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

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2018

OR

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

For the transition period from _____ to _____

Commission file number 0-21617

ProPhase Labs, Inc.

(Exact name of registrant as specified in its charter)

Delaware	23-2577138
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
621 N. Shady Retreat Road, Doylestown, Pennsylvania	18901
(Address of principal executive office)	(Zip Code)

(215) 345-0919

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer [ ] Accelerated filer [ ] Non-accelerated filer [ ] Smaller reporting company [X]
Emerging growth company [ ]

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 17, 2018
Common Stock, $0.0005 par value	11,542,045

ProPhase Labs, Inc. and Subsidiaries

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

ProPhase Labs, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(in thousands, except share and per share amounts)

	June 30, 2018 (unaudited)	December 31, 2017
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents (Note 2)	$ 3,665	$ 3,173
Marketable securities, available for sale	6,776	18,765
Escrow receivable, current portion (Note 8)	5,000	2,500
Accounts receivable, net (Note 2)	1,363	1,945
Inventory (Note 2)	2,386	1,531
Prepaid expenses and other current assets (Note 2)	357	481
Assets held for sale, discontinued operations (Note 3)	-	22
Total current assets	19,547	28,417
Property, plant and equipment, net of accumulated depreciation of $5,661 and $5,471, respectively (Note 2)	2,576	2,742
Escrow receivable (Note 8)	-	2,500
Total assets	$ 22,123	$ 33,659
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 445	$ 562
Accrued advertising and other allowances (Note 2)	98	200
Other current liabilities (Note 7)	1,052	1,050
Total current liabilities	1,595	1,812
COMMITMENTS AND CONTINGENCIES (Note 8)	-	-
STOCKHOLDERS' EQUITY		
Preferred stock, authorized 1,000,000, $.0005 par value, no shares issued (Note 5)	-	-
Common stock, $.0005 par value; authorized 50,000,000; issued: 28,101,272 and 26,313,593 shares, respectively (Note 5)	14	14
Additional paid-in-capital	58,606	58,034
Retained earnings	8,986	20,902
Treasury stock, at cost, 16,566,701 and 16,566,701 shares (Note 5)	(47,025)	(47,025)
Accumulated comprehensive loss	(53)	(78)
Total stockholders' equity	20,528	31,847
Total liabilities and stockholders' equity	$ 22,123	$ 33,659

See accompanying notes to condensed consolidated financial statements

ProPhase Labs, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(in thousands, except per share amounts)
(unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Net sales (Note 2)	$ 3,186	$ 1,905	$ 6,594	$ 2,676
Cost of sales (Note 2)	1,928	1,765	3,910	2,451
Gross profit	1,258	140	2,684	225
Operating expenses (Note 2):				
Sales and marketing	235	221	407	336
Administration	1,200	1,306	2,419	2,387
Research and development	87	224	174	258
	1,522	1,751	3,000	2,981
Interest income, net	4	151	100	97
Loss from continuing operations before income taxes (Note 6)	(260)	(1,460)	(216)	(2,659)
Income tax benefit from continuing operations	-	574	-	1,027
Loss from continuing operations	(260)	(886)	(216)	(1,632)
Discontinued operations (Note 3):				
Income (loss) from discontinued operations	-	(835)	-	530
Gain (loss) on sale of discontinued operations, net of taxes	-	(584)	-	42,684
Income (loss) from discontinued operations	-	(1,419)	-	43,214
Net income (loss)	$ (260)	$ (2,305)	$ (216)	$ 41,582
Other comprehensive income (loss):				
Unrealized gain on marketable securities	68	-	25	-
Total comprehensive income (loss)	$ (192)	$ (2,305)	$ (191)	$ 41,582
Basic earnings per share:				
Loss from continuing operations	$ (0.02)	$ (0.06)	$ (0.02)	$ (0.10)
Income (loss) from discontinued continued operations	-	(0.08)	-	2.54
Net income (loss)	$ (0.02)	$ (0.14)	$ (0.02)	$ 2.44
Diluted earnings per share:				
Loss from continuing operations	$ (0.02)	$ (0.06)	$ (0.02)	$ (0.10)
Income (loss) from discontinued continued operations	-	(0.08)	-	2.44
Net (loss) income	$ (0.02)	$ (0.14)	$ (0.02)	$ 2.34
Weighted average common shares outstanding:				
Basic	11,339	16,943	11,237	17,030
Diluted	11,339	16,943	11,237	17,680

See accompanying notes to condensed consolidated financial statements

ProPhase Labs, Inc. and Subsidiaries
Condensed Consolidated Statement of
Stockholders' Equity
(in thousands, except share data)
(unaudited)

	Common Stock Shares Outstanding, Net of Shares of Treasury Stock	Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Comprehensive Loss	Treasury Stock	Total
Balance at December 31, 2017	11,129,892	$ 14	$ 58,034	$ 20,902	$ (78)	$ (47,025)	$ 31,847
Net loss	-	-	-	(216)	-	-	(216)
Unrealized gain on marketable securities	-	-	-	-	25	-	25
Cash dividends	-	-	-	(11,700)	-	-	(11,700)
Proceeds from warrants exercised	-	-	-	-	-	-	-
Proceeds from options exercised	404,679	-	338	-	-	-	338
Share-based compensation	-	-	234	-	-	-	234
Balance at June 30, 2018	11,534,571	$ 14	$ 58,606	$ 8,986	$ (53)	$ (47,025)	$ 20,528

See accompanying notes to condensed consolidated financial statements

ProPhase Labs, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

	Six Months Ended	
	June 30, 2018	June 30, 2017
Cash flows from operating activities:		
Net income (loss)	$ (216)	$ 41,582
Adjustments to reconcile net income/loss to net cash used in operating activities:		
Realized gain from maturity of marketable securities	100	-
Gain on sale of assets, net of income taxes	-	(42,684)
Income tax benefit	-	(1,027)
Depreciation and amortization	190	419
Amortization of loan origination and warrant expenses	-	10
Share-based compensation expense	234	18
Changes in operating assets and liabilities:		
Accounts receivable	582	3,935
Inventory	(855)	770
Prepaid and other assets	132	(169)
Accounts payable	(117)	(1,240)
Accrued advertising and other allowances	(102)	(1,254)
Other current liabilities	10	(1,450)
Due to Mylan, Inc. and affiliates	(17)	717
Assets held for sale, discontinued operations	22	(294)
Net cash used in operating activities	(37)	(667)
Cash flows from investing activities:		
Purchases of marketable securities	(9,589)	-
Proceeds from maturities of marketable securities	11,930	-
Proceeds from sale of marketable securities	9,574	-
Net proceeds from the sale of assets	-	40,825
Capital expenditures	(24)	(132)
Net cash provided by investing activities	11,891	40,693
Cash flows from financing activities:		
Payment of dividends	(11,700)	-
Payments to retire secured promissory notes	-	(1,500)
Payments to acquire treasury stock		(1,858)
Proceeds from exercise of warrants and stock options	338	171
Net cash used in financing activities	(11,362)	(3,187)
Net increase in cash and cash equivalents	492	36,839
Cash and cash equivalents at beginning of period	3,173	441
Cash and cash equivalents at end of period	$ 3,665	$ 37,280
Supplemental disclosures of cash flow information		
Interest paid	$ -	$ 54
Income taxes paid	$ -	$ 1,350
Non-cash investing activities:		
Net unrealized gain, investments in marketable securities	$ 25	$ -

See accompanying notes to condensed consolidated financial statements

Note 1 – Organization and Business

ProPhase Labs, Inc. ("we", "us" or the "Company") was initially organized as a corporation in Nevada in July 1989. Effective June 18, 2015, we changed our state of incorporation from the State of Nevada to the State of Delaware. We are a vertically integrated and diversified branding, marketing and technology company engaged in the research, development, manufacture, distribution, marketing and sale of over-the-counter ("OTC") consumer healthcare products, dietary supplements and other remedies in the United States. This includes the development and marketing of dietary supplements under the TK Supplements® brand.

In August 2017, we formed ProPhase Digital Media, Inc. ("PDM"), a Delaware corporation and wholly-owned subsidiary. Our objective is for PDM to become an independent full-service direct marketing agency. PDM's first initiative will be to market the TK Supplements® product line. If successful, this may lead to the marketing of other companies' consumer products.

In addition, we also continue to actively pursue acquisition opportunities for other companies, technologies and products within and outside the consumer products industry.

We use a December 31 year-end for financial reporting purposes. References herein to "Fiscal 2018" shall mean the fiscal year ended December 31, 2018 and references to other "Fiscal" years shall mean the year, which ended on December 31 of the year indicated. The term "we", "us" or the "Company" as used herein also refer, where appropriate, to the Company, together with its subsidiaries and consolidated variable interest entities unless the context otherwise requires.

Discontinued Operations

Prior to March 29, 2017, our flagship OTC drug brand was Cold-EEZE® and our principal product was Cold-EEZE® cold remedy zinc gluconate lozenges. In addition to Cold-EEZE® cold remedy lozenges, we also marketed and distributed non-lozenge forms of our proprietary zinc gluconate formulation, (i) Cold-EEZE® cold remedy QuickMelts®, (ii) Cold-EEZE® Gummies and (iii) Cold-EEZE® cold remedy oral spray.

Effective March 29, 2017, we sold our intellectual property rights and other assets related to our Cold-EEZE® brand and product line, including all then current and pipeline over-the-counter allergy, cold, flu, multi-symptom relief and immune support treatments for adults and children to the extent each was, or was intended to be, branded "Cold-EEZE®", including all formulations and derivatives thereof (collectively referred to as the "Cold-EEZE® Business") to Mylan Consumer Healthcare Inc. (formerly known as Meda Consumer Healthcare Inc.) ("MCH") and Mylan Inc. (together with MCH, "Mylan"). As a result of the sale of the Cold-EEZE® Business, for the three and six months ended June 30, 2017, we have classified as discontinued operations (i) all income and expenses attributable to the Cold-EEZE® Business, (ii) the gain from the sale of the Cold-EEZE® Business, and (iii) the income tax expense attributed to the sale of the Cold-EEZE® Business. Excluded from the sale of the Cold-EEZE® Business were our accounts receivable and inventory. We have also retained all liabilities associated with our Cold-EEZE® Business operations arising prior to March 29, 2017.

Continuing Operations

We continue to own and operate our manufacturing facility and manufacturing business in Lebanon, Pennsylvania, and our headquarters in Doylestown, Pennsylvania. As part of the sale of the Cold-EEZE® Business, we entered into a manufacturing agreement (see Note 8) with Mylan and our wholly-owned subsidiary, Pharmaloz Manufacturing, Inc. ("PMI"), to supply various Cold-EEZE® lozenge products to Mylan. In addition to the production services we provide to Mylan under the manufacturing agreement, we produce OTC healthcare and dietary supplement products for other third-party customers in addition to performing operational tasks such as warehousing, customer order processing and shipping.

We are also pursuing a series of new product development and pre-commercialization and market testing initiatives in the OTC dietary supplement category. Initial OTC dietary supplement product development activities were completed in the fourth quarter of Fiscal 2015 under the brand name of TK Supplements®. The TK Supplements® product line comprises three men's health products: (i) Legendz XL® for sexual health, (ii) Triple Edge XL®, an energy booster plus testosterone support, and (iii) Super ProstaFlow Plus™ for prostate and urinary health. In addition to developing direct-to-consumer ("Direct Response") marketing strategies for Legendz XL®, we received initial product acceptance and shipped into a national chain drug retailer and to several regional retailers during Fiscal 2017.

Note 2 – Summary of Significant Accounting Policies

For the three and six months ended June 30, 2018 and 2017, our revenues from continuing operations have come principally from contract manufacturing OTC health care and dietary supplement products for third parties.

Basis of Presentation

The unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial statements and within the rules of the Securities and Exchange Commission ("SEC") applicable to interim financial statements and therefore do not include all disclosures that might normally be required for financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP"). The accompanying unaudited condensed consolidated financial statements have been prepared by management without audit and should be read in conjunction with our consolidated financial statements, including the notes thereto, appearing in our Annual Report, as amended on Form 10-K for the fiscal year ended December 31, 2017. In the opinion of management, all adjustments necessary for a fair presentation of the consolidated financial position, consolidated results of operations and consolidated cash flows, for the periods indicated, have been made. The results of operations for the three and six months ended June 30, 2018 are not necessarily indicative of operating results that may be achieved over the course of the full year.

Discontinued Operations Carve Out and ProPhase Allocations

For the three and six months ended June 30, 2017, results from operations for our Cold-EEZE® Business are classified as discontinued operations. The carve out of the discontinued operations (i) were prepared in accordance with the SEC's carve out rules under Staff Accounting Bulletin ("SAB") Topic 1B1 and (ii) are derived from identifying and carving out the specific assets, liabilities, net sales, cost of sales, operating expenses and interest expense associated with the Cold-EEZE® Business's operations. General administrative and overhead expenses, including personnel expenses and bonuses, and research and development overhead expenses incurred by us (for which the discontinued operation benefits from such resources) are allocated to discontinued operations based upon the percentage of the Cold-EEZE® Business's net sales to our consolidated net sales. For the three months ended June 30, 2017, we allocated (i) $319,000 of administrative expenses and (ii) $48,000 of research and development expenses, to discontinued operations in the accompanying condensed statements of operations. For the six months ended June 30, 2017, we allocated $348,000 of administrative expenses and $52,000 of research and development expenses to discontinued operations in the accompanying condensed statements of operations (see Note 3). There were no discontinued operations for the three and six months ended June 30, 2018.

Product Innovation, Seasonality of the Business and Liquidity

Our net sales are derived principally from our contract manufacturing of OTC healthcare and dietary supplements products in the United States. In addition, we are engaged in early stage commercialization and market testing activities for the TK Supplements® product line of dietary supplements.

Our sales are influenced (i) by market acceptance of our TK Supplement® products and fluctuations in the timing of purchase and (ii) by the ultimate level of demand for our contract manufactured OTC healthcare and dietary supplement products which are a function of the timing, length and severity of each cold season. Generally, a cold season is defined as the period of September to March when the incidence of the common cold rises as a consequence of the change in weather and other factors. We generally experience in the first, third and fourth quarter higher levels of net sales.

As a consequence of the scope and timing of our TK Supplements® product market launch and the seasonality of our contract manufacturing OTC business, we realize variations in operating results and demand for working capital from quarter to quarter. As of June 30, 2018, we had working capital of approximately $18.0 million, including $6.8 million marketable securities available for sale. We believe our current working capital at June 30, 2018 is at an acceptable and adequate level to support our business for at least the next twelve months.

Note 2 – Summary of Significant Accounting Policies – continued

Use of Estimates

The preparation of financial statements and the accompanying notes thereto, in conformity with GAAP, requires management to make estimates and assumptions that affect reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the respective reporting periods. Examples include the provision for bad debt, sales returns and allowances, inventory obsolescence, useful lives of property and equipment and intangible assets, impairment of property and equipment and intangible assets, income tax valuations and assumptions related to accrued advertising. These estimates and assumptions are based on historical experience, current trends and other factors that management believes to be relevant at the time the financial statements are prepared. Management reviews the accounting policies, assumptions, estimates and judgments on a quarterly basis. Actual results could differ from those estimates.

Cash and Cash Equivalents

We consider all highly liquid investments with a maturity of three months or less at the time of purchase to be cash equivalents. Cash equivalents include cash on hand and monies invested in money market funds. The carrying amount approximates the fair market value due to the short-term maturity of these investments.

Marketable Securities

We have classified our investments in marketable securities as available-for-sale and as a current asset. Our investments in marketable securities are carried at fair value, with unrealized gains and losses included as a separate component of stockholders' equity. Realized gains and losses from our marketable securities are recorded as other income (expense). We initiated short term investments in marketable securities, which carry maturity dates between one and three years from date of purchase with interest rates of 2.25% - 3.05%, during the first half of Fiscal 2018. For the six months ended June 30, 2018, we reported an unrealized gain of $25,000 and an accumulated unrealized loss of $53,000. Unrealized gains and losses are classified as other comprehensive income (loss) and the cost is determined on a specific identification basis. The following is a summary of the components of our marketable securities and the underlying fair value input level tier hierarchy (see long-lived assets below) (in thousands):

	December 31, 2017				June 30, 2018			
	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value
U.S. treasuries	$ 1,744	-	-	1,744	929	-	-	929
Corporate bonds	16,943	-	(78)	17,021	5,900		(53)	5,847
	$ 18,687	$ -	$ (78)	$ 18,765	$ 6,829	$ -	$ (53)	$ 6,776

Inventory

Inventory is valued at the lower of cost, determined on a first-in, first-out basis (FIFO), or net realizable value. Inventory items are analyzed to determine cost and the net realizable value and appropriate valuation adjustments are established. At June 30, 2018, after the 2018 write-off of certain inventory previously recorded, the financial statements include adjustments to reduce inventory for excess, obsolete or short-dated shelf-life inventory of $495,000, inclusive of adjustments of $144,000 for product samples of TK Supplements® products. At December 31, 2017, the financial statements include adjustments to reduce inventory for excess, obsolete or short-dated shelf-life inventory of $1.1 million, inclusive of an adjustment of $541,000 for product samples of TK Supplements® products.

Note 2 – Summary of Significant Accounting Policies – continued

The components of inventory are as follows (in thousands):

	June 30, 2018	December 31, 2017
Raw materials	$ 1,383	$ 1,269
Work in process	466	245
Finished goods	537	17
	$ 2,386	$ 1,531

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. We use the straight-line method in computing depreciation for financial reporting purposes. Depreciation expense is computed in accordance with the following ranges of estimated asset lives: building and improvements – ten to thirty-nine years; machinery and equipment – three to seven years; computer equipment and software – three to five years; and furniture and fixtures – five years.

Concentration of Risks

Future revenues, costs, margins and profits will continue to be influenced by our ability to maintain our manufacturing availability and capacity together with our marketing and distribution capabilities and the regulatory requirements associated with the development of OTC consumer healthcare products, dietary supplements and other remedies in order to compete on a national level and/or international level.

Our business is subject to federal and state laws and regulations adopted for the health and safety of users of our products. The manufacturing and distribution of OTC healthcare and dietary supplement products are subject to regulations by various federal, state and local agencies, including the Food and Drug Administration ("FDA") and, as applicable, the Homeopathic Pharmacopoeia of the United States.

Financial instruments that potentially subject us to significant concentrations of credit risk consist principally of cash investments, marketable securities, and trade accounts receivable. Our marketable securities are fixed income investments, which are highly liquid and can be readily purchased or sold through established markets.

We maintain cash and cash equivalents with certain major financial institutions. As of June 30, 2018, our cash and cash equivalents balance was $3.7 million and our bank balance was $3.8 million. Of the total bank balance, $500,000 was covered by federal depository insurance and $3.3 million was uninsured at June 30, 2018.

Trade accounts receivable potentially subject us to credit concentrations from time-to-time as a consequence of the timing, payment pattern and ultimate purchase volumes or shipping schedules with our customers. We extend credit to our customers based upon an evaluation of the customer's financial condition and credit history and generally we do not require collateral. Our customers include consumer products companies and large national chain, regional, specialty and local retail stores. These credit concentrations may impact our overall exposure to credit risk, either positively or negatively, in that our customers may be similarly affected by changes in economic, regulatory or other conditions that may impact the timing and collectability of amounts due to us. As a consequence of an evaluation of our customer's financial condition, payment patterns, balance due to us and other factors, we did not offset our account receivable with an allowance for bad debt at June 30, 2018 and December 31, 2017.

Note 2 – Summary of Significant Accounting Policies – continued

Long-lived Assets

We review our carrying value of our long-lived assets with definite lives whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. When indicators of impairment exist, we determine whether the estimated undiscounted sum of the future cash flows of such assets is less than their carrying amounts. If less, an impairment loss is recognized in the amount, if any, by which the carrying amount of such assets exceeds their respective fair values. The determination of fair value is based on quoted market prices in active markets, if available, or independent appraisals; sales price negotiations; or projected future cash flows discounted at a rate determined by management to be commensurate with our business risk. The estimation of fair value utilizing discounted forecasted cash flows includes significant judgments regarding assumptions of revenue, operating and marketing costs; selling and administrative expenses; interest rates; property and equipment additions and retirements; industry competition; and general economic and business conditions, among other factors.

Fair value is based on the prices that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, a three-tier fair value hierarchy prioritizes the inputs used to measure fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs for which little or no market data exists, therefore requiring an entity to develop its own assumptions.

Fair Value of Financial Instruments

Cash and cash equivalents, marketable securities, accounts receivable, assets held for sale, accounts payable, and accrued expenses are reflected in the Condensed Consolidated Financial Statements at carrying value which approximates fair value. We account for our marketable securities at fair value pursuant to Accounting Standards Codification, or ASC, 820-10, with the net unrealized gains or losses reported as a component of accumulated other comprehensive income or loss.

	As of June 30, 2018			
	Level 1	Level 2	Level 3	Total
Marketable securities				
U.S. government obligations	$ -	$ 929	$ -	$ 929
Corporate obligations	-	5,847	-	5,847
	$ -	$ 6,776	$ -	$ 6,776

Revenue Recognition

We account for revenue in accordance with ASC Topic 606, which requires revenue recognized to represent the transfer of promised goods or services to customers at an amount that reflects the consideration which is expected to be received in exchange for those goods or services. The Company recognizes revenue when its performance obligations with its customers have been satisfied. At contract inception, the Company determines if a contract is within the scope of Topic 606 and then evaluates the contract using the following five steps: (1) identify the contract with the customer; (2) identify the performance obligations; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations; and (5) recognize revenue when (or as) the entity satisfies a performance obligation.

We have not made any significant changes to judgments in applying ASC 606 during the three or six months ended June 30, 2018.

Performance Obligations

We generate sales principally through two types of customers, contract manufacturing and retail customers. Sales from product shipments to contract manufacturing and retailer customers are recognized at the time ownership is transferred to the customer. Net sales from contract manufacturing and retail customers were $3.1 million and $80,000, respectively, for the three months ended June 30, 2018 and $1.9 million and $46,000, respectively, for the three months ended June 30, 2017. Net sales from contract manufacturing and retail customers was $6.4 million and $154,000, respectively, for the six months ended June 30, 2018 and $2.6 million and $64,000, respectively, for the six months ended June 30, 2017. Revenue from retailer customers is reduced for trade promotions, estimated sales returns, cash discounts and other allowances in the same period as the related sales are recorded. No such allowance is applicable to our contract manufacturing customers. We make estimates of potential future product returns and other allowances related to current period revenue. We analyze historical returns, current trends, and changes in customer and consumer demand when evaluating the adequacy of the sales returns and other allowances.

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer and is the unit of account in ASC 606. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. The combined duties and responsibilities within each contract will be considered one single performance obligation under ASC 606 as these items would not be separately identifiable from each other promise in the contract and we provide a significant service of integrating the duties with other promises in the contracts.

Transaction Price

The transaction price is fixed based upon either (i) a combined Master Agreement and each related purchase order, or (ii) if there is no Master Agreement, the price per the individual purchase order received from each customer. The customers are invoiced at an agreed upon contractual price for each unit ordered and delivered by the Company.

Consistent with Company practice prior to the adoption of ASC 606, the Company does not collect sales tax or other similar taxes from customers. As such, there is no effect on the measurement of the transaction price.

Recognize Revenue When the Company Satisfies a Performance Obligation

Performance obligations related to contract manufacturing and retail customers are satisfied at a point in time when the goods are shipped to the customer as (i) the Company has transferred control of the assets to the customers upon shipping, and (ii) the customer obtains title and assumes the risks and rewards of ownership after the goods are shipped.

The Company does not accept returns in the contract manufacturing revenue stream. Our return policy for retailer customers accommodates returns for (i) discontinued products, (ii) store closings and (iii) products that have reached or exceeded their designated expiration date. We do not impose a period of time within which product may be returned. All requests for product returns must be submitted to us for pre-approval. The main components of our returns policy are: (i) we will accept returns that are due to damaged product that is un-saleable and such return request activity falls within an acceptable range, (ii) we will accept returns for products that have reached or exceeded designated expiration dates and (iii) we will accept returns in the event that we discontinue a product provided that the customer will have the right to return only such items that it purchased directly from us. We will not accept return requests pertaining to customer inventory "Overstocking" or "Resets". We will accept return requests for only products in its intended package configuration. We reserve the right to terminate shipment of product to customers who have made unauthorized deductions contrary to our return policy or pursue other methods of reimbursement. We compensate the customer for authorized returns by means of a credit applied to amounts owed or to be owed and in the case of discontinued product only, also by way of an exchange. We do not have any significant product exchange history.

Under ASC 606, the Company will continue to recognize contract manufacturing and retail customers at a point in time as the Company has an enforceable right to payment for goods as products are shipped to customers.

Note 2 – Summary of Significant Accounting Policies – continued

As of June 30, 2018 and December 31, 2017, we included a provision for sales allowances from continuing operations of $10,000 and $2,000, respectively. Additionally, accrued advertising and other allowances from discontinued operations as of June 30, 2018 included (i) $443,000 for estimated returns and (ii) $98,000 for cooperative incentive promotion costs. As of December 31, 2017, accrued advertising and other allowances from discontinued operations included (i) $480,000 for estimated future sales returns and (ii) $200,000 for cooperative incentive promotion costs.

As of June 30, 2018, we have deferred revenue of $52,000 in relation to Research and Development ("R&D") stability and release testing programs.

Disaggregation of Revenue

We disaggregate revenue from contracts with customers into two categories: contract manufacturing and retail customers. The Company determined that disaggregating revenue into these categories achieves the disclosure objective to depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

The following table disaggregates the Company's revenue by revenue source for the three and six months ended June 30, 2018 (in thousands):

Revenue by Customer Type	Three months ended June 30, 2018	Six months ended June 30, 2018
Contract manufacturing	$ 3,106	$ 6,440
Retail	80	154
Total Revenue	**$ 3,186**	**$ 6,594**

Practical Expedients Elected

The Company has elected the following practical expedients in applying ASC 606 across all each revenue stream:

Sales Tax Exclusion from the Transaction Price

The Company excludes from the measurement of the transaction price all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the Company from the customer.

Shipping and Handling Activities

The Company accounts for shipping and handling activities it performs after a customer obtains control of the good as activities to fulfill the promise to transfer the good.

Advertising and Incentive Promotions

Advertising and incentive promotion costs are expensed within the period in which they are utilized. Advertising and incentive promotion expense is comprised of (i) media advertising, presented as part of sales and marketing expense, (ii) cooperative incentive promotions and coupon program expenses, which are accounted for as part of net sales, and (iii) free product, which is accounted for as part of cost of sales. Advertising and incentive promotion expenses (i) incurred from continuing operations for the three months ended June 30, 2018 and 2017 were $39,000 and $21,000, respectively, and (ii) attributed to and classified as discontinued operations for the three months ended June 30, 2018 and 2017 were zero and $205,000, respectively. Advertising and incentive promotion expenses (i) incurred from continuing operations for the six months ended June 30, 2018 and 2017 were $72,000 and $53,000, respectively, and (ii) attributed to and classified as discontinued operations for the six months ended June 30, 2018 and 2017 were zero and $2.8 million, respectively. Included in prepaid expenses and other current assets was $139,000 and $139,000 at June 30, 2018 and December 31, 2017, respectively, relating to prepaid advertising and promotion expenses.

Note 2 – Summary of Significant Accounting Policies – continued

Share-Based Compensation

We recognize all share-based payments to employees and directors, including grants of stock options, as compensation expense in the financial statements based on their fair values. Fair values of stock options are determined through the use of the Black-Scholes option pricing model. The compensation cost is recognized as an expense over the requisite service period of the award, which usually coincides with the vesting period.

Stock and stock options for the purchase of our common stock, $0.0005 par value ("Common Stock"), have been granted to both employees and non-employees pursuant to the terms of certain agreements and stock option plans (see Note 5). Stock options are exercisable during a period determined by us, but in no event later than ten years from the date granted.

Research and Development

Research and development costs are charged to operations in the period incurred. Research and development costs incurred for the three months ended June 30, 2018 and 2017 (i) from continuing operations were $87,000 and $224,000, respectively, and (ii) attributed to and classified as discontinued operations were zero and $52,000, respectively. Research and development costs incurred for the six months ended June 30, 2018 and 2017 (i) from continuing operations were $175,000 and $258,000, respectively, and (ii) attributed to and classified as discontinued operations were zero and $52,000, respectively. Research and development costs are principally related to personnel expenses and new product development initiatives and costs associated with our OTC health care products, dietary supplements and other remedies.

Income Taxes

We utilize the asset and liability approach which requires the recognition of deferred tax assets and liabilities for the future tax consequences of events that have been recognized in our financial statements or tax returns. In estimating future tax consequences, we generally consider all expected future events other than enactments of changes in the tax law or rates. Until sufficient taxable income to offset the temporary timing differences attributable to operations and the tax deductions attributable to option, warrant and stock activities are assured, a valuation allowance equaling the total deferred tax asset is being provided (see Notes 3 and 6).

We utilize a two-step approach to recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount which is more than fifty percent likely of being realized upon ultimate settlement. Any interest or penalties related to income taxes will be recorded as interest or administrative expense, respectively.

As a result of our continuing tax losses, we have recorded a full valuation allowance against a net deferred tax asset. Additionally, we have not recorded a liability for unrecognized tax benefits.

Recently Adopted Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers" on revenue recognition. The new standard provides for a single five-step model to be applied to all revenue contracts with customers as well as requires additional financial statement disclosures that will enable users to understand the nature, amount, timing and uncertainty of revenue and cash flows relating to customer contracts. Companies have an option to use either a retrospective approach or cumulative effect adjustment approach to implement the standard. We adopted the new standard as of January 1, 2018, using the modified retrospective method. See the Revenue Recognition section within the Summary of Significant Accounting Policies in Note 2 for further details on the impact to our consolidated financial statements upon adoption and practical expedients elected. The implementation of the new revenue recognition standard did not have a material impact on our consolidated financial statements.

Note 2 – Summary of Significant Accounting Policies – continued

In November 2016, the FASB issued ASU No. 2016-18 "Statement of Cash Flows: Restricted Cash" which requires a statement of cash flows to explain the change during a period in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Under the new standard, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown in the statement of cash flows. ASU 2016-18 was effective for us as of January 1, 2018. We have not generally had restricted cash or restricted cash equivalents, and there is no restricted cash on the balance sheet as of June 30, 2018. The adoption of this update did not have a material impact on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments." The new standard attempts to reduce diversity in practice in how cash receipts and cash payments are presented and classified in the statement of cash flows. ASU No. 2016-15 provides guidance on eight specific cash flow issues, none of which currently apply to us. The new guidance was effective for us in the first quarter of 2018. The adoption of ASU 2016-15 did not have a material impact on the Company's financial statements.

In October 2016, the FASB issued ASU No. 2016-16, "Income Taxes: Intra-Entity Transfers of Assets Other than Inventory." The new standard requires entities to recognize the income tax consequences of an asset other than inventory when the asset transfer occurs. The new guidance was effective for us in the first quarter of 2018. The adoption of ASU 2016-15 did not have a material impact on the Company's financial statements.

Recently Issued Accounting Standards

In June 2018, the FASB issued Accounting Standards Update (ASU) 2018-07 intended to reduce cost and complexity and to improve financial reporting for nonemployee share-based payments. Currently, the accounting requirements for nonemployee and employee share-based payment transactions are significantly different. This ASU expands the scope of Topic 718, Compensation-Stock Compensation (which currently only includes share-based payments to employees) to include share-based payments issued to nonemployees for goods or services. Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. This ASU supersedes Subtopic 505-50, Equity-Equity-Based Payments to Nonemployees. The amendments in this ASU are effective for public companies for fiscal years beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact of this new standard on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02 "Leases." The new standard will require most leases to be recognized on the balance sheet which will increase reported assets and liabilities. Lessor accounting remains substantially similar to current guidance. The new standard is effective for annual and interim periods in fiscal years beginning after December 15, 2018, which for us is the first quarter of fiscal 2019 and mandates a modified retrospective transition method. We do not intend to early adopt and are currently assessing the impact of this update, but preliminarily believe that its adoption will not have a material impact on our consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments—Credit Losses." The standard modifies the impairment model for most financial assets, including trade accounts receivables and loans, and will require the use of an "expected loss" model for instruments measured at amortized cost. Under this model, entities will be required to estimate the lifetime expected credit loss on such instruments and record an allowance to offset the amortized cost basis of the financial asset, resulting in a net presentation of the amount expected to be collected on the financial asset. The effective date of the standard is for fiscal years beginning after December 15, 2019 with early adoption permitted. We are currently evaluating the impact of adoption of this update on our consolidated financial statements.

Note 3 – Discontinued Operations, Sale of the Cold-EEZE® Business

Effective March 29, 2017, we completed the sale of the Cold-EEZE® Business to Mylan.

As a consequence of the sale of the Cold-EEZE® Business, for the three months ended June 30, 2017, we classified as discontinued operations (i) the gain from the sale of the Cold-EEZE® Business, (ii) all gains and losses attributable to the Cold-EEZE® Business operations and (iii) the income tax expense attributed to the sale of the Cold-EEZE® Business (see Note 6). Excluded from the sale of the Cold-EEZE® Business were our accounts receivable and inventory, and we also retained all liabilities associated with our Cold-EEZE® Business operations arising prior to March 29, 2017.

Pursuant to the terms of the asset purchase agreement entered into with Mylan on January 6, 2017 (the "Asset Purchase Agreement"), we also agreed to a one-time sale to Mylan of certain non-lozenge-based Cold-EEZE® inventory for approximately $699,000, which approximates our cost. At June 30, 2017, we classified in our balance sheet this inventory as an asset held for sale, discontinued operations. Additionally, pursuant to the terms of the Asset Purchase Agreement, we allocated and agreed to pay Mylan an aggregate of $400,000 for future sales returns and allowances arising from certain product returns that were sold by us prior to March 30, 2017. At June 30, 2017, we classified in our balance sheet this liability as an accrued sales allowance, discontinued operations. At December 31, 2017, we classified $22,000 of assets held for sale in our balance sheet and as of June 30, 2018, the asset was sold to Mylan and removed from assets held for sale.

The net proceeds received from the sale of the Cold-EEZE® Business were as follows (in thousands):

	Amount
Gross consideration from the sale of the Cold-EEZE® Business	$ 50,000
Closing and transaction costs	(4,175)
Net proceeds from sale of the Cold-EEZE® Business	45,825
Book value of assets sold	(13)
Gain on sale of the Cold-EEZE® Business before income taxes	45,812
Income tax expense	(3,511)
Gain on sale of the Cold-EEZE® Business after income taxes	$ 42,301
Net proceeds:	
Cash paid at closing, net of closing and transaction costs	$ 43,145
Proceeds due on sale of assets, cash held in escrow (see Note 8)	5,000
	$ 48,145

For Fiscal 2017, we incurred $4.2 million in closing and transaction costs associated with the sale of the Cold-EEZE® Business which were comprised of (i) transaction fees and related closing costs of $1.9 million and (ii) performance bonuses, contract termination compensation and severance payments to certain employees associated with the sale of the Cold-EEZE® Business of $2.3 million. The compensation committee of our board of directors approved these compensation arrangements. These compensation and termination payments were paid by us in April 2017.

The following table sets forth the condensed operating results of our discontinued operations for the three and six months ended June 30, 2018 and 2017, respectively, (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net sales	$ -	$ (371)	$ -	$ 4,687
Cost of sales	-	264	-	2,037
Sales and marketing	-	200	-	1,720
Administration	-	-	-	348
Research and development	-	-	-	52
Income (loss) from discontinued operations	$ -	$ (835)	$ -	$ 530

There was no activity related to discontinued operations for the three and six months ended June 30, 2018.

Note 4 – Secured Promissory Notes and Other Obligations

Secured Promissory Notes

On December 11, 2015, we executed two subscription agreements (the "Subscription Agreements") with the investors named therein (the "Investors") providing for the purchase of 12% Secured Promissory Notes – Series A ("Notes") in the aggregate principal amount of up to $3.0 million and warrants to purchase shares of our Common Stock (the "Warrants").

Notes in the amount of $1.5 million and 51,000 Warrants, at an exercise price of $1.35 per share, which was equal to the closing price of our Common Stock on the date of investment, were issued by the Company and its wholly-owned subsidiaries, PMI and Quigley Pharma, Inc. (collectively, the "Obligors"), and funded on December 11, 2015. We incurred loan origination costs of $22,000 which was recorded as a reduction of the Notes and the origination costs are charged to interest expense over the term of the loan. The Warrants had an exercise term equal to three years and were exercisable commencing on the date of issuance. The fair value of the Warrants at the date of grant was $14,000, which was recorded as a reduction of the Notes and was charged to interest expense over the term of the loan.

The Notes bore interest at the rate of 12% per annum, payable semi-annually and the principal was due and payable on June 15, 2017. The Notes could be pre-paid at any time prior to maturity without penalty. The effective interest, inclusive of the Warrants and loan origination costs, was 14.3% per annum. For the three months ended June 30, 2018 and 2017, we charged to interest expense zero and $54,000, respectively, in connection with the Notes.

On March 29, 2017, in connection with the sale of the Cold-EEZE® Business, we paid in full the remaining principal and accrued interest due under the Notes, in the total amount of $1,553,000. Of the $1,553,000 paid to the Investors, $69,000 was netted against the aggregate exercise price of the Warrants, which were simultaneously being exercised by the Investors.

In connection with the issuance of the Notes, the Company entered into a security agreement with John E. Ligums, Jr., as collateral agent for the Investors (the "Security Agreement"), to secure the timely payment and performance in full of the Company's obligations under the Notes. Under the Security Agreement, we granted to the collateral agent, for the benefit of the Investors a lien upon and security interest in the property and assets listed as collateral in the Security Agreement, including without limitation, all of our personal property, inventory, equipment, general intangibles, cash and cash equivalents, and proceeds. In connection with the payoff of the Notes, the Security Agreement was terminated.

Note 5 – Transactions Affecting Stockholders' Equity

Our authorized capital stock consists of 50 million shares of Common Stock and 1 million shares of preferred stock, $.0005 par value ("Preferred Stock").

Preferred Stock

The Preferred Stock authorized under our certificate of incorporation may be issued from time to time in one or more series. As of June 30, 2018, no shares of Preferred Stock have been issued. Our board of directors have the full authority permitted by law to establish, without further stockholder approval, one or more series of Preferred Stock and the number of shares constituting each such series and to fix by resolution voting powers, preferences and relative, participating, optional and other special rights of each series of Preferred Stock, and the qualifications, limitations or restrictions thereof, if any. Subject to the limitation on the total number of shares of Preferred Stock that we have authority to issue under our certificate of incorporation, the board of directors is also authorized to increase or decrease the number of shares of any series, subsequent to the issue of that series, but not below the number of shares of such series then-outstanding. In case the number of shares of any series is so decreased, the shares constituting such decrease will resume the status that they had prior to the adoption of the resolution originally fixing the number of shares of such series. We may, subject to any required stockholder approval amend from time to time our certificate of incorporation to increase the number of authorized shares of Preferred Stock or Common Stock or to make other changes or additions to our capital structure or the terms of our capital stock.

2015 Equity Line of Credit

On July 30, 2015, we entered into a new equity line of credit agreement (such arrangement, the "2015 Equity Line") with Dutchess Opportunity Fund II, LP ("Dutchess"). Pursuant to the 2015 Equity Line, Dutchess committed to purchase, subject to certain restrictions and conditions, up to 3,200,000 shares of our Common Stock, over a period of 36 months from the effectiveness of the registration statement registering the resale of shares purchased by Dutchess pursuant to the Investment Agreement.

We may, at our discretion, draw on the 2015 Equity Line from time to time, as and when we determine appropriate in accordance with the terms and conditions of the 2015 Equity Line. The maximum number of shares that we are entitled to put to Dutchess in any one draw down notice shall not exceed 500,000 shares with a purchase price calculated in accordance with the terms of the 2015 Equity Line. We may deliver a notice for a subsequent put from time to time, following the one day pricing period for the prior put.

The purchase price is set at ninety-five percent (95%) of the volume weighted average price (VWAP) of the Common Stock during the one trading day immediately following our put notice. We have the right to withdraw all or any portion of any put, except that portion of the put that has already been sold to a third party, including any portion of a put that is below the minimum acceptable price set forth on the put notice, before the closing. In the event Dutchess receives more than a five percent (5%) return on the net sales for a specific put, Dutchess must remit such excess proceeds to us; however, in the event Dutchess receives less than a five percent (5%) return on the net sales for a specific put, Dutchess has the right to deduct from the proceeds of the put amount on the applicable closing date so Dutchess's return will equal five percent (5%).

There are put restrictions applied on days between the draw down notice date and the closing date with respect to that particular put. During such time, we are entitled to deliver another draw down notice. In addition, Dutchess is not obligated to purchase shares if Dutchess' total number of shares beneficially held at that time would exceed 4.99% of the number of shares of Common Stock as determined in accordance with Rule 13d-1(j) of the Securities Exchange Act of 1934, as amended. In addition, we are not permitted to draw on the facility unless there is an effective registration statement to cover the resale of the shares.

Pursuant to the terms of the 2015 Equity Line, we are obligated to file one or more registration statements with the SEC to register the resale by Dutchess of the shares of Common Stock issued or issuable under the 2015 Equity Line. In addition, we are obligated to use all commercially reasonable efforts to have the registration statement declared effective by the SEC within 90 days after the registration statement is filed. On August 4, 2015, we filed a registration statement for the underlying shares of the 2015 Equity Line with the SEC and the registration statement was declared effective by the SEC on August 21, 2015.

At June 30, 2018, we have 2,450,000 shares of our Common Stock available for sale, at our discretion, under the terms of our 2015 Equity Line and covered pursuant to an effective registration statement. The 2015 Equity Line expired in July 2018.

The 2010 Equity Compensation Plan

On May 5, 2010, our stockholders approved the 2010 Equity Compensation Plan, which has been subsequently amended and restated by our stockholders (the "2010 Plan"). The 2010 Plan provides that the total number of shares of Common Stock that may be issued under the 2010 Plan is 3.9 million shares.

During the six months ended June 30, 2018, we granted 30,000 options, exercisable at $2.35 per share and subject to vesting over a three-year term, to a consultant to acquire our Common Stock pursuant to the terms of the 2010 Plan. For the six month ended June 30, 2017, we granted, 600,000 options to employees, exercisable at $2.00 per share and subject to vesting over a four-year term. We use the Black-Scholes option pricing model to determine the fair value of the stock options and Warrants at the date of grant. Based upon our limited historical experience, we determined the expected term of the stock option grants to be 4.5 years, calculated using the "simplified" method in accordance with the SEC Staff Accounting Bulletin 110. We use the "simplified" method since our historical data does not provide a reasonable basis upon which to estimate expected term. Presented below is a summary of the terms of the grant of options. The assumptions used in determining the fair value of the 30,000 stock options granted in the first quarter of Fiscal 2018 were (i) expected option life of 4.5 years, (ii) weighted average risk rate of 2.37%, (iii) dividend yield of 0% and (iv) expected volatility of 40.06%.

During the six months ended June 30, 2018 and 2017, we issued 490,000 and 90,000 shares of common stock, respectively, upon the exercise of stock options granted under our 2010 Plan, including 250,000 shares that were issued in the six months ended June 30, 2018 pursuant to a cashless exercise. At June 30, 2018, there were 519,500 stock options outstanding under the 2010 Plan and 791,159 shares available to be issued pursuant to the terms of the 2010 Plan.

The 2010 Directors' Equity Compensation Plan

On May 5, 2010, our stockholders approved the 2010 Directors' Equity Compensation Plan which, was has been subsequently amended and restated by our stockholders (the "2010 Directors' Plan"). A primary purpose of the 2010 Directors' Plan is to provide us with the ability to pay all or a portion of the fees of directors in restricted stock instead of cash. The 2010 Directors' Plan provides that the total number of shares of Common Stock that may be issued under the 2010 Directors' Plan is equal to 675,000 shares. For the six months ended June 30, 2018 and 2017, no shares were granted to our directors under the 2010 Directors' Plan. At June 30, 2018, there were 397,808 shares of Common Stock that may be issued pursuant to the terms of the 2010 Directors' Plan.

The 2018 Stock Incentive Plan

On April 12, 2018, our stockholders approved the 2018 Stock Incentive Plan (the "2018 Stock Plan"). The 2018 Stock Plan provides for the grant of incentive stock options to eligible employees of the Company, and for the grant of nonstatutory stock options to eligible employees, directors and consultants. The purpose of the 2018 Stock Plan is to advance the interests of the Company and its stockholders by providing an incentive to attract, retain, and reward persons performing services for the Company and by motivating such persons to contribute to the growth and profitability of the Company. The 2018 Stock Plan provides that the total number of shares that may be issued pursuant to the 2018 Stock Plan is 2.3 million shares. At June 30, 2018, all 2.3 million shares have been granted in the form of stock options to Ted Karkus, our Chief Executive Officer and no stock options have been exercised under the 2018 Stock Plan (the "CEO Options") none of which have been exercised. (see Note 8). We use the Black-Scholes option pricing model to determine the fair value of the stock options and Warrants at the date of grant. Based upon our limited historical experience, we determined the expected term of the stock option grants to be 4.5 years, calculated using the "simplified" method in accordance with the SEC Staff Accounting Bulletin 110. We use the "simplified" method since our historical data does not provide a reasonable basis upon which to estimate expected term. The assumptions used in determining the fair value of the 2,300,000 stock options granted in the second quarter of Fiscal 2018 were (i) expected option life of 4.5 years, (ii) weighted average risk rate of 2.42%, (iii) dividend yield of 0% and (iv) expected volatility of 40.10%.

The 2018 Plan permits provides for certain proportionate adjustments to be made to stock options granted under the 2018 Plan upon the occurrence of certain events, including a special distribution (whether in the form of cash, shares, other securities, or other property). Accordingly, the Board has adjusted the terms of the CEO Option, such that the exercise price of the CEO Option was be reduced from $3.00 per share to $2.00 per share, effective as of June 5, 2018, the date the special cash dividend was to be paid and subject to such dividend payment being made. Compensation cost was measured for the difference between the fair value of the modified award and the fair value of the original award on the modification date. The incremental compensation cost of approximately $900,000 is being recognized over the remaining service period as the sum of the incremental compensation cost and the remaining unrecognized compensation cost for the original award on the modification date.

Prior to the modification, the Company had recognized $143,912 of compensation expense. With an original gross value of $1,554,252, the unrecognized compensation expense as of the modification date was $1,410,340.

Note 6 – Income Taxes

At December 31, 2017, there were $12.2 million in net operating loss carryforwards, subject to applicable limitations, available to us for federal purposes which will expire beginning for the year ended December 31, 2032 through 2036. Additionally, there were $13.8 million in net operating loss carryforwards, subject to limitations, available to us for state purposes, which will expire beginning for the year ended December 31, 2019 through 2037.

Utilization of net operating loss carryforwards may be subject to limitations as set forth in Section 382 of the Internal Revenue Code ("Section 382"). Based on our preliminary Section 382 analysis, we do not believe that our current net operating loss carryforwards are subject to these limitations as of June 30, 2018. However, until we complete a final Section 382 analysis upon filing of our 2018 income tax return, there can be no assurances that our preliminary analysis is accurate or complete. Should we identify any limitations upon the completion of our final Section 382 analysis, the impact could be material to our consolidated financial statements and we could incur additional income tax expense arising from the sale of the Cold-EEZE® Business.

For the six months ended June 30, 2017, we charged to discontinued operations $3.1 million for estimated federal and state income taxes arising from the sale of the Cold-EEZE® Business and we have realized an income tax benefit from continuing operations of $1.0 million as a consequence of the utilization of the federal and state net operating losses.

Until sufficient taxable income to offset the temporary timing differences attributable to operations, and the tax deductions attributable to option, warrant and stock activities are assured, a valuation allowance equaling the total deferred tax asset is being provided. As a consequence of the accumulated losses of the Company, we believe that this allowance is required due to the uncertainty of realizing these tax benefits in the future.

On December 22, 2017, the President of the United States signed into law legislation that is commonly referred to as the Tax Cuts and Jobs Act (the "TCJA"). This legislation reduced the U.S. corporate tax rate from the existing graduated rate of 15-35% to a flat 21% for tax years beginning after December 31, 2017. As a result of the enacted law, we were required to revalue our deferred tax assets and liabilities existing as of December 31, 2017 from the graduated 15-35% federal rate in effect through the end of 2017, to the new flat 21% rate. This revaluation resulted in a reduction to our deferred tax asset of $1.8 million. This amount was offset by a corresponding reduction to our valuation allowance. The other provisions of the TCJA did not have a material impact on our December 31, 2017 consolidated financial statements. Estimates used to prepare our income tax expense are based on our initial analysis of the TCJA. Given the complexity of the TCJA, anticipated guidance from the U.S. Treasury regarding implementation of the TCJA, and the potential for additional guidance from the Securities and Exchange Commission and the FASB related to the TCJA, these estimates may be adjusted during Fiscal 2018 to reflect any such guidance provided.

Note 7 – Other Current Liabilities

The following table sets forth the components of other current liabilities at June 30, 2018 and December 31, 2017, respectively, (in thousands):

	June 30, 2018	December 31, 2017
Accrued Expenses	$ 76	$ 66
Accrued Benefits	67	15
Accrued Payroll	32	79
Accrued Vacation	81	88
Sales Tax payable	3	3
Deferred revenue	52	-
Income taxes payable	740	740
Due to Mylan and affiliates	-	59
	$ 1,051	$ 1,050

Note 8– Commitments and Contingencies

Escrow Receivable

We have indemnification obligations to Mylan under the Asset Purchase Agreement that may require us to make future payments to Mylan and other related persons for any damages incurred by Mylan or such related persons as a result of any breaches of our representations, warranties, covenants or agreements contained in the Asset Purchase Agreement, or arising from the Retained Liabilities (as such term is defined in the Asset Purchase Agreement) or certain third party claims specified in the Asset Purchase Agreement. Generally, our representations and warranties survive for a period of 24 months from the closing date, other than certain fundamental representations which survive until the expiration of the applicable statute of limitations. There is a limited indemnification cap with respect to a majority of the Company's indemnification obligations under the Asset Purchase Agreement with the exception of claims for actual fraud, the breach of any fundamental representations and certain other items, which have a larger indemnification cap (e.g., the purchase price).

Pursuant to the terms of the Asset Purchase Agreement, we, Mylan, and an escrow agent entered into an Escrow Agreement at closing, pursuant to which Mylan deposited $5 million of the aggregate purchase price for the Cold-EEZE® Business into an escrow account established with the Escrow Agent in order to satisfy, in whole or in part, certain of our indemnity obligations under the Asset Purchase Agreement.

If, on the 18th month anniversary of the closing date, there are funds remaining in the escrow account, then the escrow account will be reduced by the difference, if a positive number, of (i) $2.5 million minus (ii) the aggregate amount of all escrow claims asserted by Mylan prior to this date that have either been paid out of the escrow account or are pending as of such date, and, within two business days of such date, the Escrow Agent will disburse such difference, if a positive number, to us. Within two business days of the second anniversary of the closing date, the Escrow Agent will release any funds remaining in the escrow account to us minus any amounts being reserved for escrow claims asserted by Mylan prior to such date. Upon the resolution of any pending escrow claims, the Escrow Agent will, within two business days of receipt of joint instructions or a final order from a court (as described in the Escrow Agreement) disburse such reserved amount to the parties entitled to such funds.

On May 31, 2018, we received notice of a claim for $800,000 in losses against the escrow amount. We have disputed this claim and intend to vigorously contest such claim. In the event that this or any other indemnity claim is successful, we may be required to pay Mylan such amounts out of escrow fund, pursuant to the indemnification provisions of the Asset Purchase Agreement which may reduce the amount we ultimately collect from escrow or could even require us to return a portion of the net proceeds received from the sale of the Cold-EEZE® Business if the escrow funds are insufficient to cover the losses.

Note 8– Commitments and Contingencies – continued

Manufacturing Agreement

In connection with the Asset Purchase Agreement, the Company and its wholly-owned subsidiary, PMI, entered into a Manufacturing Agreement (the "Manufacturing Agreement") with Mylan. Pursuant to the terms of the Manufacturing Agreement, Mylan (or an affiliate or designee) purchased the inventory of the Company's Cold-EEZE ® brand and product line, and PMI will manufacture certain products for Mylan, as described in the Manufacturing Agreement, at prices that reflect current market conditions for such products and include an agreed upon mark-up on our costs. Unless terminated sooner by the parties, the Manufacturing Agreement will remain in effect until March 29, 2022. Thereafter, the Manufacturing Agreement may be renewed by Mylan for up to five successive one-year periods by providing notice of its intent to renew not less than 90 days prior to the expiration of the then-current term.

Employment Agreement

On February 16, 2018, our board of directors approved the Amended and Restated 2015 Executive Employment Agreement with Ted Karkus, our Chief Executive Officer (the "Amended Employment Agreement"), which became effective February 23, 2018, and was approved by stockholders at a special meeting of stockholders held April 12, 2018. Pursuant to the terms of the Amended Employment Agreement, Mr. Karkus voluntarily agreed to reduce his base salary from the rate set forth in the 2015 Employment Agreement (*i.e.,* not less than $675,000 per annum) to a base salary of $125,000 per annum (the "Term Base Salary") through February 22, 2021. Unless otherwise determined by the mutual agreement of the Company and Mr. Karkus, on February 22, 2021 and thereafter, Mr. Karkus' salary will increase from the Term Base Salary to not less than $675,000 per annum.

In consideration of Mr. Karkus' voluntary reduction in salary, our board of directors awarded Mr. Karkus a stock option to purchase 2,300,000 shares of our Common Stock at an exercise price of $3.00 per share on February 23, 2018 (the "Executive Stock Option"). The Executive Stock Option will vest and be exercisable in 35 equal monthly installments of 63,888 shares and one monthly installment of 63,290 shares, subject to his continued employment, and subject to accelerated vesting in the event Mr. Karkus's employment is terminated for any reason other than by us for Cause or by Mr. Karkus without Good Reason (as such terms are defined in the Amended Employment Agreement). The Executive Stock Option is be exercisable for a five year term commencing on the date of grant. The Executive Stock Option was granted pursuant to the 2018 Stock Plan, which was also adopted and approved by our board of directors on February 16, 2018. The 2018 Plan, like the Amended Employment Agreement, received stockholder approval at a special meeting of stockholders held on April 12, 2018 at which time the options were considered granted. The 2018 Plan authorizes the issuance of up to 2,300,000 shares pursuant to stock options granted under the 2018 Plan, all of which were issued to Mr. Karkus as part of the Executive Stock Option.

As discussed further in Note 5, on May 7, 2018, the Compensation Committee of the board of directors approved an adjustment to the Executive Stock Option, as permitted under the 2018 Stock Plan, in relation to the special cash dividend paid to stockholders on June 5, 2018. Specifically, the board of directors reduced the exercise price of the Executive Stock Option from $3.00 per share to $2.00 per share, effective as of June 5, 2018.

Future Obligations:

We have estimated future minimum obligations over the next five years, including the remainder of Fiscal 2018, as follows (in thousands):

Fiscal Year		Employment Contracts
2018	$	62,500
2019		125,000
2020		125,000
2021		595,136
2022		675,000
	Total $	1,582,636

Note 9 – Earnings (Loss) Per Share

Basic earnings (loss) per share for continuing and discontinued operations are computed by dividing the respective net income or loss attributable to common stockholders by the weighted-average number of shares of our Common Stock outstanding for the period. Diluted earnings (loss) per share reflects the potential dilution that could occur if securities or other contracts to issue Common Stock were exercised or converted into Common Stock or resulted in the issuance of Common Stock that shared in the earnings of the entity. Diluted earnings (loss) per share also utilize the treasury stock method which prescribes a theoretical buy-back of shares from the theoretical proceeds of all options and warrants outstanding during the period. Options and warrants outstanding to acquire shares of our Common Stock at June 30, 2018 and 2017 were 2,819,500 and 2,209,000, respectively.

For the three months ended June 30, 2018 and June 30, 2017 dilutive earnings (loss) per share were the same as basic earnings per share due to the inclusion of Common Stock in the form of stock options and warrants ("Common Stock Equivalents"), when in a net loss position would have an anti-dilutive effect on loss per share. For the three months ended June 30, 2018 and 2017, there were 1,113,320 and 641,754 Common Stock Equivalents, that were in the money, that were excluded from the earnings (loss) per share computation as a consequence of their anti-dilutive effect.

For the six months ended June 30 2018, there were 889,968, Common Stock Equivalents which were in the money, that were excluded from the earnings (loss) per share computation as a consequence of their anti-dilutive effect. For the six months ended June 30, 2017 there were 650,190 Common Stock Equivalents that were in the money, which were included in the fully diluted earnings per share computation.

Note 10 – Significant Customers

Revenue from continuing operations for the three months ended June 30, 2018 and 2017 was $3.2 million and $1.9 million, respectively. Two third-party contract manufacturing customers accounted for 57.2% and 29.4%, respectively, of our revenue from continuing operations for the three months ended June 30, 2018. Two third-party contract manufacturing customers accounted for 63.3% and 13.9%, respectively, of our revenues from continuing operations for the three months ended June 30, 2017. The loss of sales to either of these large third-party contract manufacturing customers could have a material adverse effect on our business operations and financial condition.

Revenue from continuing operations for the six months ended June 30, 2018 and 2017 was $6.6 million and $2.7 million, respectively. Two third-party contract manufacturing customers accounted for 43.1% and 39.0%, respectively, of our revenue from continuing operations for the six months ended June 30, 2018. Two third-party contract manufacturing customers accounted for 43.5% and 25.1%, respectively, of our revenues from continuing operations for the six months ended June 30, 2017. The loss of sales to either of these large third-party contract manufacturing customers could have a material adverse effect on our business operations and financial condition.

We are subject to account receivable credit concentrations from time-to-time as a consequence of the timing, payment pattern and ultimate purchase volumes or shipping schedules with our customers. These concentrations may impact our overall exposure to credit risk, either positively or negatively, in that our customers may be similarly affected by changes in economic, regulatory or other conditions that may impact the timing and collectability of amounts due to us. Two customers represented 48% and 42% and one customer represented 84% of our total trade receivable balances at June 30, 2018 and December 31, 2017, respectively. Management believes that the provision for possible losses on uncollectible accounts receivable is adequate for our credit loss exposure. The allowance for doubtful accounts was zero for both June 30, 2018 and December 31, 2017.

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

The following discussion and analysis should be read in conjunction with our interim unaudited condensed financial statements and related notes included in this Quarterly Report on Form 10-Q ("Quarterly Report") and the audited financial statements and notes thereto as of and for the year ended December 31, 2017 and the related Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K/A filed with the Securities and Exchange Commission ("SEC") on August 20, 2018 (the "2017 Annual Report"). As used in this Quarterly Report, unless the context suggests otherwise, "we," "us," "our," or "ProPhase" refer to ProPhase Labs, Inc. and its subsidiaries and consolidated variable interest entities, unless the context otherwise requires.

Forward-Looking Statements

This Quarterly Report contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by the forward-looking statements. Many of these factors are beyond our ability to predict. Given the risks and uncertainties surrounding forward-looking statements, you should not place undue reliance on these statements. Forward-looking statements typically are identified by use of terms such as "anticipate", "believe", "plan", "expect", "intend", "may", "will", "should", "estimate", "predict", "potential", "continue" and similar words although some forward-looking statements are expressed differently. This Quarterly Report may contain forward-looking statements attributable to third parties relating to their estimates regarding the growth of our markets. You are cautioned that such forward-looking statements are not guarantees of future performance and that all forward-looking statements address matters that involve risk and uncertainties, and there are many important risks, uncertainties and other factors that could cause our actual results, levels of activity, performance, achievements and prospects, as well as those of the markets we serve, to differ materially from the forward-looking statements contained in this Quarterly Report.

Such risks and uncertainties include, but are not limited to:

- The ability of our management to successfully implement our business plan and strategy;
- Our ability to compete effectively, including our ability to maintain and increase our markets and/or market share in the markets in which we do business;
- Our ability to fund our operations including the cost and availability of capital and credit;
- Our ability to grow our manufacturing business and operate it profitably;
- Potential disruptions in our ability to manufacture our products and those of others or our access to raw materials;
- Our ability to successfully develop and commercialize our existing products and new products;
- Changes in our retail and distribution customers strategic business plans including, but not limited to, (i) expansions, mergers, and/or consolidations, (ii) retail shelf space allocations for products within each outlet and in particular the healthcare category in which we compete, (iii) changes in their private label assortment and (iv) product selections, distribution allocation, merchandising programs and retail pricing of our products as well as competitive products;
- The general financial and economic uncertainty, fluctuations in consumer confidence and the strength of the United States economy, and their impacts on our business including demand for our products;
- Our ability to protect our proprietary rights;
- Our continued ability to comply with regulations relating to our current products and those we manufacture for others, and any new products we develop, including our ability to effectively respond to changes in laws and regulations or the interpretation thereof including changing market rules and evolving federal, state and regional laws and regulations;
- Seasonal fluctuations in demand for the products we manufacture at our manufacturing facility; and
- Our ability to attract, retain and motivate our key employees.

You should also consider carefully the statements we make under other sections of this Quarterly Report and in our 2017 Annual Report, as well as in other documents we file from time to time with the SEC, that address additional risks that could cause our actual results to differ from those set forth in any forward-looking statements. Our forward-looking statements speak only as the date of this Quarterly Report. We undertake no obligation to publicly update or review any forward-looking statements, whether as a result of new information, future developments or otherwise, except as required by law.

General

ProPhase was initially organized in Nevada in July 1989. Effective June 18, 2015, we changed our state of incorporation from the State of Nevada to the State of Delaware. We are a vertically integrated and diversified branding, marketing and technology company with deep experience with OTC consumer healthcare products, dietary supplements and other remedies. We are engaged in the research, development, manufacture, distribution, marketing and sale of OTC consumer healthcare products, dietary supplements and other remedies in the United States. This includes the development and marketing of dietary supplements under the TK Supplements® brand.

In August 2017, we formed ProPhase Digital Media Inc. ("PDM"), a Delaware corporation and wholly-owned subsidiary. Our objective is for PDM to become an independent full-service direct marketing agency. PDM's first initiative will be to market the TK Supplements® product line. If successful, this may lead to the marketing of other companies' consumer products.

In addition, we also continue to actively pursue acquisition opportunities for other companies, technologies and products within and outside the consumer products industry.

Discontinued Operations

Prior to March 29, 2017, our flagship OTC drug brand was Cold-EEZE® and our principal product was Cold-EEZE® cold remedy zinc gluconate lozenges. In addition to Cold-EEZE® cold remedy lozenges, we also marketed and distributed non-lozenge forms of our proprietary zinc gluconate formulation, (i) Cold-EEZE® cold remedy QuickMelts®, (ii) Cold-EEZE® Gummies and (iii) Cold-EEZE® cold remedy oral spray.

Effective March 29, 2017, we sold our intellectual property rights and other assets related to our Cold-EEZE® brand and product line, including all then current and pipeline over-the-counter allergy, cold, flu, multi-symptom relief and immune support treatments for adults and children to the extent each was, or was intended to be, branded "Cold-EEZE®", including all formulations and derivatives thereof (collectively referred to as the "Cold-EEZE® Business") to Mylan Consumer Healthcare Inc. (formerly known as Meda Consumer Healthcare Inc.) ("MCH") and Mylan Inc. (together with MCH, "Mylan") pursuant to the terms of an Asset Purchase Agreement, dated January 6, 2017 (the "Asset Purchase Agreement"). As a consequence of the sale of the Cold-EEZE® Business, for the three months ended June 30, 2017, we have classified as discontinued operations (i) all income and expenses attributable to the Cold-EEZE® Business, (ii) the gain from the sale of the Cold-EEZE® Business, and (iii) the income tax expense attributed to the sale of the Cold-EEZE® Business. Excluded from the sale of the Cold-EEZE® Business were our accounts receivable and inventory. We have also retained all liabilities associated with our Cold-EEZE® Business operations arising prior to March 29, 2017. There were no discontinued operations during the three and six months ended June 30, 2018.

Continuing Operations and Product Development

We continue to own and operate our manufacturing facility and manufacturing business in Lebanon, Pennsylvania, and our headquarters in Doylestown, Pennsylvania. As part of the sale of the Cold-EEZE® Business, we entered into a manufacturing agreement (see Note 8) with Mylan and our wholly-owned subsidiary, Pharmaloz Manufacturing, Inc. ("PMI") to supply various Cold-EEZE® lozenge products to Mylan. In addition to the production services we provide to Mylan under the manufacturing agreement, we produce OTC healthcare and dietary supplement products for other third-party customers in addition to performing operational tasks such as warehousing, customer order processing and shipping.

We are also pursuing a series of new product development, pre-commercialization, and market testing initiatives in the OTC dietary supplement category. The TK Supplements® product line is comprised of three men's health products: (i) Legendz XL® for sexual health, (ii) Triple Edge XL®, a daily energy booster plus testosterone support, and (iii) Super ProstaFlow Plus™ for prostate and urinary health. We recently completed a broad series of clinical studies which support important product claims which have now been incorporated in our product packaging and marketing communications. In addition to developing direct-to-consumer marketing strategies, we received initial product acceptance into a national chain drug retailer and to several regional retailers of our Legendz XL® product during fiscal 2017.

As with any new product launch, we anticipate losses from the TK Supplements® products as we optimize our retail and direct response strategy.

Product Innovation, Seasonality of the Business and Liquidity

Our net sales are derived principally from our contract manufacturing of OTC healthcare and dietary supplements products in the United States. In addition, we are engaged in early stage commercialization and market testing activities for the TK Supplements® product line of dietary supplements.

Our net sales are derived principally from our contract manufacturing and retail customers in the United States. In addition, we are engaged in commercialization and market testing activities for the TK Supplements® product line of dietary supplements. Our sales are influenced (i) by market acceptance of our TK Supplement® products and fluctuations in the timing of purchase and the ultimate level of demand for our contract manufactured OTC healthcare and dietary supplement products which are a function of the timing, length and severity of each cold season. Generally, a cold season is defined as the period of September to March when the incidence of the common cold rises as a consequence of the change in weather and other factors. We generally experience in the first, third and fourth quarter higher levels of net sales.

As a consequence of the scope and timing of our TK Supplements® product market launch and the seasonality of our contract manufacturing OTC business, we realize variations in operating results and demand for working capital from quarter to quarter. As of June 30, 2018, we had working capital of approximately $18.0 million, including $6.8 million marketable securities available for sale. We believe our current working capital at June 30, 2018 is at an acceptable and adequate level to support our business for at least the next twelve months.

Financial Condition and Results of Operations
Results from Continuing Operations for the Three Months Ended June 30, 2018
as Compared to the Three Months Ended June 30, 2017

For the three months ended June 30, 2018, net sales were $3.2 million as compared to $1.9 million for the three months ended June 30, 2017. The increase in net sales from period to period was principally due to an increase in contract manufacturing net sales.

Cost of sales for the three months ended June 30, 2018 were $1.9 million as compared to $1.8 million for the three months ended June 30, 2017. For the three months ended June 30, 2018 and 2017, we realized a gross margin of 39.5% and 7.3%, respectively. The increase of 32.2% in gross margin from the prior period is principally due to (i) better cost management on raw materials, (ii) an increase in the absorption of fixed production costs and (iii) improved streamlining of our manufacturing processes from period to period.

Sales and marketing expense for the three months ended June 30, 2018 was $235,000 as compared to $221,000 for the three months ended June 30, 2017.

Administration expenses for the three months ended June 30, 2018 was $1.2 million as compared to $1.3 million for the three months ended June 30, 2017.

Research and development costs during the three months ended June 30, 2018 was $87,000, as compared to $224,000 for the three months ended June 30, 2017. The decrease of $137,000 in research and development costs for the three months ended June 30, 2018 as compared to the three months ended June 30, 2017 was due principally to the timing of product research expenses in the prior period.

Interest and other income for the three months ended June 30, 2018 and 2017 was $4,000 and $151,000, respectively. The decrease in interest expense for the three months ended June 30, 2018 as compared to June 30, 2017 was principally due to a $150,000 of transition services fees earned in the prior period.

For the three months ended June 30, 2017, we charged to discontinued operations $3.5 million for estimated federal and state income taxes arising from the sale of the Cold-EEZE® Business and we realized an income tax benefit from continuing operations of $1.0 million as a consequence of the utilization of the federal and state net operating losses. There were no discontinued operations during the three months ended June 30, 2018.

For the three months ended June 30, 2017, results from operations for our Cold-EEZE® Business are classified as discontinued operations. The carve out of the discontinued operations are derived from identifying and carving out the specific assets, liabilities, net sales, cost of sales, operating expenses and interest expense associated with the Cold-EEZE® Business's operations. Administrative expenses, including personnel expenses and bonuses, and research and development overhead expenses incurred by us (for which the discontinued operation benefits from such resources) are allocated to discontinued operations based upon the percentage of the Cold-EEZE® Business's net sales to our consolidated net sales. For the three months ended June 30, 2017, we allocated (i) $348,000 to administrative operating expenses, (ii) $1.5 million to sales and marketing operating expenses, and (iii) $52,000 to research and development operating expenses, in the accompanying statement of operations. As a consequence of the sale of the Cold-EEZE® Business, we recorded a gain on the sale of the assets of $42.2 million, net of $3.5 million of income tax.

As a consequence of the effects of the above, the net loss from continuing operations for the three months ended June 30, 2018 was $260,000, or ($0.02) per share as compared to net loss of $875,000, or ($0.05) per share, for the three months ended June 30, 2017. Net loss from discontinued operations for the three months ended June 30, 2018 was zero compared to $1.4 million, or (0.08) per share, at June 30, 2017. Net loss for the three months ended June 30, 2018 was $260,000, or ($0.02) per share as compared to $2.3 million, or ($0.13) per share, for the three months ended June 30, 2017.

Financial Condition and Results of Operations
Results from Continuing Operations for the Six Months Ended June 30, 2018
as Compared to the Six Months Ended June 30, 2017

For the six months ended June 30, 2018, net sales were $6.6 million as compared to $2.7 million for the six months ended June 30, 2017. The increase in net sales from period to period was principally due to the treatment of the discontinued operations for the Cold-EEZE® Business in the prior period and an increase in contract manufacturing net sales.

Cost of sales for the six months ended June 30, 2018 were $3.9 million as compared to $2.5 million for the six months ended June 30, 2017. For the six months ended June 30, 2018 and 2017, we realized a gross margin of 40.7% and 8.4%, respectively. The increase of 32.3% in gross margin from the prior period is principally due to (i) treatment of the discontinued operations for the Cold-EEZE® Business in the prior period (ii) an increase in the absorption of fixed production costs, and (iii) improved streamlining of our manufacturing processes from period to period.

Sales and marketing expense for the six months ended June 30, 2018 was $407,000 as compared to $336,000 for the six months ended June 30, 2017.

Administration expenses for the six months ended June 30, 2018 was $2.4 million as compared to $2.4 million for the six months ended June 30, 2017.

Research and development costs during the six months ended June 30, 2018 were $174,000, as compared to $258,000 for the six months ended June 30, 2017. The decrease of $83,000 in research and development costs for the six months ended June 30, 2018 as compared to the six months ended June 30, 2017 was due principally to the timing of product research expenses in the prior period.

Interest and other income for the six months ended June 30, 2018 and 2017 was $100,000 and $97,000, respectively.

For the six months ended June 30, 2017, we charged to discontinued operations $3.5 million for estimated federal and state income taxes arising from the sale of the Cold-EEZE® Business and we realized an income tax benefit from continuing operations of $1.1 million as a consequence of the utilization of the federal and state net operating losses. There were no discontinued operations during the six months ended June 30, 2018.

For the six months ended June 30, 2017, results from operations for our Cold-EEZE® Business are classified as discontinued operations. The carve out of the discontinued operations are derived from identifying and carving out the specific assets, liabilities, net sales, cost of sales, operating expenses and interest expense associated with the Cold-EEZE® Business's operations. Administrative expenses, including personnel expenses and bonuses, and research and development overhead expenses incurred by us (for which the discontinued operation benefits from such resources) are allocated to discontinued operations based upon the percentage of the Cold-EEZE® Business's net sales to our consolidated net sales. For the six months ended June 30, 2017, we allocated (i) $348,000 to administrative operating expenses, included in Administration and (ii) $52,000 to research and development operating expenses, in the accompanying statement of operations. As a consequence of the sale of the Cold-EEZE® Business, we recorded a gain on the sale of the assets of $42.3 million, net of $3.5 million of income tax.

As a consequence of the effects of the above, the net loss from continuing operations for the six months ended June 30, 2018 was $216,000, or ($0.02) per share as compared to net loss of $1.6 million, or ($0.09) for the six months ended June 30, 2017. Net income from discontinued operations for the six months ended June 30, 2018 was zero compared to $43.2 million, or $2.54 per share, at June 30, 2017. Net loss for the six months ended June 30, 2018 was $216,000, or ($0.02) per share as compared to $41.6 million, or $2.45 per share for the six months ended June 30, 2017.

Liquidity and Capital Resources

Our aggregate cash and cash equivalents and including marketable securities, as of June 30, 2018 were $10.4 million compared to $21.9 million at December 31, 2017. The decrease of $11.5 million in our cash and securities balance for the six months ended June 30, 2018 was principally due to our payment of the $1.00 special cash dividend paid in June 2018.

Equity Line of Credit

We had an equity line (the "2015 Equity Line") with Dutchess Opportunity Fund II LP ("Duchess"), pursuant to which Dutchess committed to purchase, subject to certain restrictions and conditions, up to 3,200,000 shares of our Common Stock over a period of 36 months from the effectiveness of the registration statement registering the resale of shares purchased by Dutchess pursuant to the investment agreement with Duchess. At June 30, 2018, we had 2,450,000 shares of our Common Stock available for sale, at our discretion, under the terms of the 2015 Equity Line and covered pursuant to an effective registration statement. The 2015 Equity Line expired in July 2018.

Amended and Restated Employment Agreement with Ted Karkus

On February 16, 2018, our board of directors approved the Amended and Restated 2015 Executive Employment Agreement with Ted Karkus, our Chief Executive Officer (the "Amended Employment Agreement"), which became effective February 23, 2018 and which received stockholder approval at a special meeting of stockholders held on April 12, 2018. Pursuant to the terms of the Amended Employment Agreement, Mr. Karkus has voluntarily agreed to reduce his base salary from the rate set forth in his previous employment agreement (the "Prior Employment Agreement") (i.e., not less than $675,000 per annum) to a base salary of $125,000 per annum (the "Term Base Salary") through February 22, 2021. Unless otherwise determined by the mutual agreement of the Company and Mr. Karkus, on February 22, 2021 and thereafter, Mr. Karkus' salary will increase from the Term Base Salary to not less than $675,000 per annum.

In consideration of Mr. Karkus' voluntary reduction in salary, our board of directors granted Mr. Karkus a stock option to purchase 2,300,000 shares of our common stock at an exercise price of $3.00 per share on February 23, 2018 (the "Executive Stock Option"). The Executive Stock Option will vest and be exercisable in 35 equal monthly installments of 63,888 shares and one monthly installment of 63,290 shares, subject to his continued employment, and subject to accelerated vesting in the event Mr. Karkus's employment is terminated for any reason other than by us for Cause or by Mr. Karkus without Good Reason (as such terms are defined in the Amended Employment Agreement). The Executive Stock Option is exercisable for a five-year term commencing on the date of grant. The Executive Stock Option is granted pursuant to the 2018 Stock Incentive Plan (the "2018 Plan"), which was also adopted and approved by our board of directors on February 16, 2018. The 2018 Plan, like the Amended Employment Agreement, received stockholder approval at a special meeting of stockholders held on April 12, 2018. The 2018 Plan authorizes the issuance of up to 2,300,000 shares pursuant to stock options granted under the 2018 Plan, all of which were issued to Mr. Karkus as part of the Executive Stock Option.

On May 7, 2018, the Compensation Committee of the board of directors approved an adjustment to the stock option granted to Mr. Karkus on February 23, 2018, as permitted under the Company's 2018 Stock Plan in relation to the special cash dividend. The board of directors has adjusted the terms of the Executive Stock Option, such that the exercise price of the Executive Stock Option will be reduced from $3.00 per share to $2.00 per share, effective as of June 5, 2018, the date the special cash dividend is to be paid and subject to such dividend payment being made.

Asset Purchase Agreement with Mylan

We have indemnification obligations to Mylan under the Asset Purchase Agreement that may require us to make future payments to Mylan and other related persons for any damages incurred by Mylan or such related persons as a result of any breaches of our representations, warranties, covenants or agreements contained in the Asset Purchase Agreement, or arising from the Retained Liabilities (as such term is defined in the Asset Purchase Agreement) or certain third party claims specified in the Asset Purchase Agreement. Generally, our representations and warranties survive for a period of 24 months from the closing date, which was March 29, 2017, other than certain fundamental representations which survive until the expiration of the applicable statute of limitations. There is a limited indemnification cap with respect to a majority of the Company's indemnification obligations under the Asset Purchase Agreement with the exception of claims for actual fraud, the breach of any fundamental representations and certain other items, which have a larger indemnification cap (e.g., the purchase price).

Pursuant to the terms of the Asset Purchase Agreement, we, Mylan, and an escrow agent entered into an escrow agreement (the "Escrow Agreement") at closing, pursuant to which Mylan deposited $5 million of the aggregate purchase price for the Cold-EEZE® Business into an escrow account established with the escrow agent in order to satisfy, in whole or in part, certain of our indemnity obligations under the Asset Purchase Agreement. If, on the 18th month anniversary of the closing date, there are funds remaining in the escrow account, then the escrow account will be reduced by the difference, if a positive number, of (i) $2.5 million minus (ii) the aggregate amount of all escrow claims asserted by Mylan prior to this date that have either been paid out of the escrow account or are pending as of such date, and, within two business days of such date, the escrow agent will disburse such difference, if a positive number, to us. Within two business days of the second anniversary of the closing date, the escrow agent will release any funds remaining in the escrow account to us minus any amounts being reserved for escrow claims asserted by Mylan prior to such date. Upon the resolution of any pending escrow claims, the escrow agent will, within two business days of receipt of joint instructions or a final order from a court (as described in the Escrow Agreement) disburse such reserved amount to the parties entitled to such funds.

On May 31, 2018, we received notice of a claim for $800,000 in losses against the escrow amount. We have disputed this claim and intend to vigorously contest such claim. In the event that this or any other indemnity claim is successful, we may be required to pay Mylan such amounts out of escrow fund, pursuant to the indemnification provisions of the Asset Purchase Agreement which may reduce the amount we ultimately collect from escrow or could even require us to return a portion of the net proceeds received from the sale of the Cold-EEZE® Business if the escrow funds are insufficient to cover the losses.

General

As of June 30, 2018, we had working capital of approximately $18.0 million. We believe our current working capital is an acceptable and adequate level of working capital to support our business for at least the next twelve months.

On June 25, 2018, we filed a shelf registration statement with the SEC, which was declared effective on July 5, 2018. The shelf registration statement allows us to issue, from time to time, at prices and on terms to be determined at or prior to the time of an offering, up to $75 million of any combination of an indeterminate number of shares of common stock, preferred stock, warrants and units, subject to certain limitations for so long as our public float is less than $75 million.

Management is not aware of any other trends, events or uncertainties that have or are reasonably likely to have a material negative impact upon our (i) short-term or long-term liquidity, or (ii) net sales or income from continuing operations. Any challenge to our patent or trademark rights could have a material adverse effect on our future; however, we are not aware of any condition that would make such an event probable. Our business is subject to seasonal variations thereby impacting our liquidity and working capital during the course of our fiscal year.

To the extent that we do not generate sufficient cash from operations, our cash balances will decline. We may also use our cash to explore and/or acquire new product technologies, applications, product line extensions, new contract manufacturing applications and other new product opportunities. In the event that our available cash is insufficient to support such initiatives, we may need to incur indebtedness or issue Common Stock to finance plans for growth. Volatility in the credit markets and the liquidity of major financial institutions may have an adverse effect on our ability to fund our business strategy through borrowings, under either existing or newly created instruments in the public or private markets on terms that we believe to be reasonable, if at all.

Off-Balance Sheet Arrangements

It is not our usual business practice to enter into off-balance sheet arrangements such as guarantees on loans and financial commitments and retained interests in assets transferred to an unconsolidated entity for securitization purposes. We have no off-balance sheet arrangements that have, or are reasonably likely to have, a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. Our significant accounting policies are described in Note 2 of the Notes to Condensed Consolidated Financial Statements included under Item 1 of this Part I of this Quarterly Report. However, certain accounting policies are deemed "critical", as they require management's highest degree of judgment, estimates and assumptions. These accounting policies, estimates, and disclosures have been discussed with Audit Committee of our Board of Directors. A discussion of our critical accounting policies and estimates, the judgments and uncertainties affecting their application and the likelihood that materially different amounts would be reported under different conditions or using different assumptions are as follows:

Revenue Recognition – Sales Allowance

When providing for the appropriate sales returns, allowances, cash discounts and cooperative incentive promotion costs ("Sales Allowances"), we apply a uniform and consistent method for making certain assumptions for estimating these provisions. These estimates and assumptions are based on historical experience, current trends and other factors that management believes to be relevant at the time the financial statements are prepared. Management reviews the accounting policies, assumptions, estimates and judgments on a quarterly basis. Actual results could differ from those estimates.

Under ASC 606, the Company shall continue to recognize contract manufacturing and retail customers at a point in time as the Company has an enforceable right to payment for goods as products are shipped to customers.

Pursuant to the Asset Purchase Agreement, we are responsible for and continue to accept product returns of the Cold-EEZE® Business for product shipped prior to March 30, 2017. Additionally, pursuant to the terms of the Asset Purchase Agreement, we allocated and agreed to pay Mylan an aggregate of $400,000 for future a sales returns and allowances arising from certain product returns that were sold by us prior to March 30, 2017.

As of June 30, 2018 and December 31, 2017, we included a provision for sales allowances from continuing operations of $4,000 and $2,000, respectively. Additionally, accrued advertising and other allowances from discontinued operations as of June 30, 2018, included (i) $443,000 for estimated returns and $98,000 for cooperative incentive promotion costs. As of December 31, 2017, accrued advertising and other allowances from discontinued operations included (i) $480,000 for estimated future sales returns and (ii) $200,000 for cooperative incentive promotion costs.

As of June 30, 2018, we have deferred revenue of $52,000 in relation to R&D stability and release testing programs.

Income Taxes

Accounting for income taxes requires recognition of deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities. These deferred taxes are measured by applying the provisions of tax laws in effect at the balance sheet date, including the impact of the Tax Cuts and Jobs Act enacted on December 22, 2017 (the "TCJA"). The TCJA made broad and significant changes to the U.S. Tax Code that affects the year ended December 31, 2017, including, but not limited to, a change in the federal rate from 35% to 21%, effective January 1, 2018.

The Company recognizes in income the effect of a change in tax rates on deferred tax assets and liabilities in the period that includes the TCJA enactment date. We utilize the asset and liability approach which requires the recognition of deferred tax assets and liabilities for the future tax consequences of events that have been recognized in our financial statements or tax returns. In estimating future tax consequences, we generally consider all expected future events other than enactments of changes in the tax law or rates. Until sufficient taxable income to offset the temporary timing differences attributable to operations and the tax deductions attributable to option, warrant and stock activities are assured, a valuation allowance equaling the total net current and non-current deferred tax asset is being provided.

Recently Adopted Accounting Standards

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers" on revenue recognition. The new standard provides for a single five-step model to be applied to all revenue contracts with customers as well as requires additional financial statement disclosures that will enable users to understand the nature, amount, timing and uncertainty of revenue and cash flows relating to customer contracts. Companies have an option to use either a retrospective approach or cumulative effect adjustment approach to implement the standard. We adopted the new standard as of January 1, 2018, using the modified retrospective method. See the Revenue Recognition section within the Summary of Significant Accounting Policies in Note 2 for further details on the impact to the our consolidated financial statements upon adoption and practical expedients elected. The implementation of the new revenue recognition standard did not have a material impact on our consolidated financial statements.

In November 2016, the FASB issued ASU No. 2016-18 "Statement of Cash Flows: Restricted Cash" which requires a statement of cash flows to explain the change during a period in the total cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Under the new standard, amounts generally described as restricted cash and restricted cash equivalents should be included with cash and cash equivalents when reconciling the beginning-of-period and end-of-period total amounts shown in the statement of cash flows. ASU 2016-18 was effective for us as of January 1, 2018. We have not generally had restricted cash or restricted cash equivalents, and there is no restricted cash on the balance sheet as of June 30, 2018. The adoption of this update did not have a material impact on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments." The new standard attempts to reduce diversity in practice in how cash receipts and cash payments are presented and classified in the statement of cash flows. ASU No. 2016-15 provides guidance on eight specific cash flow issues, none of which currently apply to us. The new guidance was effective for us in the first quarter of 2018. The adoption of ASU 2016-15 did not have a material impact on the Company's financial statements.

In October 2016, the FASB issued ASU No. 2016-16, "Income Taxes: Intra-Entity Transfers of Assets Other than Inventory." The new standard requires entities to recognize the income tax consequences of an asset other than inventory when the asset transfer occurs. The new guidance was effective for us in the first quarter of 2018. The adoption of ASU 2016-15 did not have a material impact on the Company's financial statements.

Recently Issued Accounting Standards

In June 2018, the FASB issued Accounting Standards Update (ASU) 2018-07 intended to reduce cost and complexity and to improve financial reporting for nonemployee share-based payments. Currently, the accounting requirements for nonemployee and employee share-based payment transactions are significantly different. This ASU expands the scope of Topic 718, Compensation-Stock Compensation (which currently only includes share-based payments to employees) to include share-based payments issued to nonemployees for goods or services. Consequently, the accounting for share-based payments to nonemployees and employees will be substantially aligned. This ASU supersedes Subtopic 505-50, Equity-Equity-Based Payments to Nonemployees. The amendments in this ASU are effective for public companies for fiscal years beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact of this new standard on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02 "Leases." The new standard will require most leases to be recognized on the balance sheet which will increase reported assets and liabilities. Lessor accounting remains substantially similar to current guidance. The new standard is effective for annual and interim periods in fiscal years beginning after December 15, 2018, which for us is the first quarter of fiscal 2019 and mandates a modified retrospective transition method. We do not intend to early adopt and are currently assessing the impact of this update, but preliminarily believe that its adoption will not have a material impact on our consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments—Credit Losses." The standard modifies the impairment model for most financial assets, including trade accounts receivables and loans, and will require the use of an "expected loss" model for instruments measured at amortized cost. Under this model, entities will be required to estimate the lifetime expected credit loss on such instruments and record an allowance to offset the amortized cost basis of the financial asset, resulting in a net presentation of the amount expected to be collected on the financial asset. The effective date of the standard is for fiscal years beginning after December 15, 2019 with early adoption permitted. We are currently evaluating the impact of adoption of this update on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Like virtually all commercial enterprises, we can be exposed to the risk ("market risk") that the cash flows to be received or paid relating to certain financial instruments could change as a result of changes in interest rate, exchange rates, commodity prices, equity prices and other market changes.

Our operations are not subject to risks of material foreign currency fluctuations, nor do we use derivative financial instruments in our investment practices. We place our marketable investments in instruments that meet high credit quality standards. We do not expect material losses with respect to our investment portfolio or excessive exposure to market risks associated with interest rates. The impact on our results of one percentage point change in short-term interest rates would not have a material impact on our future earnings, fair value, or cash flows related to investments in cash equivalents or interest-earning marketable securities.

Current economic conditions may cause a decline in business and consumer spending which could adversely affect our business and financial performance including the collection of accounts receivables, realization of inventory and recoverability of assets. In addition, our business and financial performance may be adversely affected by current and future economic conditions, including a reduction in the availability of credit, financial market volatility and recession.

Item 4. Controls and Procedures.

Disclosure controls and procedures

We maintain "disclosure controls and procedures," as that term is defined in Rule 13a-15(e), promulgated by the SEC pursuant to the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including the principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurances that the objectives of the control system will be met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. However, our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives.

Our management, under the supervision and with the participation of the principal executive officer and principal accounting and financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this quarterly report on Form 10-Q. Based on this evaluation, our principal executive officer and principal accounting and financial officer concluded that as of June 30, 2018, our disclosure controls and procedures were not effective due to a material weakness identified in our internal control over financial reporting.

A material weakness is a deficiency or a combination of control deficiencies in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

Following the filing of our original 2017 Form 10-K and during the financial statement close process for the quarter ended June 30, 2018 in connection with the preparation of our 2017 Federal and State income tax returns, management identified a material weakness that existed as of June 30, 2018 and at December 31, 2017, primarily related to our lack of adequate controls over the accounting for recording of income tax expense and the allocation of income tax expense/ benefit between continuing and discontinued operations.

Plan for Material Weakness in Internal Control over Financial Reporting

Starting in August 2018, the Company's management has begun to design and implement certain remediation measures to address the above-described material weakness and enhance the Company's internal control over financial reporting. We will take the following actions to improve the design and operating effectiveness of our internal control in order to remediate this material weakness:

As part of our remediation measure, the Company has identified and will implement plans to enhance the Company's process and controls including ensuring adequate, resources, use of tax accounting experts and management oversight with respect to the review of income tax reporting and disclosures.

Changes in internal control over financial reporting

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

Part II. Other Information

Item 1. Legal Proceedings.

The Company is not currently involved in any legal proceeding arising in the normal course of business. From time to time, the Company could become involved in disputes and various litigation matters that arise in the normal course of business. These may include disputes and lawsuits related to intellectual property, licensing, contract law and employee relations matters.

Item 1A. Risk Factors.

There have been no material changes to the risks described in Item 1A. Risk Factors of the 2017 Annual Report filed on Form 10-K/A.

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

None

Item 3. Defaults Upon Senior Securities.

None

Item 4. Mine Safety Disclosures.

Not applicable

Item 5. Other Information.

None

Item 6. Exhibits

Exhibit No.	Description
10.1	2018 Stock Incentive Plan (incorporated by reference to Exhibit 10.1 to the Form 8-K (File No. 000-21617) filed on April 16, 2018)
10.2	Amended and Restated 2010 Equity Compensation Plan (incorporated by reference to Exhibit 10.1 to the Form 8-K (File No. 000-21617) filed on May 24, 2018)
10.3	Amended and Restated 2010 Directors' Equity Compensation Plan (incorporated by reference to Exhibit 10.2 to the Form 8-K (File No. 000-21617) filed on May 24, 2018)
10.4	Stock Option Amendment Agreement with Ted Karkus
31.1	Certification by the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification by the Chief Accounting Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification by the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification by the Chief Accounting Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101. INS#	XBRL Instance Document
101.SCH#	XBRL Taxonomy Extension Schema Document
101.CAL#	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF#	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB#	XBRL Taxonomy Extension Label Linkbase Document
101.PRE#	XBRL Taxonomy Extension Presentation Linkbase Document

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.

ProPhase Labs, Inc.

By: */s/ Ted Karkus*
Ted Karkus
Chairman of the Board and Chief Executive Officer
(Principal Executive Officer)

Date: August 20, 2018

By: */s/ Monica Brady*
Monica Brady
Chief Accounting Officer
(Principal Accounting and Financial Officer)

Date: August 20, 2018

EXHIBIT 10.4

PROPHASE LABS, INC.

STOCK OPTION AMENDMENT AGREEMENT

THIS STOCK OPTION AMENDMENT AGREEMENT (this "**Amendment Agreement**") is made by and among, ProPhase Labs, Inc. ("**ProPhase**" or the "**Company**"), a Delaware corporation, and Ted Karkus (the "**Optionholder**").

RECITALS

WHEREAS, on February 23, 2018, the Company granted a stock option to Optionholder to purchase 2,300,000 shares of the common stock of ProPhase at a price of $3.00 per share (the **"Option")** under the Company's 2018 Stock Incentive Plan (the "**Plan**");

WHEREAS, on May 7, 2018, the Board of Directors (the "**Board**") of ProPhase declared a special cash dividend of $1.00 per share (the "**Dividend**");

WHEREAS, on May 7, 2018, the Compensation Committee of the Board approved a downward adjustment to the exercise price of the Option equal to the per share amount of the Dividend, as permitted under the Plan, which permits certain proportionate adjustments to be made to stock options upon the occurrence of certain events, including a distribution by the Company (whether in the form of cash, shares, other securities, or other property);

WHEREAS, the Board has adjusted the terms of the Option, such that the exercise price of the Option has been reduced from $3.00 per share to $2.00 per share, effective as of June 5, 2018, the date the Dividend was paid; and

WHEREAS, the parties hereto desire to amend the Option to reflect the downward adjustment to the per share exercise price of the Option from $3.00 per share to $2.00 per share, effective as of June 5, 2018.

NOW, THEREFORE, the Option is hereby amended as follows:

1. Exercise Price. The exercise price at which shares of stock shall be purchasable upon exercise of the Option shall be $2 per share (the "**Exercise Price**"), subject to adjustment as provided in the Plan.

2. Except as expressly provided above, the original terms and conditions of the Option shall remain in full force and effect.

3. The Exercise Price represents an amount the Company believes to be no less than the fair market value of a share of Company stock as of the date of this Amendment Agreement, determined in good faith in compliance with the requirements of Section 409A of the Internal Revenue Code of 1986 (as amended). However, there is no guarantee that the Internal Revenue Service ("**IRS**") will agree with the Company's determination. By signing below, Optionholder agrees that the Company, its directors, officers and stockholders shall not be held liable for any tax, penalty, interest or cost incurred by Optionholder as a result of such determination by the IRS.

4. This Amendment Agreement shall be governed by the laws of the State of Delaware as such laws are applied to agreements between Delaware residents entered into and to be performed entirely within the State of Delaware.

5. This Amendment Agreement may be executed in counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

[Remainder of Page Intentionally Left Blank]

IN WITNESS WHEREOF, the Company and the Option holder have executed this Amendment Agreement as of this ___ day of June, 2018.

PROPHASE LABS, INC.	TED KARKUS
By: */s/ Monica Brady*	*/s/ Ted Karkus*
Name: Monica Brady	Signature
Title: Chief Accounting Officer	

EXHIBIT 31.1

OFFICER'S CERTIFICATION PURSUANT TO
RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934

I, Ted Karkus, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of ProPhase Labs, Inc.;

2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report;

3. Based on my knowledge, the financial statements, and other financial information included in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this Quarterly Report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15d-15(f) for the registrant and have:

   (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Quarterly Report is being prepared;

   (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this Quarterly Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 20, 2018

By: */s/ Ted Karkus*
Ted Karkus
Chairman of the Board and Chief Executive Officer
(Principal Executive Officer)

EXHIBIT 31.2

OFFICER'S CERTIFICATION PURSUANT TO
RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934

I, Monica Brady, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of ProPhase Labs, Inc.;

2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report;

3. Based on my knowledge, the financial statements, and other financial information included in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this Quarterly Report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f) and 15d-15(f) for the registrant and have:

   (a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this Quarterly Report is being prepared;

   (b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this Quarterly Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 20, 2018

By: */s/ Monica Brady*
Monica Brady
Chief Accounting Officer
(Principal Accounting and Financial Officer)

EXHIBIT 32.1

PROPHASE LABS, INC.
CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO RULE 13a-14(b) OF THE SECURITIES EXCHANGE ACT OF 1934
AND 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Ted Karkus, Chief Executive Officer of ProPhase Labs, Inc., a Delaware corporation (the "Registrant"), in connection with the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), do hereby represent, warrant and certify, in compliance with Rule 13a-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

/s/ Ted Karkus
Ted Karkus
Chairman of the Board and Chief Executive Officer
(Principal Executive Officer)
August 20, 2018

EXHIBIT 32.2

PROPHASE LABS, INC.
CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO RULE 13a-14(b) OF THE SECURITIES EXCHANGE ACT OF 1934
AND 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Monica Brady, Chief Accounting Officer of ProPhase Labs, Inc., a Delaware corporation (the "Registrant"), in connection with the Registrant's Quarterly Report on Form 10-Q for the period ended June 30, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), do hereby represent, warrant and certify, in compliance with Rule 13a-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Registrant.

/s/ Monica Brady
Monica Brady
Chief Accounting Officer
(Principal Accounting and Financial Officer)
August 20, 2018