes computed using the statutory income tax rate, compared to the effective tax rate, is as follows:

	<b>2014</b>	<b>2013</b>
Federal tax benefit at the expected statutory rate	34.0%	34.0%
State income tax, net of federal tax benefit	3.4	5.8
Expired net operating loss carryforwards	(0.8)	(9.7)
Other	(8.4)	(2.9)
Valuation allowance	(28.2)	(27.2)
Income tax benefit - effective rate	0.0%	0.0%

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Following authoritative guidance, we recognize the tax benefit from a tax position if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position.

Our practice is to recognize interest and/or penalties related to income tax matters in income tax expense; however we have had no accrued interest or penalties at either July 31, 2014 or July 31, 2013. We are subject to income taxes in the United States and in California, and our historical tax years remain subject to future examination by the U.S. and California tax authorities. During the year ended July 31, 2014, we did not record any activity related to our unrecognized tax benefits.

The Company and its subsidiaries are subject to federal income tax as well as income tax of multiple state jurisdictions. With few exceptions, the Company is no longer subject to income tax examination by tax authorities in major jurisdictions for years prior to 2008. However, to the extent allowed by law, the taxing authorities may have the right to examine prior periods where net operating losses were generated and carried forward, and make adjustments up to the amount of the carryforwards. The Company is not currently under examination by the IRS or state taxing authorities.

### **13. Subsequent Events**

During the period from July 31, 2014 until present, we issued a total of 9,990,659 shares of common stock and warrants to purchase 3,996,259 shares of common stock for gross proceeds of approximately \$7.49 million. Additionally, in connection with the price adjustment terms in subscription agreements we previously entered into with investors in prior private placements prior to July 31, 2014, we issued an aggregate of 95,366 shares of common stock and warrants to purchase up to an aggregate of 648,053 shares of common stock to existing investors who purchased shares from the Company in private placement transactions. The shares of common stock and the warrants issued under the private placements were offered and sold without registration under the Securities Act, or state securities laws, in reliance on the exemptions provided by Section 4(a)(2) of the Securities Act and Regulation D promulgated thereunder and in reliance on similar exemptions under applicable state laws, based on the lack of any general solicitation or advertising in connection with the sale of the securities; the representation of each investor to the Company that it is an accredited investor (as that term is defined in Rule 501 of Regulation D) and that it was purchasing the securities for its own account and without a view to distribute them. The securities, including the shares underlying the warrants, may not be offered or sold in the United States without an effective registration statement or pursuant to an exemption from applicable registration requirements.

Tom Y. Lee, CPA was appointed to our Board on October 24, 2014. Mr. Lee is currently the Chairman and CEO of Unidose Systems, Inc., a contract manufacturer of single-dose applicator and formulation OEM products, and has served as Chairman and CEO since 2008. Mr. Lee is a former board member and audit committee chairman at First Continental Bank (which merged with United Commercial Bank in 2003). Mr. Lee has been an active CPA since 1983 and earned his Master of Science in accounting from California State University Long Beach and his Bachelors in Business Administration from TamKang University in Taipei, Taiwan.