

BIOLARGO, INC.
Form 10-Q
May 14, 2018

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2018.

or

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

For the transition period from _____ to _____

Commission File Number 000-19709

Edgar Filing: BIOLARGO, INC. - Form 10-Q

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

Large accelerated filer Accelerated filer Emerging growth company
Non-accelerated filer Smaller reporting company

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

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

The number of shares of the Registrant’s Common Stock outstanding as of May 12, 2018 was 122,154,066 shares.

Table of Contents

BIOLARGO, INC.

FORM 10-Q

INDEX

PART I

Item 1 <u>Financial Statements</u>	1
Item 2 <u>Management's Discussion and Analysis and Financial Condition and Results of Operations</u>	24
Item 4 <u>Controls and Procedures</u>	32

PART II

Item 2 <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	34
Item 5 <u>Other Information</u>	36
Item 6 <u>Exhibits</u>	37
<u>Signatures</u>	37
<u>Exhibit Index</u>	38

i.

Table of Contents**PART I – FINANCIAL INFORMATION****Item 1. Financial Statements****BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS****AS OF DECEMBER 31, 2017 AND MARCH 31, 2018**

	DECEMBER 31, 2017	MARCH 31, 2018 (Unaudited)
Assets		
Current assets:		
Cash and cash equivalents	\$990,457	\$921,942
Accounts receivable, net of allowance of \$2,500	94,413	102,310
Inventories	53,973	56,805
Prepaid expenses and other current assets	20,000	32,745
Total current assets	1,158,843	1,113,802
Leasehold improvement and equipment, net of depreciation	108,865	117,295
Other non-current assets	32,530	32,530
Deferred offering cost	195,182	191,494
Total assets	\$1,495,420	\$1,455,121
Liabilities and stockholders' deficit		
Current liabilities:		
Accounts payable and accrued expenses	\$224,105	\$351,000
Convertible notes payable	5,248,847	5,398,847
Discount on convertible notes payable, net of amortization	(1,257,182)	(697,231)
Total current liabilities	4,215,770	5,052,616
Long-term liabilities:		
Line of credit	—	390,000
Convertible notes payable	1,539,271	1,769,271
Discount on convertible notes payable and line of credit, net of amortization	(850,000)	(1,141,478)
Total liabilities	4,905,041	6,070,409

COMMITMENTS, CONTINGENCIES (Note 11)

STOCKHOLDERS' EQUITY (DEFICIT):

Convertible Preferred Series A, \$.00067 Par Value, 50,000,000 Shares Authorized, -no Shares Issued and Outstanding, at December 31, 2017 and March 31, 2018	—	—
Common stock, \$.00067 Par Value, 200,000,000 Shares Authorized, 104,164,465 and 106,406,584 Shares Issued, at December 31, 2017 and March 31, 2018	69,871	71,421
Additional paid-in capital	97,093,144	98,605,285
Accumulated deficit	(101,204,846)	(103,825,209)
Accumulated other comprehensive loss	(62,489)	(54,840)
Total Biolargo, Inc. and Subsidiaries stockholders' equity (deficit)	(4,104,320)	(5,203,343)
Non-controlling interest (Note 9)	694,699	588,055
Total stockholders' equity (deficit)	(3,409,621)	(4,615,288)
Total liabilities and stockholders' equity (deficit)	\$1,495,420	\$1,455,121

See accompanying notes to unaudited consolidated financial statements.

Table of Contents**BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****AND COMPREHENSIVE LOSS****FOR THE THREE MONTHS ENDED MARCH 31, 2017 AND 2018****(UNAUDITED)**

	MARCH	MARCH
	31, 2017	31, 2018
Revenue		
Product revenue	\$46,017	\$224,397
Service revenue	—	38,632
Total revenue	46,017	263,029
Cost of revenue		
Cost of goods sold	(22,530)	(134,464)
Cost of service	—	(28,728)
Gross profit	23,487	99,837
Selling, general and administrative expenses	1,055,055	1,169,613
Research and development	391,336	521,730
Depreciation and amortization	7,924	10,323
Operating loss	(1,430,828)	(1,601,829)
Other (expense) income		
Grant income	58,788	4,669
Interest expense	(953,636)	(832,408)
Total other (expense) income	(894,848)	(827,739)
Net loss	(2,325,676)	(2,429,568)
Net loss attributable to noncontrolling interest	(63,256)	(106,644)
Net loss attributable to common shareholders	\$(2,262,420)	\$(2,322,924)
Net loss per share attributable to common stockholders:		
Loss per share attributable to shareholders – basic and diluted	\$(0.02)	\$(0.02)
Weighted average number of common shares outstanding:	94,444,945	104,695,818
Comprehensive loss attributable to common shareholders		

Edgar Filing: BIOLARGO, INC. - Form 10-Q

Net loss	\$(2,325,676)	\$(2,429,568)
Foreign translation adjustment	(11,376)	7,649
Comprehensive loss	(2,337,052)	(2,421,919)
Comprehensive loss attributable to noncontrolling interest	(63,256)	(106,644)
Comprehensive loss attributable to shareholders	\$(2,273,796)	\$(2,315,275)

See accompanying notes to unaudited consolidated financial statements.

Table of Contents**BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENT OF STOCKHOLDERS' DEFICIT
FOR THE THREE MONTHS ENDED MARCH 31, 2018**

(UNAUDITED)

	Common stock		Additional	Accumulated	Accumulated	Non-	Total
	Shares	Amount	paid-in capital	deficit	other comprehensive loss	controlling interest	
Balance, December 31, 2017	104,164,465	\$ 69,871	\$ 97,093,144	\$(101,204,846)	\$ (62,489)	\$ 694,699	\$(3,409,621)
Issuance of common stock for service	714,436	482	195,569	—	—	—	196,051
Issuance of common stock for interest	617,072	458	164,609	—	—	—	165,067
Financing fee in stock	252,385	168	84,905	—	—	—	85,073
Sale of stock for cash	658,226	442	167,778	—	—	—	168,220
Stock option compensation expense	—	—	320,090	—	—	—	320,090
Warrants and conversion feature issued as discount on convertible notes payable, note payable and line of credit	—	—	281,571	—	—	—	281,751
Deemed dividend	—	—	297,439	(297,439)	—	—	—
Net loss	—	—	—	(2,322,924)	—	(106,644)	(2,429,568)
Foreign currency translation	—	—	—	—	7,649	—	7,649
Balance, March 31, 2018	106,406,584	\$ 71,421	\$ 98,605,285	\$(103,825,209)	\$ (54,840)	\$ 588,055	\$(4,615,288)

See accompanying notes to unaudited consolidated financial statements.

3

Table of Contents**BIOLARGO, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE THREE MONTHS ENDED MARCH 31, 2017 AND 2018****(UNAUDITED)**

	March	March
	31, 2017	31, 2018
Cash flows from operating activities		
Net loss	\$(2,325,676)	\$(2,429,568)
Adjustments to reconcile net loss to net cash used in operating activities:		
Stock option compensation expense	280,288	320,090
Common stock issued for interest and fees for services from consultants	261,409	361,118
Interest expense related to amortization of the discount on convertible notes payable	771,124	635,297
Deferred offering cost expense	—	3,688
Bad debt expense	15,000	—
Depreciation and amortization expense	7,924	10,323
Changes in assets and liabilities:		
Accounts receivable	(9,442)	(7,897)
Inventories	9,818	(2,832)
Prepaid expenses and other current assets	(143,293)	(12,745)
Accounts payable and accrued expenses	36,596	126,895
Officer bonus	(80,000)	—
Net cash used in operating activities	(1,176,252)	(995,631)
Cash flows from investing activities		
Leasehold improvements	—	(18,753)
Net cash used in investing activities	—	(18,753)
Cash flows from financing activities		
Proceeds from line of credit	175,000	390,000
Proceeds from convertible notes	125,000	380,000
Proceeds from sale of stock to Lincoln Park Capital	—	168,220
Proceeds from exercise of warrants	153,000	—
Net cash provided by financing activities	453,000	938,220
Effect of foreign currency translation	(11,376)	7,649
Net change in cash and cash equivalents	\$(734,628)	\$(68,515)
Cash and cash equivalents at beginning of period	\$1,910,153	\$990,457
Cash and cash equivalents at end of period	\$1,175,525	\$921,942
Supplemental disclosures of cash flow information		

Edgar Filing: BIOLARGO, INC. - Form 10-Q

Cash paid during the period for:		
Interest	\$—	\$—
Income taxes	\$5,350	\$—
Non-cash investing and financing activities:		
Conversion of accounts payable and salary into stock options	\$141,763	\$—
Fair value of common stock issued for cash for stock financing offering	\$—	\$85,073
Fair value of warrants issued in conjunction with convertible notes payable	\$125,000	\$281,751
Settlement of accounts payable and interest in shares of common stock	\$261,409	\$—
Deemed dividend	\$—	\$297,439
Convertible notes into shares of common stock	\$400,000	\$—

See accompanying notes to unaudited consolidated financial statements

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Note 1. Business and Liquidity

Description of Business

We are an innovation company driven by our mission to “make life better” by developing breakthrough platform technologies, nurturing and building businesses around the intellectual property, while providing capital and support along the journey from “cradle” to “maturity”. We have two divisions generating operational revenue – Odor-No-More, selling odor control products, and BioLargo Engineering, Science & Technologies, LLC (“BLEST”), providing professional engineering services to third party clients as well as working on our product development projects. We have a research and development facility in Canada, and consolidate our financials with our partially owned subsidiary, Clyra Medical Technologies, Inc., a company focused on commercializing our technologies in the medical field (see Note 9).

Liquidity / Going Concern

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. As reflected in the accompanying consolidated financial statements, for the three months ended March 31, 2018 we had a net loss of \$2,429,568, and used \$995,631 cash in operations, and at March 31, 2018, had negative working capital of \$3,938,814, current assets of \$1,113,802, and an accumulated stockholders’ deficit of \$103,825,209. The foregoing factors raise substantial doubt about our ability to continue as a going concern. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies and achieve profitable operations by licensing or otherwise commercializing products incorporating our technologies. The consolidated financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Our total cash balance was \$921,942 at March 31, 2018. We had revenues of \$263,029 in the three months ended March 31, 2018, which amount was not sufficient to fund our operations. Although our revenue increased, it was *not* sufficient to fund

our operations. We believe our cash position is insufficient to maintain our current level of operations and research/development, and that we will be required to raise substantial additional capital to expand our operations and fund our future business plans. We intend to continue to raise money through private securities offerings for the foreseeable future, and through our agreement with Lincoln Park (see Note 4).

At times in the past we have not had enough cash or sources of capital to pay our accounts payable and expenses as they arise, and have relied on the issuance of stock options and common stock, as well as extended payment terms with our vendors, to continue to operate. We will be required to raise substantial additional capital to expand our operations, including without limitation, hiring additional personnel, additional scientific and third-party testing, costs associated with obtaining regulatory approvals and filing additional patent applications to protect our intellectual property, and possible strategic acquisitions or alliances, as well as to meet our liabilities as they become due for the next 12 months.

The unaudited consolidated financial statements of the Company have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and pursuant to Rule 8-03 of Regulation S-X under the Securities Act of 1933, as amended. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. For some of our activities, we are still operating in the early stages of the sales and distribution process, and therefore our operating results for the three months ended March 31, 2018 are not necessarily indicative of the results that may be expected for the year ending December 31, 2018, or for any other period. These unaudited consolidated financial statements and notes should be read in conjunction with the Company's audited consolidated financial statements and accompanying notes included in the Annual Report on Form 10-K for the year ended December 31, 2017 filed with the Securities and Exchange Commission (the "SEC") on March 14, 2018.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Note 2. Summary of Significant Accounting Policies

In the opinion of management, the accompanying balance sheet and related statements of operations, cashflows, and stockholders' deficit include all adjustments, consisting only of normal recurring items, necessary for their fair presentation in conformity with accounting principles generally accepted in the United States of America.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company, its majority owned subsidiaries, and Clyra. Management believes Clyra's financial statements are appropriately consolidated with that of the Company after reviewing the guidance of ASC Topic 810, "Consolidation" and because the Company is Clyra's largest shareholder, owning 46.3% of its outstanding voting stock at March 31, 2018, and two members of BioLargo's board of directors are two of three members of Clyra's board of directors (see Note 9). All intercompany accounts and transactions have been eliminated.

Foreign Currency

The Company has designated the functional currency of BioLargo Water, Inc., our Canadian subsidiary, to be the Canadian dollar. Therefore, translation gains and losses resulting from differences in exchange rates are recorded in accumulated other comprehensive income.

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturities of three months or less when acquired to be cash equivalents. Substantially all cash equivalents are held in short-term money market accounts at one of the largest

financial institutions in the United States. From time to time, our cash account balances are greater than the Federal Deposit Insurance Corporation insurance limit of \$250,000 per owner per bank, and during such times, we are exposed to credit loss for amounts in excess of insured limits in the event of non-performance by the financial institution. We do not anticipate non-performance by our financial institution.

Our cash balances were made up of the following:

	DECEMBER	March
	31, 2017	31, 2018
BioLargo, Inc. and wholly owned subsidiaries	\$ 461,914	\$574,106
Clyra Medical Technologies, Inc.	528,543	347,836
Total	\$ 990,457	\$921,942

Accounts Receivable

Trade accounts receivable are recorded net of allowances for doubtful accounts. Estimates for allowances for doubtful accounts are determined based on payment history and individual customer circumstances. The allowance for doubtful accounts as of December 31, 2017 and March 31, 2018 was \$2,500, respectively.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Credit Concentration

The Company had three customers during the three months ended March 31, 2017 and 2018 that each accounted for more than 10% of consolidated revenues in the respective periods as follows:

	March		March	
	31,		31,	
	2017		2018	
Customer A	28	%	39	%
Customer B	17	%	<10	%
Customer C	12	%	<10	%
Customer D	<10	%	18	%
Customer E	<10	%	18	%

The Company had five customers that accounted for more than 10% of consolidated accounts receivable at December 31, 2017 and three customers at March 31, 2018 as follows:

	December		March	
	31, 2017		31,	
			2018	
Customer A	12	%	23	%
Customer B	19	%	<10	%
Customer C	12	%	<10	%
Customer D	10	%	<10	%
Customer E	10	%	<10	%
Customer F	<10	%	13	%
Customer G	<10	%	11	%

Inventory

Inventories are stated at the lower of cost or net realizable value using the average cost method. Inventories consisted of:

	DECEMBER	MARCH
	31, 2017	31, 2018
Raw material	\$ 34,104	\$ 48,211
Finished goods	19,869	8,594
Total	\$ 53,973	\$ 56,805

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and revenues and expenses during the period reported. Actual results could differ from those estimates. Estimates are used when accounting for stock-based transactions, debt transactions, deemed dividends, allowance for bad debt, asset depreciation and amortization, among others.

The methods, estimates and judgments we use in applying these most critical accounting policies have a significant impact on the results of our consolidated financial statements.

Share-based Payments

For stock and stock options issued to consultants and other non-employees for services, the Company measures and records an expense as of the earlier of the date at which either: a commitment for performance by the non-employee has been reached or the non-employee's performance is complete. The equity instruments are measured at the current fair value, and for stock options, the instruments are measured at fair value using the Black Scholes options model.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

For equity instruments issued and outstanding where performance is not complete, but the instrument has been recorded, those instruments are measured again at their then current fair market values at each of the reporting dates (they are “marked-to market”) until the performance and the contract are complete.

Warrants

The Unit Offerings of our convertible promissory note and a Series A stock purchase warrant are accounted for under the fair value and relative fair value method.

The warrant is first analyzed per its terms as to whether it has derivative features or not. If the warrant is determined to be a derivative, then it is measured at fair value using the Black Scholes Option Model, and recorded as a liability on the balance sheet. The warrant is re-measured at its then current fair value at each subsequent reporting date (it is “marked-to-market”).

If the warrant is determined to not have derivative features, it is recorded into equity at its fair value using the Black Scholes option model, however, limited to a relative fair value based upon the percentage of its fair value to the total fair value including the fair value of the convertible note.

The convertible note is recorded at its fair value, limited to a relative fair value based upon the percentage of its fair value to the total fair value including the fair value of the warrant. Further, the convertible promissory note is examined for any intrinsic beneficial conversion feature (“BCF”) of which the convertible price of the note is less than the closing stock price on date of issuance. If the relative fair value method is used to value the convertible promissory note and there is an intrinsic BCF, a further analysis is undertaken of the BCF using an effective conversion price which assumes the conversion price is the relative fair value divided by the number of shares the convertible debt is converted into by its terms. The adjusted BCF value is accounted for as equity.

The warrant and BCF relative fair values are also recorded as a discount to the convertible promissory notes. As present, these equity features of the convertible promissory notes have recorded a discount to the convertible notes

that is substantially equal to the proceeds received.

Non-Cash Transactions

We have established a policy relative to the methodology to determine the value assigned to each intangible we acquire, and/or services or products received for non-cash consideration of our common stock. The value is based on the market price of our common stock issued as consideration, at the date of the agreement of each transaction or when the service is rendered or product is received.

Revenue Recognition

We adopted ASU 2014-09, "Revenue from Contracts with Customers", Topic 606, as of December 15, 2017 and applied for the fiscal year starting January 1, 2018. The guidance focuses on the core principle for revenue recognition.

The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps:

Step 1: Identify the contract(s) with a customer.

Step 2: Identify the performance obligations in the contract.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Step 3: Determine the transaction price.

Step 4: Allocate the transaction price to the performance obligations in the contract.

Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

We have revenue from two subsidiaries, Odor-No-More and BLEST. Odor-No-More identifies its contract with the customer through a purchase order whether in writing or verbal, in which the details of the contract are defined including the transaction price and method of shipment. The only performance obligation is to create and ship the product and each product has separate pricing. Odor-No-More recognizes revenue when the order for its goods are shipped, wither FOB warehouse of FOB destination, depending on the customer's choice of title transfer. Revenue is recognized with a reduction for sales discounts, as appropriate and negotiated in the customer's purchase order.

BLEST, identifies services to be performed in a written contract, which specifies the performance obligations and the rate at which the services will be billed. Each service is separately negotiated and priced. Revenue is recognized when services are performed and completed. BLEST bills time and materials for the services it provides. To date, there have been no discounts or other financing terms for the contracts.

We also may generate revenues from royalties and license fees from our intellectual property. In the event we do so, we anticipate a licensee would pay a license fee in one or more installments and ongoing royalties based on their sales of products incorporating or using our licensed intellectual property. Upon entering into a licensing agreement, we will determine the appropriate method of recognizing the royalty and license fees.

Government Grants

We have been awarded multiple research grants from the Canadian National Research Institute – Industrial Research Assistance Program (NRC-IRAP) and the National Science and Engineering Research Council of Canada (NSERC). The grants received are considered other income and are included in our consolidated statements of operations. We received our first grant in 2015 and have been awarded over 50 grants totaling approximately \$1,600,000. Some of the funds from these grants are given directly to third parties (such as the University of Alberta or a third-party research scientist) to support research on our technology. The grants have terms generally ranging between six and eighteen months and support a majority, but not all, of the related research budget costs. This cooperative research allows us to utilize (i) a depth of resources and talent to accomplish highly skilled work, (ii) financial aid to support research and development costs, (iii) independent and credible validation of our technical claims.

The grants typically provide for (i) recurring monthly amounts, (ii) reimbursement of costs for research talent for which we invoice to request payment, and (iii) ancillary cost reimbursement for research talent travel related costs. All awarded grants have specific requirements on how the money is spent, typically to employ researchers. None of the funds may be used for general administrative expenses or overhead in the United States. These grants have substantially increased our level of research and development activities in Canada. We continue to apply for Canadian government and agency grants to fund research and development activities. Not all of our grant applications have been awarded, and no assurance can be made that any pending grant application, or any future grant applications, will be awarded.

Business Segment Information

In 2017, the Company operated with three business segments - Odor-No-More, Clyra, and BioLargo/other. In 2018, the Company determined that it operates a fourth business segment – BLEST, based on the manner in which the chief operating decision maker now manages the engineering division, including resource allocation and performance assessment.

Odor-No-More is engaged in developing and selling products using the BioLargo technology. Clyra is engaged in developing medical products using the BioLargo technology, with an emphasis in advanced wound care. BLEST is engaged in providing professional engineering services. BioLargo/Other includes certain functional roles that do not engage in revenue generating activities, such as corporate operations and oversight, research and development, and general corporate and administrative functions, including finance, human resources, marketing and legal.

The segment information for the three months ended March 31, 2018, is as follows:

	Odor-No-		BioLargo /		Total
	More	Clyra	BLEST	Other	
Revenues	\$ 224,397	\$—	\$ 38,632	\$—	\$ 263,029
Cost of goods/services	(134,464)	—	(28,728)	—	(163,192)

Edgar Filing: BIOLARGO, INC. - Form 10-Q

Depreciation and amortization	4,093	—	6,230	—	10,323
Interest expense	—	—	—	832,408	832,408
Expenditures for assets	—	—	18,753	—	18,753
Equipment, net of depreciation	42,299	—	74,996	—	117,295
Net loss	(200,000)	(198,721)	(46,387)	(1,984,460)	(2,429,568)
Tangible assets, net	293,997	347,836	140,722	448,542	1,231,097

9

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The segment information for the three months ended March 31, 2017, is as follows (BLEST was not formed or operational during the three months ended March 31, 2017, and is thus not reflected in this table):

	Odor-No-		BioLargo /	Total
	More	Clyra	Other	
Revenues	\$46,017	\$—	\$—	\$46,017
Cost of goods/services	(22,530)	—	—	(22,530)
Depreciation and amortization	7,924	—	—	7,924
Interest expense	—	8,750	944,886	953,636
Expenditures for assets	—	—	—	—
Equipment, net of depreciation	54,121	—	—	54,121
Net loss	(175,000)	(137,082)	(2,013,594)	(2,325,676)
Tangible assets, net	180,292	268,771	1,015,039	1,464,092

Earnings (Loss) Per Share

We report basic and diluted earnings (loss) per share (“EPS”) for common and common share equivalents. Basic EPS is computed by dividing reported earnings by the weighted average shares outstanding. Diluted EPS is computed by adding to the weighted average shares the dilutive effect if stock options and warrants were exercised into common stock. For the three months ended March 31, 2017 and 2018, the denominator in the diluted EPS computation is the same as the denominator for basic EPS due to the anti-dilutive effect of the warrants and stock options on the Company’s net loss.

Recent Accounting Pronouncements

In May 2017, the FASB issued ASU 2017-09, “Compensation – Stock Compensation (topic 718)”. The amendments in this Update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. An entity should account for the effects of a modification unless all the following are met: (i) the fair value (or calculated value or intrinsic value, if such an alternative measurement method is used) of the modified award is the same as the fair value (or calculated value or intrinsic

value, if such an alternative measurement method is used) of the original award immediately before the original award is modified, (ii) The vesting conditions of the modified award are the same as the vesting conditions of the original award immediately before the original award is modified and (iii) the classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. The amendments in this Update are effective for all entities for annual periods, and interim periods within those annual periods, beginning after December 15, 2017. Management has analyzed the new guideline and it has not substantially impacted our accounting for stock compensation awards upon adoption in the current period.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

In March 2016, the FASB issued Accounting Standards Update (ASU) No. 2016-09, “Improvements to Employee Share-Based Payment Accounting,” which simplifies several aspects of the accounting for share-based award transactions and adds two practical expedients for nonpublic entities. The new standards are effective for annual periods beginning after December 15, 2017. An entity that elects early adoption must adopt all the amendments in the same period. Management has analyzed the new guideline and it has not substantially impacted our consolidated financial statements upon adoption during the current period.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02, “Leases”. The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The new guidelines will create a ROU asset and lease liability for the Company’s lease agreements in place at the time the standard goes into effect. Currently, the Company has two real property leases with terms longer than 12 months.

Note 3. Change in Derivative Liability Treatment

BioLargo adopted ASU 2017-11 as of July 1, 2017. With this adoption, we eliminated the derivative liability, and the changes in the fair value of the derivative liability, related to negative covenants in multiple warrants issued that required a reduction of warrant exercise price under certain circumstances. The Company made a cumulative effect adjustment to the consolidated balance sheet as of January 1, 2017, which adjusted the beginning balance in the accumulated deficit account by \$663,560.

Note 4. Lincoln Park Financing

On August 25, 2017, we entered into a stock purchase agreement (“LPC Purchase Agreement”) with Lincoln Park Capital Fund, LLC (“Lincoln Park”), pursuant to which Lincoln Park agreed to purchase from us at our request up to an aggregate of \$10,000,000 of our common stock (subject to certain limitations) from time to time over a period of three years. Concurrently, we entered into a registration rights agreement with Lincoln Park (“LPC RRA”), pursuant to which we were required to file with the Securities and Exchange Commission (“SEC”) a registration statement on Form S-1 to register for resale under the Securities Act of 1933, as amended, the shares of common stock that have been or may be issued to Lincoln Park under the LPC Purchase Agreement. The registration statement was filed, and on September 22, 2017, it was deemed effective by the SEC. The LPC Purchase Agreement allows us, from time to time and at our sole discretion, to direct Lincoln Park to purchase shares of our common stock, subject to limitations in both volume and dollar amount. The volume of shares is limited to a maximum of 50,000 shares if our stock closes at less than \$0.50 per share, 75,000 if it closes from \$0.50 to \$0.74 per share, 100,000 if it closes from \$0.75 to \$1.24 per share, and 200,000 if it closes at or above \$1.25 per share. The maximum dollar amount for any single purchase is \$500,000. There are no trading volume requirements under the LPC Purchase Agreement, and we alone control the timing and amount of any sales of our common stock to Lincoln Park. The purchase price of the shares that may be sold to Lincoln Park under the Purchase Agreement is the lower of (i) the lowest sale price on the date of purchase, or (ii) the average of the three lowest closing prices in the prior 12 business days. The purchase price per share will be equitably adjusted for any reorganization, recapitalization, non-cash dividend, stock split, or other similar transaction occurring during the business days used to compute such price. We may at any time in our sole discretion terminate the LPC Purchase Agreement without fee, penalty or cost upon one business day notice. There are no restrictions on future financings, rights of first refusal, participation rights, penalties or liquidated damages in the LPC Purchase Agreement or LPC RRA other than a prohibition on entering into a “Variable Rate Transaction,” as defined in the Purchase Agreement. Lincoln Park may not assign or transfer its rights and obligations under the Purchase Agreement.

In consideration for entering into the LPC Purchase Agreement, on August 25, 2017, we issued to Lincoln Park 488,998 shares of common stock as an “initial commitment fee.” For no additional consideration, when and if Lincoln Park purchases (at the Company’s discretion) any portion of the \$10,000,000 aggregate commitment, we are required to issue up to 488,998 shares, pro-rata, as “additional commitment shares”. For example, if we elect, at our sole discretion, to require Lincoln Park to purchase \$25,000 of our stock, then we would issue 1,222 additional commitment shares, which is the product of \$25,000 (the amount we have elected to sell) divided by \$10,000,000 (total amount we can sell Lincoln Park pursuant to the LPC Purchase Agreement) multiplied by 488,998 (the total number of additional commitment shares). The additional commitment shares will only be issued pursuant to this formula as and when we elect at our discretion to sell stock to Lincoln Park.

From inception of the contract in August 2017 through March 31, 2018, we elected to sell Lincoln Park shares of our common stock for which we received \$679,305, and issued Lincoln Park 1,825,000 shares, and 33,217 “additional commitment shares”. We recorded the stock sale in our equity statement and the additional shares issued as a fee for the transaction was offset against the shares issued.

During the three-months ended March 31, 2018, we elected to sell to Lincoln Park 650,000 shares of our common stock for which we received \$168,220. Additionally, we issued Lincoln Park 8,226 “additional commitment” shares.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Note 5. Debt Obligations

The following table summarizes our debt obligations outstanding as of December 31, 2017 and March 31, 2018.

	December	March
	31, 2017	31, 2018
Current liabilities		
Convertible notes payable		
One-year convertible notes, mature July 18, 2018	\$280,000	\$280,000
Convertible notes, mature June 1, 2018	4,468,847	4,468,847
Nine-month convertible note, matures September 18, 2018	500,000	500,000
Nine-month convertible note, matures October 16, 2018	—	150,000
Total convertible notes payable	\$5,248,847	\$5,398,847
Long-term liabilities:		
Line of credit, matures September 1, 2019	\$—	\$390,000
Convertible notes payable		
Convertible note, matures July 20, 2019	440,000	440,000
Convertible notes, mature June 17, 2019	283,571	283,571
Convertible notes, mature December 31, 2019	292,000	292,000
Convertible note, matures March 8, 2020	—	50,000
Convertible notes, mature June 20, 2020	523,700	603,700
Convertible notes, mature April 20, 2021	—	100,000
Total convertible notes payable	\$1,539,271	\$1,769,271
Total	\$6,788,118	\$7,558,118

For the three months ended March 31, 2017 and 2018, we recorded \$953,636 and \$832,408 of interest expense related to the amortization of our discount on our convertible notes payable, line of credit, and interest from our convertible notes and line of credit.

Subsequent to March 31, 2018, holders of notes representing \$4,133,738 in the above table agreed to convert their notes prior to maturity (see Note 12).

See our Annual Report on Form 10-K for the year ended December 31, 2017, for a complete description of the debt obligations set forth in the above table. The following describes changes to the debt obligations for the three months ended March 31, 2018.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

FirstFire Global Opportunity Fund Investment (matures October 16, 2018)

On January 16, 2018, we entered into a securities purchase agreement (the “FirstFire Purchase Agreement”) and a registration rights agreement (the “FirstFire RRA”) with FirstFire Global Opportunity Fund, LLC (“FirstFire”), and issued a convertible promissory note (the “FirstFire Note”) in the aggregate principal amount of \$150,000 at 5% annual interest, which is convertible into shares of common stock of the Company at \$0.394 per share, subject to the terms, and certain limitations and conditions set forth in the FirstFire Purchase Agreement and FirstFire Note. FirstFire may convert the FirstFire Note at any time. The Company may require the conversion of the FirstFire Note in the event the Company’s common stock has traded at a price per share of \$0.75 or above for the ten trading days immediately preceding the mandatory conversion, and the shares underlying the conversion are subject to an effective registration statement filed with the SEC. The FirstFire Note matures on October 16, 2018.

Pursuant to the FirstFire Purchase Agreement, the Company issued 75,000 shares of common stock to FirstFire as a commitment fee (the “FirstFire Commitment Shares”) at \$0.39 per share and \$29,250 is recorded as a discount on convertible notes and will amortize to interest expense over the term of the note.

Under the Note and FirstFire Purchase Agreement, the Company has reserved 394,949 shares of common stock for issuance upon conversion of the Note. Pursuant to the FirstFire RRA, the Company agreed to file a registration statement with the SEC registering all shares of common stock into which the FirstFire Note is convertible, and the FirstFire Commitment Shares. The FirstFire Purchase Agreement allows for an adjustment to the number of FirstFire Commitment Shares in the event the closing price of our common stock, on the earlier of the date the registration statement is deemed effective and 20 trading days following the six-month anniversary of the FirstFire Note, is lower than the closing price on January 16, 2018 (which was \$0.39). In such event, additional shares would be issued to FirstFire such that the aggregate FirstFire Commitment Shares issued have the same value as the shares issued on January 16, 2018.

Pursuant to the requirements set forth in the registration rights agreements, we filed a registration statement with the SEC which was deemed effective as of February 8, 2018. On February 8, 2018, our common stock last traded at \$0.3147 per share. Because the last traded price of our common stock on the date the registration statement was deemed effective was less than the price of our common stock on the dates of the FirstFire Purchase Agreements, at their option, we are required to issue additional “commitment shares”. FirstFire exercised that right, and we issued 36,536 additional shares of our common stock and \$11,498 is recorded as additional discount on convertible notes and

will amortize to interest expense over the term of the note.

FirstFire represented to the Company, among other things, that it was an “accredited investor” (as such term is defined in Rule 501(a) of Regulation D under the Securities Act of 1933, as amended). The FirstFire Note, FirstFire Purchase Agreement, and the FirstFire RRA contain customary representations, warranties, agreements and conditions including indemnification rights and obligations of the parties. The FirstFire Note contains a price protection provision such that if we issue a security with any term more favorable to the holder of such security that was not similarly provided in the FirstFire Note, then the Company shall notify FirstFire of such additional or more favorable term and such term, at its option, shall become a part of the FirstFire Note.

Line of credit, matures September 1, 2019

On March 1, 2018, we received \$390,000 pursuant to a line of credit, accruing interest at a rate of 18% per annum, for which we have pledged our inventory and accounts receivable as collateral. Interest is paid quarterly, and, at the option of the holder, payable in either (i) cash, (ii) our common stock, calculated based on the 20-day average closing price, or (iii) options to purchase our common stock, priced at the 20-day average closing price, the number of shares doubled, and expiring 10 years from the date of grant. The holder of the line of credit has the right to call due the outstanding principal amount on 30-days’ notice at any time after September 1, 2019.

Each investor, for no additional consideration, received a warrant to purchase our common stock. (See Note 7). The warrant allows for the purchase of the number of common shares equal to the investment amount (e.g., one warrant share for each dollar invested).

Two-Year Convertible Note, matures July 20, 2019

On July 20, 2017, the Company accepted \$400,000 and issued a promissory note with a 10% original issue discount in the principal amount of \$440,000, matures July 20, 2019 and accrues interest at 12%. The note originally provided that interest was to be paid quarterly beginning October 1, 2017, in either cash, common stock, or an option to purchase common stock, in the holder’s discretion. On January 25, 2018, the interest provisions in the note were modified such that the 12% annual simple interest is due at maturity.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

At maturity, the principal amount of the note and any accrued and unpaid interest automatically converts, at the holder's option, into either BioLargo common shares at \$0.42 per share, 2,000 shares of Clyra Medical Technologies common stock held by BioLargo, or any combination thereof. The fair value of the beneficial conversion feature resulted in a \$171,429 recorded on our consolidated balance sheet as a discount on convertible notes payable, net of current portion. The discount will be amortized monthly as interest expense through July 20, 2019.

Note payable, matures March 8, 2020

On March 8, 2018, we received \$50,000 and entered into a note payable. The note is due on upon demand from the noteholder, with sixty days' notice. The demand may not be made before June 30, 2018, and in the absence of the demand, the maturity date is March 8, 2023. In lieu of interest, we issued the note holder a warrant to purchase 150,000 shares of our common stock at an exercise price of \$0.35. The warrant expires February 28, 2023. The shares available for purchase vest in increments of 6,250 shares per month. (See Note 7.)

Convertible Notes, mature June 20, 2020 (Summer 2017 Unit Offering)

On May 24, 2017, we commenced a private securities offering (titled the "Summer 2017 Unit Offering") which offered the sale of \$1,500,000 of "Units," each Unit consisting of a convertible promissory note and stock purchase warrant. Concurrently, we issued Pricing Supplement No. 1 setting the initial unit/conversion price at \$0.42 per share, and the initial warrant exercise price at \$0.65 per share. The promissory notes issued to investors mature June 20, 2020, and bear interest at the rate of 12% per annum on the amount invested. Any interest due will be paid quarterly in arrears in cash or shares of common stock. If paid by the issuance of common stock, interest is paid at a conversion price equal to the average closing price of the Company's common stock over the 20 trading days prior to the interest payment due date. The principal amount of the note may be paid by the issuance of shares of common stock, or cash, upon maturity at the Company's election. Promissory notes may be converted at any time by the investor, at maturity by the Company, or by the Company prior to maturity, so long as the following conditions are met: (i) the Shares issued as payment are registered with the SEC; and (ii) the Company's common stock closes for ten consecutive trading days at or above three times the Unit price.

In addition to the convertible promissory note, each investor received a warrant allowing for the purchase of the number of shares of BioLargo common stock equal to the investment amount divided by the unit/conversion price (e.g., one warrant share for each share of common stock which the investor is eligible to receive through conversion of the note). (See Note 7.) The warrants expire on June 20, 2022. The Company may “call” the warrants, requiring the investor to exercise their warrants within 30 days or forever lose the rights to do so, only if the following conditions have been met: (i) the underlying Shares are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

Through December 31, 2017, we had received \$523,700 in investments in the Summer 2017 Unit Offering, from ten accredited investors, all pursuant to Pricing Supplement No. 1. No investments were received pursuant to a second pricing supplement issued on December 11, 2017, setting the unit price at \$0.394 per share. On February 22, 2018, we issued Pricing Supplement No. 3, setting the Unit price to \$0.30 and the warrant exercise price at \$0.48. During the three months ended March 31, 2018, we received \$80,000 in investments from two accredited investors pursuant to this third pricing supplement. The offering was terminated at the conclusion of processing these two investments.

The offering documents assured the investors that in the event a subsequent pricing supplement offered a lower conversion or exercise price, prior investors would be given those favorable terms. Because we issued a third pricing supplement lowering the Unit price to \$0.30 per share, the unit price for the prior investors was lowered to \$0.30. As a result, the number of warrant shares available for purchase by each investor increased. (See Note 7.)

Subsequent to March 31, 2018, holders of \$478,700 of Summer 2017 Offering notes elected to accept the Company’s offer of incentive shares to convert these notes prior to maturity (see Note 12).

Convertible Notes, mature April 20, 2021 (Spring 2018 Unit Offering)

On March 1, 2018, we commenced a private securities offering (titled the “Spring 2018 Unit Offering”) which offered the sale of \$1,500,000 of “Units,” each Unit consisting of a convertible promissory note and stock purchase warrant. Concurrently, we issued Pricing Supplement No. 1 setting the initial unit/conversion price at \$0.30 per share, and the initial warrant exercise price at \$0.48 per share. The promissory notes issued to investors mature April 20, 2021, and bear interest at the rate of 12% per annum on the amount invested. Any interest due will be paid quarterly in arrears in cash or shares of common stock. If paid by the issuance of common stock, interest is paid at a conversion price equal to the average closing price of the Company’s common stock over the 20 trading days prior to the interest payment due date. The principal amount of the note may be paid by the issuance of shares of common stock, or cash, upon maturity at the Company’s election. Promissory notes may be converted at any time by the investor, at maturity by the Company, or by the Company prior to maturity, so long as the following conditions are met: (i) the Shares issued as payment are registered with the SEC; and (ii) the Company’s common stock closes for ten consecutive trading days at or above three times the Unit price.

In addition to the convertible promissory note, each investor will receive a warrant allowing for the purchase of the number of shares of BioLargo common stock equal to the investment amount divided by the unit/conversion price (e.g., one warrant share for each share of common stock which the investor is eligible to receive through conversion of the note). (See Note 7.)

Through March 31, 2018, we had received one investment for \$100,000 in this offering, and issued a warrant to purchase 333,333 shares. This investment was received from an entity owned/controlled by a member of our board of directors.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Note 6. Share-Based Compensation

During the three months ended March 31, 2017 and 2018, we recorded an aggregate \$280,288 and \$320,090, respectively, in selling general and administrative expense related to the issuance of stock options.

2007 Equity Incentive Plan

On September 7, 2007, and as amended April 29, 2011, the BioLargo, Inc. 2007 Equity Incentive Plan (“2007 Plan”) was adopted as a means of providing our directors, key employees and consultants additional incentive to provide services. Both stock options and stock grants were made under this plan for a period of 10 years. It expired on its terms on September 7, 2017. The Board’s Compensation Committee administers this plan. As plan administrator, the Compensation Committee has sole discretion to set the price of the options. The Company is in the process of implementing a new stock option plan for 2018.

On February 10, 2017, we extended the engagement agreement with our Chief Financial Officer, retroactive to October 1, 2016. The sole consideration for the one-year extension was the issuance of an option to purchase 300,000 shares of our common stock, at an exercise price of \$0.69 per share which was equal to the closing price of our common stock on the date of grant. The option expires February 10, 2027, and vests over the term of the engagement with 125,000 shares having vested as of February 10, 2017, and the remaining shares to vest 25,000 shares monthly beginning March 1, 2017, and each month thereafter, so long as his agreement is in full force and effect. The fair value of the option totaled \$207,000, during the three months ended March 31, 2017, \$103,500 is recorded as selling, general and administrative expense on our statement of operations. The balance vested monthly through September 30, 2017.

Activity for our stock options under the 2007 Plan for the three months ended March 31, 2017 and 2018 is as follows:

Weighted

As of March 31, 2017:	Options Outstanding	Exercise Price per share		Average Price per share
Balance, December 31, 2016	9,916,586	\$0.23–	1.89	\$ 0.44
Granted	300,000	0.69		0.69
Expired	—	—		—
Balance, March 31, 2017	10,216,586	\$0.23–	1.89	\$ 0.47

As of March 31, 2018:	Options Outstanding	Exercise Price per share		Weighted Average Price per share
Balance, December 31, 2017	9,831,586	\$0.23–	1.89	\$ 0.44
Granted	—	—		—
Expired	(50,000)	1.89		1.89
Balance, March 31, 2018	9,781,586	\$0.23–	1.65	\$ 0.43

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Options issued Outside of the 2007 Equity Incentive Plan

On January 31, 2018, we issued options to purchase 18,071 shares of our common stock at an exercise price of \$0.28 per share, expiring 10 years from the date of grant. The fair value of these options total \$5,060 and is recorded as selling, general and administrative expenses.

On February 28, 2018, we issued options to purchase 21,429 shares of our common stock at an exercise price of \$0.28 per share expiring 10 years from the date of grant. The fair value of these options total \$6,000 and is recorded as selling, general and administrative expenses.

On March 31, 2018, we issued options to purchase 565,649 shares of our common stock at an exercise price of \$0.26 per share to members of our board of directors for services, an employee in lieu of salary, and to consultants for services. The fair value of these options totaled \$146,503 and is recorded as selling, general and administrative expenses.

On February 1, 2017, as part of an agreement we executed with a strategic advisor, we issued an option to purchase 300,000 shares of our common stock with an exercise price of \$0.67, the stock price on grant date. The option expires ten years from the date of issuance and the option vests in 12,500 equal amounts over 24 months. The agreement also calls for the strategic advisor to provide deliverables focused in the water industry such as business plans and strategic initiatives for the Company. During the three months ended March 31, 2017, 25,000 options vested resulting in a fair value of \$15,000 recorded as selling, general and administrative expense on our statement of operations. This agreement terminated in November 2017, and the remaining unvested 175,000 options were cancelled.

On March 31, 2017, we issued options to purchase 283,526 shares of our common stock at an exercise price of \$0.50 per share to members of our board of directors, in lieu of \$65,000 in fees and to vendors in lieu or accrued and unpaid fees \$56,671. The weighted-average fair value of these options totaled \$141,763 and an additional \$20,092 was recorded as selling, general and administrative expenses.

Edgar Filing: BIOLARGO, INC. - Form 10-Q

Activity of our stock options issued outside of the 2007 Equity Incentive Plan for the three months ended March 31, 2017 and 2018 is as follows:

As of March 31, 2017:	Options Outstanding	Exercise Price per share	Weighted Average Price per share
Balance, December 31, 2016	20,148,766	\$0.18-1.00	\$ 0.40
Granted	583,526	0.50-0.67	0.59
Expired	—	—	—
Balance, March 31, 2017	20,732,292	\$0.18-1.00	\$ 0.41

As of March 31, 2018:	Options Outstanding	Exercise Price per share	Weighted Average Price per share
Balance, December 31, 2017	20,018,408	\$0.25- 1.00	\$ 0.51
Granted	619,435	0.26- 0.28	0.26
Expired	(2,400,000)	0.99	0.99
Balance, March 31, 2018	18,237,843	\$0.25- 1.00	\$ 0.45

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

For employees, we recognize compensation expense for stock option awards on a straight-line basis over the applicable service period of the award, which is the vesting period. Share-based compensation expense is based on the grant date fair value estimated using the Black-Scholes Option Pricing Model. The following methodology and assumptions were used to calculate share-based compensation for the three months ended March 31:

	2017	2007	2018
	Non	Plan	Non
	Plan	Plan	Plan
Risk free interest rate	2.40 %	2.40 %	2.43 %
Expected volatility	601 %	601 %	563 %
Expected dividend yield	—	—	—
Forfeiture rate	—	—	—
Expected life in years	7	7	7

Expected price volatility is the measure by which our stock price is expected to fluctuate during the expected term of an option. Expected 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 rate used in the Black-Scholes calculation is based on the prevailing U.S. Treasury yield as determined by the U.S. Federal Reserve. We have never paid any cash dividends on our common stock and do not anticipate paying cash dividends on our common stock in the foreseeable future.

Historically, we have not had significant forfeitures of unvested stock options. A significant number of our stock option grants are fully vested at issuance or have short vesting provisions. Therefore, we have estimated the forfeiture rate of our outstanding stock options as zero.

Note 7. Warrants

Warrants Issued Concurrently with Spring 2018 Unit Offering

During the three months ended March 31, 2018, pursuant to the terms of our Spring 2018 Unit Offering (see Note 5), we issued a warrant to purchase up to an aggregate 333,333 shares of our common stock at an exercise price of \$0.48 per share to the investor in the Spring 2018 Offering, a member of our board of directors. The warrant expires April 20, 2023. The relative fair value of the warrant resulted in \$49,306 recorded as a discount on our convertible notes on our consolidated balance sheet in the period issued.

The Company may “call” these warrants, requiring the holder to exercise their warrants within 30 days or forever lose the rights to do so, if the following conditions have been met: (i) the shares of common stock underlying the warrants are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

Warrants Issued Concurrently with Line of Credit Offering

During the three months ended March 31, 2018, pursuant to the terms of our Line of Credit (see Note 5, “Line of Credit, matures September 1, 2019”), we issued warrants to purchase up to an aggregate 390,000 shares of our common stock at an exercise price of \$0.35 per share. These warrants expire March 1, 2023. The relative fair value of these warrants resulted in \$85,002 recorded as a discount on our “convertible notes payable and line of credit” on our consolidated balance sheet in the period issued.

The Company may “call” these warrants, requiring the holder to exercise their warrants within 30 days or forever lose the rights to do so, if the following conditions have been met: (i) the shares of common stock underlying the warrants are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Warrants Issued Concurrently with Note Payable

During the three months ended March 31, 2018, pursuant to the terms of the note payable. (see Note 5, “Note payable, matures March 8, 2020”), we issued warrants to purchase up to an aggregate 150,000 shares of our common stock at an exercise price of \$0.35 per share. At the end of each month 6,250 warrants vest as long as the note payable is outstanding. Although the note matures March 8, 2020, the investor may call the note at any time after June 30, 2018. Thus, a minimum of 25,000 warrants will vest, and the fair value of these warrants totaled \$6,500. Of this amount \$1,625 was recorded as interest expense and the remaining \$4,875 is recorded as a discount on our consolidated balance sheet in the period issued. These warrants expire February 28, 2023.

Warrants Issued to Summer 2017 Unit Offering Investors

Pursuant to the Summer 2017 Unit Offering, we issued warrants to purchase the number of shares of stock equal to each investor’s investment amount, divided by the “unit price” set forth in a “pricing supplement”. The offering documents assured the investors that in the event a subsequent pricing supplement offered a lower conversion or exercise price, prior investors would be given those favorable terms. On February 12, 2018, we issued a third pricing supplement, lowering the unit price to \$0.30. As a result of this reduction, the number of shares purchasable pursuant to warrants issued to prior investors increased by an aggregate 416,478 shares. Additionally, during the three months ended March 31, 2018, we accepted two final investments in the aggregate amount of \$80,000, pursuant to the third pricing supplement, and issued these investors warrants to purchase an aggregate 266,667 shares. The relative fair value of these warrants, including the increase in purchasable shares, resulted in \$103,322 recorded as a discount on our consolidated balance sheet in the period issued.

Warrants Issued Concurrently with One Year Convertible Notes

We have accepted \$250,000 investments and issued one-year OID convertible notes on three occasions: July 8, 2016, December 30, 2016, and July 17, 2017. In addition to the notes, the investors received warrants on each of those three dates to purchase an aggregate 400,000 shares of our common stock. These warrants were initially exercisable at \$0.65 per share (for July 2016 warrants), \$0.70 per share (for December 2016 warrants), and \$0.65 per share (for July 2017 warrants), and expire five years from the date of grant. Each of the warrants contain a provision that the exercise

price may be reduced in the event we sell our common stock or issue warrants to third parties at a lower prices, with particular exclusions, the details of which are available in our Form 10-K. The exercise price of these warrants has decreased, and the number of shares increased, on multiple occasions prior to December 31, 2017, most recently on December 11, 2017, at which time the exercise price was reduced to \$0.394 per share, and the number of shares issuable pursuant to the warrants, in the aggregate, increased from the original 1,200,000 shares, to 2,081,216.

On February 22, 2018, we sold shares of our common stock to Lincoln Park Capital at \$0.25 per share (see Note 4). Since these securities were sold at less than the then previously adjusted \$0.394 warrant exercise price, the exercise price of the warrants were decreased from \$0.394 to \$0.25 per share, and the number of shares issuable pursuant to the warrants increased by an aggregate 1,198,784 shares. The fair value of the warrants issued totaled \$297,439 and is recorded as a deemed dividend in our equity statement for the three months ended March 31, 2018.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

We have certain warrants outstanding to purchase our common stock, at various prices, as described in the following table:

	Number of Shares	Price Range
As of March 31, 2017		
Outstanding as of December 31, 2016	20,035,114	\$0.125– 1.00
Issued	219,298	0.70
Exercised	(510,000)	0.30
Outstanding as of March 31, 2017	19,744,412	0.125– 1.00
As of March 31, 2018		
Outstanding as of December 31, 2017	22,104,817	\$0.125– 1.00
Issued	2,611,513	0.25 – 0.48
Exercised	—	—
Outstanding as of March 31, 2018	24,716,330	\$0.125– 1.00

The fair value of each award grant is estimated on the date of grant using the Black-Scholes option-pricing model. The determination of expense of warrants issued for services or settlement also uses the option-pricing model. The principal assumptions we used in applying this model were as follows for the three months ended March 31:

	2017	2018
Risk free interest rate	1.93 %	2.54%
Expected volatility	297 %	252%
Expected dividend yield	—	—
Forfeiture rate	—	—
Expected life in years	5	5- 10

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The risk-free interest rate is based on U.S. Treasury yields in effect at the time of grant. Expected volatilities are based on historical volatility of our common stock.

Note 8. Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses included the following:

	December 31, 2017	March 31, 2018
Accounts payable and accrued expenses	\$173,357	\$273,817
Accrued interest	50,748	77,183
Total accounts payable and accrued expenses	\$224,105	\$351,000

Issuance of Common Stock in exchange for payment of payables

Payment of Officer Salaries

On March 31, 2018, we issued 323,030 shares of our common stock at \$0.26 per share in lieu of \$83,665 of accrued and unpaid obligations to two of our officers. The price-per-share was based on the closing price of our common stock on the last day of the month.

Payment of Consultant Fees and Accrued Interest

During the three months ended March 31, 2018, we issued 391,406 shares of our common stock, at prices ranging between \$0.26 - \$0.41 per share, in lieu of \$112,388 of accrued and unpaid obligations to consultants.

During the three months ended March 31, 2017, we issued 144,545 shares of our common stock, at prices ranging between \$0.50 - \$0.70, in lieu of \$82,480 of accrued and unpaid obligations to consultants.

During the three months ended March 31, 2018, we issued 617,072 shares of our common stock, at \$0.25 per share, in lieu of accrued interest totaling \$165,067.

During the three months ended March 31, 2017, we issued 310,404 shares of our common stock, at prices ranging between, \$0.53 - \$0.70 per share, in lieu of accrued interest totaling \$178,929.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

Note 9. Noncontrolling Interest

Clyra Medical Technologies

In May 2012, we formed a subsidiary for the purpose of marketing and selling medical products containing our technology, Clyra Medical Technologies, Inc. (“Clyra”). We initially owned 100% of this subsidiary, and then Clyra granted shares to management, such that we owned approximately 85% of Clyra’s shares.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Clyra Private Securities Offering

On December 30, 2015, Clyra sold shares of its Series A Preferred Stock (“Preferred Shares”) to Sanatio Capital, LLC (“Sanatio”) for \$750,000. As a result of the sale, Sanatio owned 40% of Clyra’s issued and outstanding shares, BioLargo owned 54%, and the remainder was owned by management. Concurrent with the sale of the Preferred Shares, the shareholders entered into a shareholders’ agreement that provides for a three-member board of directors, consisting of the company’s president, a person appointed by BioLargo, and a person appointed by Sanatio. BioLargo appointed its president, Dennis P. Calvert, to serve on Clyra’s board. Sanatio appointed its owner, Jack B. Strommen, to serve on the board. In June 2017, Mr. Strommen was elected to BioLargo’s board of directors.

As set forth in Clyra’s Amended and Restated Articles of Incorporation, Preferred Shares accrue an annual dividend of 8% for a period of five years. Although the dividends began to accrue immediately, Clyra has no obligation to declare a dividend until a product of the company has received a premarket approval by the United States Federal Drug Administration (“FDA”), or for which a premarket notification pursuant to form 510(k) has been submitted and for which the FDA has given written clearance to market the product in the United States (either, “FDA Approval”). After FDA Approval, annually on December 20, and unless prohibited by California law governing distributions to shareholders, Clyra is required to declare and pay any accruing dividends to holders of Preferred Shares then accrued but unpaid. As the declaration and payment of such dividends is contingent on an uncertain future event, no liability has been recorded for the dividends. The accumulated and undeclared dividend balance as of March 31, 2018 is \$135,000.

Holders of Preferred Shares are entitled to preferential payments in the event of a liquidation, dissolution or winding up of the company, in an amount equal to any accrued and unpaid dividends. After such preference, any remaining assets are distributed pro-rata between holders of Clyra common stock and Preferred Shares as if the Preferred Shares had converted to Clyra common stock. Holders of Preferred Shares may convert the shares to Clyra common stock initially on a one-to-one basis. The conversion formula is subject to change in the event Clyra sells stock at a lower price than the price paid by Sanatio.

In April 2017, BioLargo purchased 500 shares of Clyra common stock from a former member of Clyra’s management for \$40,000.

Clyra Line of Credit

On March 31, 2017, Clyra obtained a \$250,000 line of credit from Sanatio Capital LLC, accruing interest at a rate of 10% per annum and a 5% original issue discount. The line of credit was scheduled to mature on March 31, 2019, but was subsequently converted to Clyra stock in full payment (see below).

In August 2017, Clyra commenced a private securities offering of its common shares at a price of \$160 per share, and accepted \$1,000,000 in subscriptions. It issued 6,250 shares of its common stock to two investors. Of that amount, BioLargo invested \$250,000 and was issued 1,562.5 shares. On August 4, 2017, Clyra issued 1,690 shares of its common stock at \$160 per share to Sanatio in exchange for payment of the \$270,400 principal and interest outstanding under the line of credit held by Sanatio (see above). Subsequent to the issuance of shares to investors in the offering, and to Sanatio for the conversion of the line of credit, BioLargo owned 15,297.5 shares of Clyra common stock, which is 46.3% of the outstanding stock at Clyra. Two members of BioLargo's board of directors (Dennis P. Calvert and Jack B. Strommen) comprise a majority of the three-member Clyra board of directors. Management has determined that BioLargo does control Clyra after reviewing the guidance of ASC Topic 810, "Consolidation". While BioLargo does not have voting interest control through 50% ownership of Clyra, it does exercise control under the Variable Interest Model. BioLargo is the primary beneficiary since it has the power to direct Clyra's activities that most significantly impact Clyra's performance and it has the obligation to absorb losses or receive benefits (through royalties and licensing) that could be potentially significant to Clyra. BioLargo has consolidated Clyra's operations through March 31, 2018.

On September 27, 2017, Clyra submitted to the FDA an application for premarket notification under Section 510(k) for a wound care product. It is now in the formal review process by the FDA.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

BioLargo Maritime Solutions

The Company has an additional subsidiary, BioLargo Maritime Solutions, whereby if certain factors are met, a noncontrolling equity interest in this subsidiary has been pledged to its management.

Note 10. BioLargo Engineering, Science and Technologies, LLC

In September 2017, we commenced a full service environmental engineering firm and formed a Tennessee entity named BioLargo Engineering, Science & Technologies, LLC (“BLEST”). In conjunction with the start of this subsidiary, we entered into a three-year office lease in the Knoxville Tennessee area, and entered into employment agreements with seven scientists and engineers. These agreements and related operational obligations add approximately \$100,000 to our monthly budget for payroll, taxes, benefits, insurance, and other related obligations. The company was capitalized with two classes of membership units: Class A, 100% owned by BioLargo, and Class B, held by management of BLEST, and which initially have no “profit interest,” as that term is defined in Tennessee law. However, over the succeeding five years, the Class B members can earn up to a 30% profit interest. They also have been granted options to purchase up to an aggregate 2,000,000 shares of BioLargo, Inc. common stock. The profit interest and option shares are subject to a five year vesting schedule tied to the performance of the subsidiary, including gross revenue targets that increase over time, obtaining positive cash flow by March 31, 2018, collecting 90% of its account receivables, obtaining a profit of 10% in its first year (and increasing in subsequent years), making progress in the scale-up and commercialization of our AOS system, and using BioLargo research scientists (such as our Canadian team) for billable work on client projects. The details of these transactions were reported on a Form 8-K filed with the SEC on September 8, 2017. Given the significant performance criteria, the Class B units and the stock options will only be recognized in compensation expense if or when the criteria are satisfied. It is still too early to make a determination as to whether BLEST will meet some of the performance criteria. Through March 31, 2018 and as of the end of 2017, BLEST has not met any of the criteria and therefore no portion of the Class B Units and stock options have been earned or vested.

Note 11. Commitments and Contingencies

Calvert Employment Agreement

On May 2, 2017, the Company entered into an employment agreement with its President and Chief Executive Officer Dennis P. Calvert (the “Calvert Employment Agreement”), replacing in its entirety the previous employment agreement with Mr. Calvert dated April 30, 2007.

The Calvert Employment Agreement provides that Mr. Calvert will continue to serve as our President and Chief Executive Officer and receive base compensation equal to his current rate of pay of \$288,603 annually. In addition to this base compensation, the agreement provides that he is eligible to participate in incentive plans, stock option plans, and similar arrangements as determined by the Company’s Board of Directors, health insurance premium payments for himself and his immediate family, a car allowance of \$800 per month, paid vacation of four weeks per year, and bonuses in such amount as the Compensation Committee may determine from time to time.

The Calvert Employment Agreement provides that Mr. Calvert will be granted an option (the “Option”) to purchase 3,731,322 shares of the Company’s common stock. The Option shall be a non-qualified stock option, exercisable at \$0.45 per share, which represents the market price of the Company’s common stock as of the date of the agreement, exercisable for ten years from the date of grant and vesting in equal increments over five years. Notwithstanding the foregoing, any portion of the Option which has not yet vested shall be immediately vested in the event of, and prior to, a change of control, as defined in the Calvert Employment Agreement. The agreement also provides for a grant of 1,500,000 shares of common stock, subject to the execution of a “lock-up agreement” whereby the shares remain unvested unless and until the earlier of (i) a sale of the Company, (ii) the successful commercialization of the Company’s products or technologies as demonstrated by its receipt of at least \$3,000,000 in cash, or the recognition of \$3,000,000 in revenue, over a 12-month period from the sale of products and/or the license of technology, and (iii) the Company’s breach of the employment agreement resulting in his termination. The Option contains the other terms standard in option agreements issued by the Company, including provisions for a cashless exercise.

Table of Contents

BIOLARGO, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The Calvert Employment Agreement has a term of five years, unless earlier terminated in accordance with its terms. The Calvert Employment Agreement provides that Mr. Calvert's employment may be terminated by the Company due to his death or disability, for cause, or upon a merger, acquisition, bankruptcy or dissolution of the Company. "Disability" as used in the Calvert Employment Agreement means physical or mental incapacity or illness rendering Mr. Calvert unable to perform his duties on a long-term basis (i) as evidenced by his failure or inability to perform his duties for a total of 120 days in any 360-day period, or (ii) as determined by an independent and licensed physician whom Company selects, or (iii) as determined without recourse by the Company's disability insurance carrier. "Cause" means that Mr. Calvert has (i) engaged in willful misconduct in connection with the Company's business; or (ii) been convicted of, or plead guilty or nolo contendere in connection with, fraud or any crime that constitutes a felony or that involves moral turpitude or theft. If Mr. Calvert's employment is terminated due to merger or acquisition, then he will be eligible to receive the greater of (i) one year's compensation plus an additional one-half year for each year of service since the effective date of the employment agreement or (ii) one year's compensation plus an additional one-half year for each year remaining in the term of the agreement. Otherwise, he is only entitled to receive compensation due through the date of termination.

The Calvert Employment Agreement requires Mr. Calvert to keep certain information confidential, not to solicit customers or employees of the Company or interfere with any business relationship of the Company, and to assign all inventions made or created during the term of the Calvert Employment Agreement as "work made for hire".

Clyra Consulting Agreement

Our partially owned subsidiary Clyra (see Note 9) entered into a consulting agreement with Beach House Consulting, LLC, through which Jack B. Strommen will be providing consulting services to Clyra related to its sales and marketing activities once it has received FDA Approval (as defined in Note 9 and the associated agreement) on a product, at which point the agreement provides that Mr. Strommen is to receive \$23,438 per month for a period of four years. This agreement has not started, and the total cash obligation related to the agreement would be \$1,125,024 over four years.

Note 12. Subsequent Events.

Management has evaluated subsequent events through the date of the filing of this Quarterly Report and management noted the following for disclosure.

Conversion of Unit Notes

On May 7, 2018, we (BioLargo, Inc., the “Company”) issued 15,747,482 shares of our common stock in satisfaction of \$4,133,738 of convertible promissory notes issued in our “unit” offerings at varying conversion prices, maturing on the following dates:

Note Description	Principal Outstanding March 31, 2018	Amount Converted to Stock	Principal Amount Remaining
Convertible notes, mature June 1, 2018	\$ 4,468,847	\$(3,154,467)	\$1,314,380
Convertible notes, mature June 17, 2019	\$ 283,571	\$(283,571)	---
Convertible notes, mature December 31, 2019	\$ 292,000	\$(217,000)	\$75,000
Convertible notes, mature June 20, 2020	\$ 603,700	\$(478,700)	\$125,000

These conversions were voluntary on the part of the noteholders and prior to the various maturity dates on notes that were issued in prior “unit” offerings conducted by the Company (2015 Unit Offering, Winter 2016 Unit Offering, and Summer 2017 Unit Offering). We offered these noteholders incentives to convert their notes early. Noteholders with conversion prices of \$0.25 and \$0.30 were offered incentive shares equal to one and one-half times the number of shares issuable for the payment of interest that would accrue from the last interest payment date of March 20, 2018, through the maturity of the note, at a fixed price of \$0.25 per share (for example, a note that would have yielded \$1,000 in interest, would receive 1,000 times 1.5 divided by 0.25 equals 6,000 incentive shares). We offered holders of notes with conversion prices higher than \$0.30 the ability to reduce their conversion price to \$0.30 by paying additional funds equal to six or twenty percent of their original investment (6% for notes with original conversion prices of \$0.35, and 20% for notes with original conversion prices of \$0.55 and \$0.57). The additional funds did not increase the amount of the note payable, nor did the reduced conversion price affect the number of shares purchasable under the warrant issued with their “unit” investment. Holders of 38 notes elected to pay an aggregate \$261,781 to reduce the conversion prices of their notes to \$0.30.

Table of Contents

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

This quarterly report on Form 10-Q contains forward-looking statements. These forward-looking statements involve risks and uncertainties, including statements regarding BioLargo’s capital needs, business plans and expectations. Such forward-looking statements involve risks and uncertainties regarding BioLargo’s ability to carry out its planned development and production of products. Forward-looking statements are made, without limitation, in relation to BioLargo’s operating plans, BioLargo’s liquidity and financial condition, availability of funds, operating and exploration costs and the market in which BioLargo competes. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as “may”, “will”, “should”, “expect”, “plan”, “intend”, “anticipate”, “believe”, “estimate”, “predict”, “potential” or “continue”, the negative of such terms or other comparable terminology. Actual events or results may differ materially. In evaluating these statements, you should consider various factors, including the risks outlined in our Form most recent annual report on Form 10-K, and, from time to time, in other reports BioLargo files with the SEC. These factors may cause BioLargo’s actual results to differ materially from any forward-looking statement. BioLargo disclaims any obligation to publicly update these statements, or disclose any difference between its actual results and those reflected in these statements. The information constitutes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Given these uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements.

Unless otherwise expressly stated herein, all statements, including forward-looking statements, set forth in this Form 10-Q are as of March 31, 2018, unless expressly stated otherwise, and we undertake no duty to update this information.

As used in this report, “we” and “Company” refers to (i) BioLargo, Inc., a Delaware corporation; (ii) its wholly-owned subsidiaries BioLargo Life Technologies, Inc., a California corporation, Odor-No-More, Inc., a California corporation, BioLargo Water USA, Inc., a California corporation, BioLargo Development Corp., a California corporation, BioLargo Maritime Solutions, Inc., a California corporation, BioLargo Engineering, Science & Technologies, LLC, a Tennessee limited liability company, and Canadian subsidiary BioLargo Water, Inc.; and (iii) Clyra Medical Technologies, Inc. (“Clyra”), a partially owned subsidiary.

The following discussion and analysis should be read in conjunction with our unaudited consolidated financial statements and the related notes to the consolidated financial statements included elsewhere in this report.

Our Business- A Sustainable Technology Incubator

BioLargo, Inc. is an innovation company driven by our mission is to “make life better” by developing breakthrough platform technologies, nurturing and building businesses around the intellectual property, while providing capital and support along the journey from “cradle” to “maturity”. Our business strategy is straightforward: we invent or acquire technologies that we believe have the potential to be disruptive in large commercial markets; we incubate these technologies to advance and promote their commercial success as we leverage our considerable scientific, engineering, and entrepreneurial talent; we then monetize these technical assets through a variety of business structures that may include licensure, joint venture, sale, spin off, or by deploying direct to market strategies. We seek to unlock the value of the underlying technologies to both advance our purposeful mission while we create value for our stockholders

Our first significant commercial success is unfolding now for our odor control products sold through our subsidiary, Odor No More, Inc. Sales are increasing as we focus on two areas: serving the solid waste handling and wastewater treatment industries with our CupriDyne Clean industrial odor control products, and the U.S. government through our Nature’s Best Solution products. We are gearing up for rapid growth as our products are experiencing market adoption.

Our second commercial operation provides professional engineering services, through our subsidiary BioLargo Engineering, Science & Technologies, LLC (“BLEST”). We provide a menu of professional engineering services to compliment and nurture our technologies as well as serve clients on a fee-for-service basis.

Table of Contents

In addition to our two operating subsidiaries, we have technologies and products in the development pipeline progressing towards commercialization, including our “Advanced Oxidation System,” that we target to have commercially ready in late 2018 or early 2019, and our medical products, which will be ready for commercialization as soon as we pass FDA clearance.

Industrial Odor Control — CupriDyne Clean

Our CupriDyne Clean industrial products reduce and eliminate tough odors and VOC’s in various industrial settings, delivered as a liquid through misting systems, sprayers, water trucks and similar water delivery systems. We also offer powders that can be mixed to create liquids on site for our customers. We believe the product is the number one performing odor-control product in the market. It is priced 25% to 50% below competing products.

We sell CupriDyne Clean for use in landfills, solid waste transfer stations, waste processing and recycling operations, waste-water treatment facilities, waste to energy conversion operations, materials recovery facilities, food processing operations, and livestock production facilities. Customers and experts from these markets report that effective odor control is a top priority in their daily operations and their commitment to serve their local communities where they operate.

In mid-2017, we signed “national purchasing agreements” with three of the largest waste management companies in the United States. These agreements provide us “official” vendor status and authorize us to sell product to the customers’ local operations. These customers are expanding the use of CupriDyne Clean.

We believe our sales of CupriDyne Clean are expanding because our product works better than competing products by eliminating, rather than masking, odors. Our clients have expressed dissatisfaction with existing products, and have told us that as a result of using our product, neighbor complaints have decreased significantly. We estimate there are almost 2,000 active landfills¹, almost 8,000 transfer stations², and almost 16,000 public wastewater treatment facilities³ in the United States. We are very focused on selling to these three markets, and to our “national purchasing agreement” clients.

In the first quarter of 2018, we achieved a new record level of sales (see Results of Operations, below). Because of the expanding demand for our products, we also hired two new sales executives to focus on expanding our relationships with already existing national accounts, as well as an account support staff person that started May 1, 2018. We intend to continue adding both sales and support staff as the demand for our product continues to expand and as capital resources allow.

We believe that our sales executive staff performs a number of critical functions while working to serve our customer's needs. They must be knowledgeable about the general operating procedures of our customers. They need to understand how best to deploy our products to achieve maximum success and value. They often are called upon to troubleshoot and offer suggestions to help our customers achieve optimal success with the use of our products.

As a result of our continued performance and attention to satisfying our customers, we were recently awarded the approvals to begin servicing all of the locations within a regional marketplace operated one of our national accounts. We are also expanding our work within these national accounts around the country. We also have been asked by a number of our customers, both national and municipal, to develop bids to provide design, build and install proposals for equipment and systems that would be used deliver our product within the local operating environment for our current accounts. We have tasked our engineering team to take the lead on these projects.

¹ "Municipal Solid Waste Landfills - Economic Impact Analysis for the Proposed New Subpart to the New Source Performance Standards" (2014), by U.S. Environmental Protection Agency Office of Air and Radiation and Office of Air Quality Planning and Standards.

² The top 5 Waste Management companies in the US, as of 2011, operated 624 transfer stations, and 565 landfills. "Municipal Solid Waste Landfills - Economic Impact Analysis for the Proposed New Subpart to the New Source Performance Standards" (2014), by U.S. Environmental Protection Agency Office of Air and Radiation and Office of Air Quality Planning and Standards. This is a ratio of 1:4 (landfill to transfer stations). The estimated number of transfer stations is this ratio multiplied by the approximate 1,900 total landfills, and rounded.

³ "Failure to Act, The Economic Impact of Current Investment Trends in Water and Wastewater Treatment Infrastructure" (2011), by American Society of Civil Engineers and Economic Development Research Group. Figure includes treatment facilities owned and operated by municipalities, as well as those owned and/or operated by private entities contracting with municipalities.

Table of Contents

Full Service Environmental Engineering

In September 2017 we formed a subsidiary for the purpose of offering full service environmental engineering to third parties, and to provide engineering support services to our internal teams to accelerate the commercialization of our AOS technologies. Its website is found at www.BioLargoEngineering.com.

The subsidiary, BioLargo Engineering, Science & Technologies, LLC (“BLEST”), entered into a three-year office lease in the Knoxville Tennessee area, and entered into employment agreements with seven scientists and engineers with a combined 200+ years’ experience in diverse engineering fields. The team is led by Randall Moore, who served as Manager of Operations for Consulting and Engineering for the Knoxville office of CB&I Environmental & Infrastructure. The other team members are also former employees of CB&I. The team is highly experienced across multiple industries and they are considered experts in their respective fields, including chemical engineering, wastewater treatment (including design, operations, data gathering and data evaluation), process safety, energy efficiency, air pollution, design and control, technology evaluation, technology integration, air quality management & testing, engineering management, permitting, industrial hygiene, applied research and development, air testing, environmental permitting, HAZOP review, chemical processing, thermal design, computational fluid dynamics, mechanical engineering, mechanical design, NEPDES permitting, RCRA/TSCA compliance and permitting, project management, storm water design & permitting, marine engineering, AutoCAD, bench chemistry, continuous emission monitoring system operator, data handling and evaluation and decommissioning and decontamination of radiological and chemical contaminated facilities.

Our engineering team has focused its efforts in two areas. First, servicing third party clients in similar roles as to what they did at CB&I and throughout their well-established careers. Their first client is a CB&I spin off that provides engineering services world wide, and they have already started providing services to local utilities. They are evaluating, bidding on, negotiating, and generally pursuing other commercial opportunities immediately.

Second, our team is working to assist BioLargo to scale-up, engineer and commercialize our AOS water treatment technologies, as well as support other technology and product development efforts within the BioLargo family of companies, including its industrial odor control solutions. By way of example, the team is working with Odor-No-More and its customers to customize misting systems to deliver the CupriDyne Clean liquid products. BLEST will also pursue new inventions and be available to provide assistance where needed for any commercial opportunities that are presented by and through any and all operating units of BioLargo.

During the three months ended March 31, 2018, BLEST secured a new relationship and was retained to serve as “Owner’s Engineer” for a proposed \$687 million integrated biofuels production project to be built on the east coast. The proposed facility would convert hundreds of tons per day of municipal solid wastes and plastics into high-grade fuels and paraffin waxes, while diverting hundreds of thousands of tons of waste from landfills per year. Our team’s initial role in this project is to provide the project’s ownership team with consulting engineering support as the project

becomes finalized. BLEST is now under contract to be paid for engineering services rendered for the pre-project phase, and assuming the project moves ahead, we anticipate that our contractual relationship will expand to an important multi-year role in the project's overall engineering management. BLEST has developed a long list of projects and bids with prospective clients, tracking more than 40 projects and associated bids to supply engineering services to outside clients. The menu includes a long list of projects that would include odor and VOC control, wastewater management, AOS related projects and a host of traditional environmental engineering services. Internal capabilities have also been extended to include research into a new method of lithium refining through strategic relationships. In addition to the ongoing work with the Odor No More division representing more than \$300,000 in new business already out to bid, it has secured ongoing work with the APTIM Picatinny Arsenal and it was recently notified that it was in final consideration as a preferred supplier/vendor to one of the largest oil and gas companies in the world to help solve a series of challenges to process and clean up produced water at one facility. If successfully awarded, the project is estimated to be worth approximately \$1.3 million in revenue to BLEST, which would include roughly 50% for materials and equipment and 50% for engineering services. Management believes that any one or two of the prospective projects will carry the BLEST organization to positive cash flow.

Recent client requests have presented opportunities to serve a number of clients with specific interest in managing high concentrations of ammonia and polyaromatic hydrocarbons, wastewater for breweries and legionella management / mitigation strategies for high traffic buildings.

Advanced Wound Care - Clyra Medical

We formed Clyra Medical Technologies, Inc. ("Clyra") to commercialize our technology in the medical products industry, which we believe can be disruptive to many existing product lines. Our initial product focus is in the "advanced wound care" field, which includes traumatic injury, diabetic ulcers, and chronic hard-to-heal wounds.

Our advanced wound care products combine broad-spectrum antimicrobial capabilities with iodine's natural and well-understood metabolic pathway to promote healing. Our products are highly differentiated from existing antimicrobials in multiple ways - by the gentle nature in which they can perform, reduced product costs, extended antimicrobial activity, and biofilm efficacy. In addition, iodine has no known acquired microbial resistance, unlike many competing products. We believe the markets for these products will include infection control and wound therapy for chronic wounds. We also intend to pursue and study the use of our technology as a compliment to regenerative tissue therapy. In 2017, we filed a third patent application related to our technology for use in medical products. Two applications were filed in 2016. While these patent applications are pending, we intend to continue expanding patent coverage as we refine our medical products. In late 2017, Clyra completed product development on its first design with its advanced wound care technology, and retained Emergo, a global leader in the medical device regulatory field, to prepare and submit to the U.S. Food & Drug Administration ("FDA") premarket notification of a medical device under Section 510(k) of the Food, Drug, and Cosmetic Act. The 510(k) notification was submitted to the FDA's Center for Devices and Radiological Health ("CDRH"). The submission was referred by the CDRH to the FDA Office of Combination Products ("OCP"), which has jurisdiction to classify a product as a drug, device, biological product, or combination product. We asked the OCP for a determination whether our product should be regulated as a medical device, drug, or combination product, and the OCP replied requesting significant additional information. Clyra is evaluating this request and its options on how to move forward. While doing so, Clyra has prepared an application for a second product for submission to the FDA under Section 510(k), and has additional products in development.

Clyra intends these submissions to be the first two of multiple future FDA submissions for “advanced wound care”, and believes our technology has the potential for disruption in other key medical related fields, including dental and veterinary medicine.

While we remain confident that we will ultimately receive premarket clearance for our products, we can make no assurance or prediction as to success of Clyra’s efforts, and must wait patiently for the process with the FDA to conclude.

Table of Contents

BioLargo Water and the Advanced Oxidation System - AOS

BioLargo Water is our wholly owned subsidiary located on campus at the University of Alberta that has been primarily engaged in the research and development of our Advanced Oxidation System (AOS). The AOS is a water treatment device in development that generates a series of highly oxidative species of iodine and other molecules that, because of the proprietary configuration and inner constituents of the AOS, eliminate pathogenic organisms with extreme efficacy.

The key value proposition of the AOS is its ability to eliminate a wide variety of contaminants with high performance while consuming extremely low levels of input electricity – a trait made possible by the complex set of highly oxidative iodine compounds generated within the AOS reactor. Our proof-of-concept and case studies have generated results that suggest the AOS will be more cost- and energy-efficient than commonly used advanced water treatment technologies such as UV, electro- chlorination, and ozonation. This value proposition sets the AOS technology above other water treatment options, as we believe the AOS may allow safe and reliable water treatment for significantly lower cost compared to its competitors and may even enable advanced water treatment in applications where it otherwise would have been prohibitively costly.

Our AOS was the result of break-throughs in both advanced iodine electrochemistry and advances in materials engineering, and its invention led to BioLargo's co-founding a multi-year research chair whose goal was to solve the contaminated water issues associated with the Canadian Oil Sands at the University of Alberta Department of Engineering in conjunction with the top five oil companies in Canada, the regional water district, and various environmental agencies of the Canadian government. Based on recovering oil prices and our ongoing work in Canada, we recently reinitiated discussions with a number of stakeholders in the oil sands industry to begin commercial piloting for our AOS to help treat and remediate oil sands process-affected water (OSPW) found in tailings ponds in the Canadian oil sands, an application that currently has no good technical solution. We have recently applied for significant grant funding to re-initiate our work to help treat OSPW, and we will be notified about the status of our funding application in the coming months.

Our work is continually progressing to support a number of commercial applications, with a key focus on wastewater treatment, food processing, agriculture, and oil and gas. We are also at the early stages of evaluating opportunities in in the storm drain recapture/recycling, and drinking water. Our AOS is an award-winning invention that is supported by science and engineering financial support and grants from various federal and provincial funding agencies in Canada such as NSERC, NRC- IRAP, and Alberta Innovates.

Recent AOS Milestones

In late 2017 we acquired a team of engineers and formed our own engineering services company, BioLargo Engineering Science and Technologies, LLC, (“BLEST”) (see above for more details) to provide internal and external engineering services. BLEST is actively preparing a process engineering package for the AOS system. Major components of the package will include: design basis, process flow diagrams, piping and instrumentation diagrams, process control strategy document and materials of construction specifications. This work is underway.

Table of Contents

In early 2018 we have engaged in a series of important commercially focused activities around the AOS, including discussions with a series of industrial collaborators to do commercial piloting in 2018. We have also reengaged stakeholders in the Oil Sands industry for commercial piloting. We have begun negotiations with potential strategic partners from industry to perform commercial pilots with the intent use our AOS as a polishing step (replacing UV, electro-chlorination, or ozone) within their existing treatment trains (complete water treatment solutions). Importantly, we have designed and begun assembling our own proprietary water treatment train. We have also submitted and are currently submitting applications for a series of substantial government grants (totaling more than \$4M USD) to focus on specific targets in industry, like wastewater, food processing and oil and gas applications. We are narrowly focused on validating efficacy for a few specific client challenges to offer a re awarded a CA\$235,000 grant from the Canadian Government's Industrial Research Assistance Program (NRC-IRAP) to fund our first on-site pilot project. The pilot is intended to demonstrate the AOS' ability to disinfect and decontaminate water at high flow-rates, allowing for recycling, reuse, and/or safe water discharge. Moreover, continuous treatment and recycling of the processed water in this pilot project will allow for a comprehensive assessment of the long term economic advantage (both operating and capital costs) and conservation benefits of the AOS for both energy and water, in comparison with conventional wastewater treatment technologies. Ultimately, we expect the results of this pilot to lay an important foundation for the technical and business case that convinces future customers to purchase the AOS.

This is an important step for our AOS technology, as well as for our company. We are confident in our disruptive water treatment technology and have proven its treatment capabilities in the lab ad nauseum. However, a pilot project for the AOS, as with any technology, is crucial to prove its reliability to industry stakeholders as well the capital cost and operating costs of our technology at-scale. These data will be critical to pave the way for future market adoption. And, we have many other pilots in evaluation. Our R & D team has developed a novel configuration for the AOS that features a spiral design. Testing for the new design has been highly encouraging. Management believes it will continue to advance the scale-up to higher volume throughputs of water flow and enhances the AOS ability to be more compact and longer lasting in the field. This work is not complete, but management believes it does represent a significant step forward to achieving high throughput quality results.

Results of Operations—Comparison of the three months ended March 31, 2018 and 2017

Revenue

Our revenue from product sales for the three months ended March 31, 2018 increased by over 400% - to approximately \$225,000 - compared with the three months ended March 31, 2017 of approximately \$45,000. . The increase is due to an increase in the volume of sales of our CupriDyne Clean Industrial Odor Control product to landfills and waste processing operations, and of our Specimen Transport Solidifier pouches to the U.S. military. And, we are pleased to report that total sales generated in the first four and a half months of 2018 are approximately \$425,000. Our average monthly revenue has increased from approximately \$25,000 the first half of 2017, to almost \$60,000 the second half of 2017, to approximately \$95,000 per month thus far in 2018. Assuming sales continue at

this level, we would expect total revenue for Odor No More to exceed \$1,100,000 in 2018. However, we are expanding our sales force and infrastructure and attempting to scale our operations to increase sales significantly.

While management is optimistic that it can succeed in doing so, no assurances can be made of future revenues. We are optimistic for multiple reasons. First, we have experienced an increase in our government orders. Second, we were recently approved as the supplier for 100% of the regional locations operated by one of our large national waste management accounts. Sales for these locations are just now beginning. Third, we have been asked by multiple clients to submit bids to design, construct, install and service equipment and systems to expand the use of our product within their operations. If accepted, these bids will result in revenues from engineering services for the design/build aspects, as well as our future CupriDyne Clean sales. We have more than \$300,000 in bids out at the request of our clients and once completed, assuming we are awarded these bids, product sales would naturally increase as our clients expand the use of our products in these locations. Fourth, we are expanding our sales staff, and intend to continue to do so the remainder of the year. It is important to note that our sales staff is a combination of sales, account relationship management and operations field support. We are actively working with our customers to insure that our customers experience the optimal success with our products and our clients are appreciative and supportive of our company. While these new sales staff additions have already contributed to improving incremental sales, they are early and still in training. We would normally expect them to be able to generate meaningful revenues as they complete their training program over the first 5 - 6 months of work with the company. We plan to continue to grow our sales staff over the next 9 - 12 months assuming the continued demand for our products with our national accounts continues to expand and capital resources continue to be available.

Table of Contents

Sales of our CupriDyne Clean products generated approximately 50% of our revenue in the three months ended March 31, 2018 (approximately \$115,000), which is a comparable percentage to our year ended December 31, 2017 results. The majority of these sales are pursuant to our “National Purchasing Agreements” with two of the largest waste handling companies in the United States. Our CupriDyne Clean sales revenue increased due to an increase in the volume of sales resulting from continued market penetration and ongoing marketing and sales efforts. We continue to receive extremely positive feedback from our customers about our service, our product’s effectiveness, and its cost savings. In 2018, we have hired additional sales personnel and staff to support additional sales. Given the continued expansion with our national accounts, we continue to expect higher sales volume for the remainder of 2018. We do not yet have enough history or sales volume to identify trends or uncertainties related to our CupriDyne Clean sales, although we are discovering that landfills and transfer stations in colder climates generally have less of a need for odor control products during winter months. It is unclear whether this fact will materially affect our product sales.

Sales of our Specimen Transport Solidifier pouches to the U.S. Defense Logistics Agency generated approximately 45% of our revenue in the three months ended March 31, 2018 (approximately \$100,000), compared with approximately \$18,000 in the three months ended March 31, 2017. These sales were primarily through our distributor Downeast Logistics. The vast majority of these sales of our Specimen Transport Solidifier pouches are made through a bid process in response to a request for bids to which any qualified government vendor can respond. We cannot know in advance the frequency or size of such requests from the U.S. Government, or whether our bids will be successful, and as such we are uncertain as to our future revenues through this system.

Our engineering division generated approximately \$38,000 in revenue for the three months ended March 31, 2018. As this division started in late 2017, the three months ended March 31, 2017 does not provide a comparison; however, compared with the prior three months ended December 31, 2017, revenue increased by approximately 300% or \$26,000. The increase in this quarter over last is due to an increase in the number of client contracts and hours billed by our professional staff. Although we expect our engineering division to continue to increase revenues in the future, we do not expect similar quarter-to-quarter percentage increases.

Cost of Goods Sold and Services

Our cost of goods sold includes costs of raw materials, contract manufacturing, and other direct expenses related to the manufacturing of our products. As a percentage of gross sales, our costs of goods was 60% in the three months ended March 31, 2018, versus 49% in the three months ended March 31, 2017. This increase is partially attributed to the fact that a larger percentage of our sales came from government orders through our distributor at a lower margin than our other products. With the increase in our sales volume, we are starting to purchase some raw materials directly from manufacturers at increasingly more attractive prices, and we expect those savings to be reflected in higher margins in 2018.

Our cost of services includes costs of employee time, a portion of overhead, and, when applicable, cost of subcontractors.

Selling, General and Administrative Expense

Our Selling, General and Administrative (“SG&A”) expenses include both cash and non-cash expenses. Our total SG&A increased approximately \$115,000 (11%) in the three months ended March 31, 2018 compared to the same period in 2017. The largest components of our selling, general and administrative expenses included:

	March 31, 2017	March 31, 2018	% change	
Salaries and payroll-related expenses	\$326,193	\$450,964	38	%
Consulting expense	197,330	162,700	(18)	%
Professional fees	193,418	191,976	(1)	%
Investor relations	40,086	32,680	(18)	%

Table of Contents

Our salaries and payroll related expenses increased in the three months ended March 31, 2018 due to an increased level of activities related to our operations, including the formation of our engineering subsidiary and hiring of associated personnel in the second half of 2017, and a general increase in our activities and operations, as reflected in the increase in our sales revenue. Our consulting fees decreased in the three months ended March 31, 2018 due a reduction in the use of outside investor relation firms during that period. The Company has maintained investor relations support with internal personnel.

Research and Development

Research and development expenses increased \$130,393 (33%) for the three months ended March 31, 2018, as compared to the same period in 2017. These expenses increased in part as a result of the formation of our engineering subsidiary, where we have accelerated the work related to the scale-up, engineering and testing of our AOS technology.

Interest expense

Interest expense decreased \$121,228 (13%) for the three months ended March 31, 2018, as compared to the same period in 2017. Our interest expense decreased as we adjusted the discount on our convertible notes and line of credit which reduced interest expense for the three-month period. The decrease was offset by an increase in interest expense related to our outstanding debt. From March 31, 2017 through March 31, 2018, we increased our debt balance by approximately \$2,000,000. It now totals over \$7,500,000 on which we are paying interest. Subsequent to March 31, 2018 we converted \$5,447,758 debt to equity, and thus will no longer be incurring interest on these obligations. This amount is comprised of \$4,133,738 that was recently converted into equity, and \$1,314,380 that matures June 1, 2018, and for which we have the option to convert to equity. Our interest expense will be significantly higher during the three months ended June 30, 2018 as we will expense any remaining discount on the converted notes. Thereafter, we expect our interest expense to decrease by approximately \$150,000 per quarter, assuming no new debt agreement is entered into.

Net Loss

Net loss increased \$103,892 (4%) for the three months ended March 31, 2018, as compared to the same period in 2017. The net loss was somewhat offset by an increase in revenue, nevertheless, the net loss increased mainly due to the increased interest expense and to increased research and development expense. The net loss per share did not change as the increase in net loss was offset by the increase in common shares outstanding. We do not expect to generate revenues in amount significant enough for us to generate a profit in the foreseeable future. (See Part I, Item II, "Our Business", above.)

Liquidity and Capital Resources

We have been, and anticipate that we will continue to be, limited in terms of our capital resources. Our total cash and cash equivalents were approximately \$920,000 at March 31, 2018, a decrease of approximately \$70,000 since December 31, 2017.

The accompanying consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of our business. For the three months ended March 31, 2018, we had a net loss of approximately \$2,430,000. At March 31, 2018, we had current assets of approximately \$1,114,000, debt obligations maturing in 2018 for which we cannot compel the conversion to stock, except in limited circumstances, of \$930,000, additional debt obligations for which we can compel conversion into stock at maturity of approximately \$6,200,000, a working capital deficit of approximately \$3,939,000, and an accumulated deficit of approximately \$103,825,000. We expect our working capital deficit to decrease significantly in the three months ending June 30, 2018 as a result of the conversion of \$4,470,000 of convertible notes into stock on or prior to June 1, 2018. Ultimately, our ability to continue as a going concern is dependent upon our ability to attract significant new sources of capital, attain a reasonable threshold of operating efficiencies, and achieve profitable operations. These consolidated financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

Table of Contents

Cash and profits from our product sales are not sufficient to fund our operations. We have been required to financially support the operations of our subsidiaries, none of which are operating at a positive cash flow. Only one subsidiary, Clyra, has financing in place to fund operations for the immediate future. It is important to note that Clyra intends to pursue direct investment to support its further product development and go to market strategy. Sales of our CupriDyne Clean products are increasing, and our engineering subsidiary has begun generating revenue, but we do not expect those divisions to support the general corporate overhead in the immediate future. As such, we will be required to raise substantial additional capital to continue our operations and fund our future business plans. We are continually take steps to raise capital to fund our operations, including a current private securities offering, and a recent offer to holders of unit offering notes to reduce conversion and warrant exercise prices (see Part II, Item 2, below). Although we have in place a financing arrangement with Lincoln Park (see Note 4, of the Notes to the Consolidated Financial Statements), we are reluctant to utilize that instrument while our stock price is below \$0.25. During the three months ended March 31, 2018, we received approximately \$168,000 from sales of stock to Lincoln Park, and \$770,000 net proceeds from our private securities offerings.

As of March 31, 2018, we had approximately \$5,400,000 in principal amounts due on various debt obligations due in 2018 (see Note 5, “Debt Obligations”, of the Notes to the Consolidated Financial Statements), including approximately \$4,500,000 due on June 1, 2018, which we have the discretion to pay through the issuance of common stock, and \$930,000 due later in the year, for which our discretion to convert to equity is restricted by the price of our common stock. Since March 31, 2018, holders have agreed to convert to equity \$3,154,467 of obligations due June 1, 2018 (see Part II Item 2, “Conversion of Unit Offering Notes”, below). The remaining amount we intend to convert to equity at maturity. For the notes due later in the year in the aggregate amount of \$930,000, we are negotiating with the holders of those notes for extensions and/or alternative payment arrangements, and if unsuccessful, intend to refinance these obligations.

In addition to our financing arrangement with Lincoln Park, and the private securities offerings discussed above, we are continuing to explore alternatives for our current and longer-term financial requirements, including additional raises of capital from investors in the form of convertible debt or equity, and significant grant funding from government sources. It is unlikely that we will be able to qualify for bank or other financial institutional debt financing until such time as our operations are considerably more advanced and we are able to demonstrate the financial strength to provide confidence for a lender, which we do not currently believe is likely to occur for at least the next 12 months or more.

If we are unable to raise sufficient capital, we may be required to curtail some of our operations, including efforts to develop, test, market, evaluate and license our technologies and products. If we were forced to curtail aspects of our operations, there could be a material adverse impact on our financial condition and results of operations.

Critical Accounting Policies

Our unaudited interim consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America. Preparation of these statements requires management to make judgments and estimates. Some accounting policies have a significant impact on amounts reported in these financial statements. A summary of significant accounting policies and a description of accounting policies that are considered critical may be found in our Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on March 30, 2018, in the Notes to the Consolidated Financial Statements and the Critical Accounting Estimates sections. In addition, refer to Note 2 to the consolidated interim consolidated financial statements included in Part I, Item 1 of this report.

The methods, estimates, and judgments the Company uses in applying these most critical accounting policies have a significant impact on the results of the Company reports in its consolidated financial statements.

Table of Contents

It the Company's policy to expense share based payments as of the date of grant in accordance with Auditing Standard Codification Topic 718 "Share-Based Payment." Application of this pronouncement requires significant judgment regarding the assumptions used in the selected option pricing model, including stock price volatility and employee exercise behavior. Most of these inputs are either highly dependent on the current economic environment at the date of grant or forward-looking expectations projected over the expected term of the award. As a result, the actual impact of adoption on future earnings could differ significantly from our current estimate.

Recent Accounting Pronouncements

See Note 2, "Recent Accounting Pronouncements", to the Consolidated Financial Statements.

Item 4. Controls and Procedures

We conducted an evaluation, under the supervision and with the participation of management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of the end of the period covered by this Report.

Our procedures have been designed to ensure that the information relating to our company, including our consolidated subsidiaries, required to be disclosed in our SEC reports is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate to allow for timely decisions regarding required disclosure. However, our Company is continuing to grow and evolve. In 2017, we added an engineering division operating in Tennessee. The volume of our product sales continues to grow, increasing strain on our accounting systems. And, our operations do not yet generate enough cash to fund operations, and thus we rely on financing activities to maintain our level of operations and fund our anticipated growth. In combination, these activities put stress on our overall controls and procedures. Based on this evaluation, our chief executive officer and chief financial officer concluded that as of the evaluation date our disclosure controls and procedures were not effective, due to the material weakness identified below.

It should be noted that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions, regardless of how remote.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rules 13a-15(f) and 15d-15(f). Our internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures are being made only in accordance with authorizations of management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our assets that could have a material effect on the financial statements.

Table of Contents

Under the supervision and with the participation of our management, including our chief executive officer and the chief financial officer, we have established internal control procedures in accordance with the guidelines established in the 2013 Framework —Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (“COSO”). Recognizing the dynamic nature and growth of the Company’s business during the prior 12 months, including the addition of an engineering division, growth of the core operations, and the increase in the number of employees, management has recognized the strain on the overall internal control environment. As a result, management has concluded that its internal controls over financial reporting are not effective. Management identified a material weakness with respect to deficiencies in its financial closing and reporting procedures. Management believes this is due to a lack of resources. Management intends to add accounting personnel and operating staff and more sophisticated systems in order to improve its reporting procedures and internal controls, subject to available capital. A material weakness is a significant deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected. Although management is making progress related to remediating the material weakness, noted at December 31, 2017, it has not yet completed the work. There was no further change in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Our management, including our chief executive officer and chief financial officer, does not expect that our disclosure controls or our internal control over financial reporting, or any system we design or implement in the future, will prevent or detect all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system’s objectives will be met. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Table of Contents

PART II

OTHER INFORMATION

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Stock Issued for Services

During the three months ended March 31, 2018, we issued 144,545 shares of common stock in lieu of fees for service provided by consultants, resulting in a grant date fair value of \$82,480.

During the three months ended March 31, 2018, we issued 310,404 shares of common stock as payment for interest due on unit offering notes, resulting in a grant date fair value of \$178,929.

Issuance of Stock Options in exchange for payment of payables

On January 31, 2018, we issued options to purchase 18,071 shares of our common stock at an exercise price of \$0.28 per share, expiring 10 years from the date of grant. The fair value of these options total \$5,060 and is recorded as selling, general and administrative expenses.

On February 28, 2018, we issued options to purchase 21,429 shares of our common stock at an exercise price of \$0.28 per share expiring 10 years from the date of grant. The fair value of these options total \$6,000 and is recorded as selling, general and administrative expenses.

On March 31, 2018, we issued options to purchase 565,649 shares of our common stock at an exercise price of \$0.26 per share to members of our board of directors for services, an employee in lieu of salary, and to consultants for services. The fair value of these options totaled \$146,503 and is recorded as selling, general and administrative expenses.

Summer 2017 Unit Offering

On May 24, 2017, we commenced a private securities offering (titled the “Summer 2017 Unit Offering”) which offered the sale of \$1,500,000 of “Units,” each Unit consisting of a convertible promissory note and stock purchase warrant. On February 12, 2018, we issued Pricing Supplement No. 3, setting the unit/conversion price at \$0.30 per share, and the warrant exercise price at \$0.48 per share. The promissory notes issued to investors mature June 20, 2020, and bear interest at the rate of 12% per annum on the amount invested. Any interest due will be paid quarterly in arrears in cash or shares of common stock. If paid by the issuance of common stock, interest is paid at a conversion price equal to the average closing price of the Company’s common stock over the 20 trading days prior to the interest payment due date. The principal amount of the note may be paid by the issuance of shares of common stock, or cash, upon maturity at the Company’s election. Promissory notes may be converted at any time by the investor, at maturity by the Company, or by the Company prior to maturity, so long as the following conditions are met: (i) the Shares issued as payment are registered with the SEC; and (ii) the Company’s common stock closes for ten consecutive trading days at or above three times the Unit price.

In addition to the convertible promissory note, each investor receives a warrant allowing for the purchase of the number of shares of BioLargo common stock equal to the investment amount divided by the unit/conversion price (e.g., one warrant share for each share of common stock which the investor is eligible to receive through conversion of the note). (See Note 7.) The warrants expire on June 20, 2022. The Company may “call” the warrants, requiring the investor to exercise their warrants within 30 days or forever lose the rights to do so, only if the following conditions have been met: (i) the underlying Shares are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

Table of Contents

The offering was terminated on March 16, 2018. During the three months ended March 31, 2018, we received \$80,000 in investments from two accredited investors, and issued warrants to purchase 266,667 shares of common stock at \$0.48 per share.

The offering documents assured the investors that in the event a subsequent pricing supplement offered a lower conversion or exercise price, prior investors would be given those favorable terms. As a result of the issuance of the third pricing supplement, the unit prices for previous investors was reduced to \$0.30, and warrant exercise prices reduced to \$0.48. As a result of this reduction, the number of warrant shares available to each investor increased. (See Note 7.)

Spring 2018 Unit Offering

On March 26, 2018, we commenced a private securities offering (titled the “Summer 2017 Unit Offering”) which offered the sale of \$1,500,000 of “Units,” each Unit consisting of a convertible promissory note and stock purchase warrant. Concurrently, we issued Pricing Supplement No. 1., setting the initial unit/conversion price at \$0.30 per share, and the initial warrant exercise price at \$0.48 per share. The promissory notes issued to investors mature April 20, 2021, and bear interest at the rate of 12% per annum on the amount invested. Any interest due will be paid quarterly in arrears in cash or shares of common stock. If paid by the issuance of common stock, interest is paid at a conversion price equal to the average closing price of the Company’s common stock over the 20 trading days prior to the interest payment due date. The principal amount of the note may be paid by the issuance of shares of common stock, or cash, upon maturity at the Company’s election. Promissory notes may be converted at any time by the investor, at maturity by the Company, or by the Company prior to maturity, so long as the following conditions are met: (i) the Shares issued as payment are registered with the SEC; and (ii) the Company’s common stock closes for ten consecutive trading days at or above three times the Unit price.

In addition to the convertible promissory note, each investor received a warrant allowing for the purchase of the number of shares of BioLargo common stock equal to the investment amount divided by the unit/conversion price (e.g., one warrant share for each share of common stock which the investor is eligible to receive through conversion of the note). (See Note 7.) The warrants expire on April 20, 2023. The Company may “call” the warrants, requiring the investor to exercise their warrants within 30 days or forever lose the rights to do so, only if the following conditions have been met: (i) the underlying Shares are registered with the SEC and (ii) the Company’s common stock closes for 10 consecutive trading days at or above two times the exercise price.

From the inception of the offering through March 31, 2018, we had received \$100,000 in investments from one accredited investor. In addition to the convertible promissory note in face amount of \$100,000, this investor received a warrant to purchase 333,334 shares of our common stock at \$0.48 per share.

The offering documents assured the investors that in the event a subsequent pricing supplement offered a lower conversion or exercise price, prior investors would be given those favorable terms. On December 29, 2017, we issued a second pricing supplement, lowering the conversion price to \$0.394. As a result of this reduction, we notified each investor of the decrease in conversion price, and increased the number of warrant shares available to each investor. (See Note 7.)

Conversion of Unit Offering Notes

On May 7, 2018, we (BioLargo, Inc., the “Company”) issued 15,747,482 shares of our common stock in satisfaction of \$4,133,738 of convertible promissory notes issued in our “unit” offerings at varying conversion prices, maturing on the following dates:

Note Description	Principal Outstanding	Amount Converted to	Principal Amount
	March 31, 2018	Stock	Remaining
Convertible notes, mature June 1, 2018	\$ 4,468,847	\$(3,154,467)	\$ 1,314,380
Convertible notes, mature June 17, 2019	\$ 283,571	\$(283,571)	---
Convertible notes, mature December 31, 2019	\$ 292,000	\$(217,000)	\$ 75,000
Convertible notes, mature June 20, 2020	\$ 603,700	\$(478,700)	\$ 125,000

These conversions were voluntary on the part of the noteholders and prior to the various maturity dates on notes that were issued in prior “unit” offerings conducted by the Company (2015 Unit Offering, Winter 2016 Unit Offering, and Summer 2017 Unit Offering). We offered these noteholders incentives to convert their notes early. Noteholders with conversion prices of \$0.25 and \$0.30 were offered incentive shares equal to one and one-half times the number of shares issuable for the payment of interest that would accrue from the last interest payment date of March 20, 2018, through the maturity of the note, at a fixed price of \$0.25 per share (for example, a note that would have yielded \$1,000 in interest, would receive 1,000 times 1.5 divided by 0.25 equals 6,000 incentive shares). We offered holders of notes with conversion prices higher than \$0.30 the ability to reduce their conversion price to \$0.30 by paying additional funds equal to six or twenty percent of their original investment (6% for notes with original conversion prices of \$0.35, and 20% for notes with original conversion prices of \$0.55 and \$0.57). The additional funds did not increase the amount of the note payable, nor did the reduced conversion price affect the number of shares purchasable under the warrant issued with their “unit” investment. Holders of 38 notes elected to pay an aggregate \$261,781 to reduce the conversion prices of their notes to \$0.30.

All of these offerings and sales were made in reliance on the exemption from registration contained in Section 4(2) of the Securities Exchange Act and/or Regulation D promulgated thereunder as not involving a public offering of securities.

Table of Contents

FirstFire Global Opportunity Fund Investment

On January 16, 2018, we entered into a securities purchase agreement (the “FirstFire Purchase Agreement”) and a registration rights agreement (the “FirstFire RRA”) with FirstFire Global Opportunity Fund, LLC (“FirstFire”), and issued a convertible promissory note (the “FirstFire Note”) in the aggregate principal amount of \$150,000 at 5% annual interest, which is convertible into shares of common stock of the Company at \$0.394 per share, subject to the terms, and certain limitations and conditions set forth in the FirstFire Purchase Agreement and FirstFire Note. FirstFire may convert the FirstFire Note at any time. The Company may require the conversion of the FirstFire Note in the event the Company’s common stock has traded at a price per share of \$0.75 or above for the ten trading days immediately preceding the mandatory conversion, and the shares underlying the conversion are subject to an effective registration statement filed with the SEC. The FirstFire Note matures on October 16, 2018.

Pursuant to the FirstFire Purchase Agreement, the Company issued 75,000 shares of common stock to FirstFire as a commitment fee (the “FirstFire Commitment Shares”).

Under the Note and FirstFire Purchase Agreement, the Company has reserved 394,949 shares of common stock for issuance upon conversion of the Note. Pursuant to the FirstFire RRA, the Company agreed to file a registration statement with the SEC registering all shares of common stock into which the FirstFire Note is convertible, and the FirstFire Commitment Shares. The FirstFire Purchase Agreement allows for an adjustment to the number of FirstFire Commitment Shares in the event the closing price of our common stock, on the earlier of the date the registration statement is deemed effective and 20 trading days following the six-month anniversary of the FirstFire Note, is lower than the closing price on January 16, 2018 (which was \$0.39). In such event, additional shares would be issued to FirstFire such that the aggregate FirstFire Commitment Shares issued have the same value as the shares issued on January 16, 2018.

FirstFire represented to the Company, among other things, that it was an “accredited investor” (as such term is defined in Rule 501(a) of Regulation D under the Securities Act of 1933, as amended). The FirstFire Note, FirstFire Purchase Agreement, and the FirstFire RRA contain customary representations, warranties, agreements and conditions including indemnification rights and obligations of the parties. The FirstFire Note contains a price protection provision such that if we issue a security with any term more favorable to the holder of such security that was not similarly provided in the FirstFire Note, then the Company shall notify FirstFire of such additional or more favorable term and such term, at its option, shall become a part of the FirstFire Note.

We expect that proceeds from the FirstFire Note will be used for working capital and general corporate purposes.

Registration of Shares underlying Vista and FirstFire Investments

On December 18, 2017, we entered into the Vista Purchase Agreement and Vista RRA (see Note 5, “Convertible Note, matures September 18, 2018 (Vista Capital)”.) On January 16, 2018, we entered into the FirstFire Purchase Agreement and FirstFire RRA on similar terms as the Vista Purchase Agreement and Vista RRA.(See Note 13, “FirstFire Global Opportunity Fund Investment”.)

Pursuant to the requirements set forth in the registration rights agreements, we filed a registration statement with the SEC which was deemed effective as of February 8, 2018. On February 8, 2018, our common stock last traded at \$0.31 per share. Because the last traded price of our common stock on the date the registration statement was deemed effective was less than the price of our common stock on the dates of the Vista and FirstFire Purchase Agreements, at their option, we are required to issue additional “commitment shares”. Both companies have exercised that right, and we issued 140,849 and 36,536 additional shares of our common stock to Vista Capital and FirstFire, respectively.

Item 5. Other Information

Sales of Registered Stock to Lincoln Park

During the three months ended March 31, 2018, we sold to Lincoln Park (see Note 4) 650,000 shares of our common stock, and received \$168,220 in proceeds. Associated with these sales, we issued Lincoln Park 8,226 “additional commitment shares.”

Table of Contents

Item 6. Exhibits

The exhibits listed in the Exhibit Index following the signature pages of this Quarterly Report on Form 10-Q are filed with, or furnished with, or incorporated by reference in, this Quarterly Report on Form 10-Q.

SIGNATURES

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

BIOLARGO, INC.

Date: May 14, 2018 By: /s/ DENNIS P. CALVERT
Dennis P. Calvert

Chief Executive Officer

Date: May 14, 2018 By: /s/ CHARLES K. DARGAN, II
Chief Financial Officer

Table of Contents**EXHIBIT INDEX**

<u>Exhibit Number</u>	<u>Exhibit Description</u>	<u>Incorporated by Reference Herein</u>	
		<u>Form</u>	<u>File Date</u>
3.1	<u>Bylaws of BioLargo, Inc., as amended and restated</u>	Form 10-KSB	5/23/2003
3.2	<u>Amended and Restated Certificate of Incorporation for BioLargo, Inc. filed March 16, 2007</u>	Form 10-KSB	5/4/2007
4.1	<u>Form of Convertible Promissory Note issued in 2015 Unit Offering</u>	Form 10-K3/31/2015	
4.2	<u>Form of Series A Stock Purchase Warrant issued in 2015 Unit Offering</u>	Form 10-K3/31/2015	
4.3	<u>Form of Stock Options issued in exchange for reduction in accounts payable.</u>	Form 10-K3/31/2015	
4.4	<u>Amended and Restated Articles of Incorporation of Clyra Medical Technologies, Inc.</u>	Form 8-K	1/6/2016
4.5	<u>Form of Warrant issued to One Year Note holder in July 2016</u>	Form 10-Q8/15/2016	
4.6	<u>Form of Note Issued in Winter 2016 Unit Offering</u>	Form S-1	1/25/2017
4.7	<u>Form of Warrant Issued in Winter 2016 Unit Offering</u>	Form S-1	1/25/2017
4.8	<u>Form of Warrant issued to One Year Note holder dated December 30, 2016</u>	Form S-1	1/25/2017
4.9	<u>Option to purchase common stock issued to Dennis P. Calvert dated May 2, 2017</u>	Form 8-K	5/4/2017
4.10	<u>Form of Note issued in Summer 2017 Offering</u>	Form 10-Q8/14/2017	
4.11	<u>Form of Warrant issued in Summer 2017 Offering</u>	Form 10-Q8/14/2017	
4.12	<u>Form of One-Year Note issued July 2017</u>	Form 10-Q8/14/2017	
4.13	<u>Form of Warrant issued to One-Year Noteholder July 2017</u>	Form 10-Q8/14/2017	
4.14	<u>\$440,000 convertible note, matures July 20, 2019</u>	Form 10-Q8/14/2017	
4.15	<u>Securities Purchase Agreement, dated as of December 14, 2017 by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 8-K	12/22/2017
4.16	<u>Registration Rights Agreement, dated as of December 14, 2017, by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 8-K	12/22/2017
4.17	<u>Note, dated as of December 14, 2017, by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 8-K	12/22/2017
4.18	<u>Amendment, dated as of December 18, 2017, by and between BioLargo, Inc. and Vista Capital Investments, LLC.</u>	Form 8-K	12/22/2017
4.19	<u>Stock Option dated December 31, 2017, issued to Chief Financial Officer Charles K. Dargan II</u>	Form 8-K	1/3/2018
4.20	<u>Purchase Agreement, dated as of August 25, 2017 by and between BioLargo, Inc. and Lincoln Park Capital Fund, LLC</u>	Form 8-K	8/31/2017
4.21	<u>Registration Rights Agreement, dated as of August 25, 2017, by and between BioLargo, Inc. and Lincoln Park Capital Fund, LLC</u>	Form 8-K	8/31/2017
4.22*	<u>Line of credit, matures September 1, 2019</u>		
4.23*	<u>Warrant issued with Line of credit that matures September 1, 2019</u>		
4.24*	<u>\$50,000 convertible note, matures March 8, 2020</u>		
4.25*	<u>Form of convertible notes that mature April 20, 2021 (Spring 2018 Offering)</u>		
4.26*	<u>Form of warrant issued with Convertible notes that mature April 20, 2021 (Spring 2018 Offering)</u>		
4.27*	<u>Amendment to \$440,000 convertible notes that matures July 20, 2019</u>		

Edgar Filing: BIOLARGO, INC. - Form 10-Q

10.1†	<u>February 10, 2017 extension to Engagement Extension Agreement with Charles K. Dargan, II.</u>	Form 8-K 2/14/2017
10.2†	<u>Employment Agreement with Dennis P. Calvert dated May 2, 2017.</u>	Form 8-K 5/4/2017
10.3†	<u>Lock-Up Agreement with Dennis P. Calvert dated April 30, 2017</u>	Form 8-K 5/4/2017
10.4†	<u>Lock-Up Agreement with Dennis P. Calvert dated May 2, 2017.</u>	Form 8-K 5/4/2017
10.5†	<u>Engagement Agreement extension dated December 31, 2017, between BioLargo, Inc. and Charles K. Dargan, II</u>	Form 8-K 1/3/2018
31.1*	<u>Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and Rules 13(a)-14 and 15(d)-14 under the Securities Exchange Act of 1934</u>	
31.2*	<u>Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and Rules 13(a)-14 and 15(d)-14 under the Securities Exchange Act of 1934</u>	
32*	<u>Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.</u>	
101.INS**	XBRL Instance	
101.SCH**	XBRL Taxonomy Extension Schema	
101.CAL**	XBRL Taxonomy Extension Calculation	
101.DEF**	XBRL Taxonomy Extension Definition	
101.LAB**	XBRL Taxonomy Extension Labels	
101.PRE**	XBRL Taxonomy Extension Presentation	

* Filed herewith

** Furnished herewith

† Management contract or compensatory plan, contract or arrangement