SOURCEFIRE INC
Form DEF 14A
April 05, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities
Exchange Act of 1934 (Amendment No.)

Filed by the Registrant þ
Filed by a Party other than the Registrant o
Check the appropriate box:

o Preliminary Proxy Statement
o **Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
þ Definitive Proxy Statement
o Definitive Additional Materials
o Soliciting Material Pursuant to §240.14a-12

SOURCEFIRE, INC.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

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SOURCEFIRE, INC.
9770 Patuxent Woods Drive
Columbia, Maryland 21046

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS
To Be Held On May 26, 2011

Dear Stockholder:

You are cordially invited to attend the Annual Meeting of Stockholders of Sourcefire, Inc., a Delaware corporation (the ***Company***). The meeting will be held on Thursday, May 26, 2011 at 10:00 a.m. local time at the Courtyard by Marriott Columbia, 8910 Stanford Boulevard, Columbia, MD 21045 for the following purposes:

1. To elect the three (3) directors nominated by our Board of Directors and named in the proxy statement to hold office until the 2014 Annual Meeting of Stockholders.

2. To hold an advisory vote on executive compensation.

3. To hold an advisory vote on the frequency of holding an advisory vote on executive compensation.

4. To ratify the selection of Ernst & Young LLP as independent auditors of the Company for its fiscal year ending December 31, 2011.

5. To conduct any other business properly brought before the meeting or any adjournment or postponement thereof.

These items of business are more fully described in the Proxy Statement accompanying this Notice.

On or about April 8, 2011, we will mail a Notice of Internet Availability of Proxy Materials to all stockholders of record entitled to vote at the Annual Meeting, other than those stockholders who previously requested electronic or paper delivery of communications from us. The Notice contains instructions on how to access an electronic copy of our proxy materials, including this proxy statement and our Annual Report. The Notice also contains instructions on how to request a paper copy of the proxy statement.

The record date for the Annual Meeting is March 28, 2011. Only stockholders of record at the close of business on that date may vote at the meeting or any adjournment thereof.

By Order of the Board of Directors

Douglas W. McNitt

Secretary and General Counsel

Columbia, Maryland
April 5, 2011

You are cordially invited to attend the meeting in person. Whether or not you expect to attend the meeting, please complete, date, sign and return the enclosed proxy, or vote over the telephone or the Internet as instructed in these materials, as promptly as possible in order to ensure your representation at the meeting. A

return envelope (which is postage prepaid if mailed in the United States) is enclosed for your convenience. Even if you have voted by proxy, you may still vote in person if you attend the meeting. Please note, however, that if your shares are held of record by a broker, bank or other nominee and you wish to vote at the meeting, you must obtain a proxy issued in your name from that record holder.

Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting of Stockholders to Be Held on May 26, 2011.

The Proxy Statement and Annual Report to Stockholders are available at www.proxyvote.com.

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SOURCEFIRE, INC.
9770 Patuxent Woods Drive
Columbia, Maryland 21046

PROXY STATEMENT
FOR THE 2011 ANNUAL MEETING OF STOCKHOLDERS
May 26, 2011

QUESTIONS AND ANSWERS ABOUT THIS PROXY MATERIAL AND VOTING

What matters will be voted on at the Annual Meeting?

There are four matters scheduled for a vote:

Proposal 1: To elect the three directors nominated by our board of directors and named in this proxy statement as directors to serve for a three year term;

Proposal 2: To hold an advisory vote on executive compensation;

Proposal 3: To hold an advisory vote on the frequency of holding an advisory vote on executive compensation;

Proposal 4: To ratify the appointment of Ernst & Young LLP as independent auditors of the Company for its fiscal year ending December 31, 2011; and

Such other business as may properly come before the Annual Meeting or any adjournment or postponement of the Annual Meeting.

How does the Board of Directors recommend that I vote?

The Board of Directors recommends that you vote:

FOR the election of the three directors nominated by our Board of Directors and named in the proxy statement as directors to serve for a three year term;

FOR the approval, on an advisory basis, of the compensation of our named executive officers;

For, on an advisory basis, an advisory vote on executive compensation once ever three years;

FOR the ratification of the appointment of Ernst & Young LLP as independent auditors of the Company for its fiscal year ending December 31, 2011.

Why am I receiving these materials?

We have delivered these proxy materials to you because the Board of Directors of Sourcefire, Inc. (sometimes referred to as the ***Company*** or ***Sourcefire***) is soliciting your proxy to vote at the 2011 Annual Meeting of Stockholders including at any adjournments or postponements of the meeting. You are invited to attend the annual meeting to vote on the proposals described in this proxy statement. However, you do not need to attend the meeting to vote your shares. Instead, you may simply complete, sign and return the enclosed proxy card, or follow the instructions below to

submit your proxy over the telephone or on the Internet.

Who can vote at the annual meeting?

Only stockholders of record at the close of business on March 28, 2011 will be entitled to vote at the annual meeting. On this record date, there were 28,418,248 shares of common stock outstanding and entitled to vote. Each share of common stock outstanding entitles the holder to one vote on each matter to be voted on at the annual meeting.

Stockholder of Record: Shares Registered in Your Name

If on March 28, 2011 your shares were registered directly in your name with the Company s transfer agent, Continental Stock Transfer and Trust Co., then you are a stockholder of record. As a stockholder of record, you may vote in person at the meeting or vote by proxy. Whether or not you plan to attend the meeting, we urge you to fill out and return the enclosed proxy card or vote by proxy over the telephone or on the Internet as instructed below to ensure your vote is counted.

Beneficial Owner: Shares Registered in the Name of a Broker or Bank

If on March 28, 2011 your shares were held, not in your name, but rather in an account at a brokerage firm, bank, dealer, or other similar organization, then you are the beneficial owner of shares held in street name and these proxy materials are being forwarded to you by that organization. The organization holding your account is considered to be the stockholder of record for purposes of voting at the annual meeting. As a beneficial owner, you have the right to direct your broker or other agent regarding how to vote the shares in your account. If you hold your shares through a broker and you do not give instructions to the record holder on how to vote, the record holder will be entitled to vote your shares in its discretion on certain matters considered routine. The New York Stock Exchange (NYSE) will determine whether the proposals presented at the Annual Meeting are routine or not routine. If a proposal is routine, a broker holding shares for an owner in street name may vote in its discretion on the proposal without receiving voting instructions from the owner. If a proposal is not routine, the broker or other entity may vote on the proposal only if the owner has provided voting instructions. A broker non-vote occurs when the broker is unable to vote on a proposal because the proposal is not routine and the street name owner does not provide any voting instructions. Please follow the voting instructions provided by the organization holding your shares to ensure your vote is counted. Under the rules of the NYSE, your broker does not have the discretion to vote your shares on non-routine matters such as Proposals 1, 2 and 3. However, your broker does have discretion to vote your shares on routine matters such as Proposal 4. You are also invited to attend the annual meeting. However, since you are not the stockholder of record, you may not vote your shares in person at the meeting unless you request and obtain a valid proxy from your broker or other agent.

What if another matter is properly brought before the meeting?

The Board of Directors knows of no other matters that will be presented for consideration at the annual meeting. If any other matters are properly brought before the meeting, it is the intention of the persons named in the accompanying proxy to vote on those matters in accordance with their best judgment.

How do I vote?

The procedures for voting are fairly simple:

Stockholder of Record: Shares Registered in Your Name

If you are a stockholder of record, you may vote in person at the annual meeting, vote by proxy using the enclosed proxy card, vote by proxy over the telephone, or vote by proxy on the Internet. Whether or not you plan to attend the meeting, we urge you to vote by proxy to ensure your vote is counted. You may still attend the meeting and vote in person even if you have already voted by proxy.

To vote in person, come to the annual meeting and we will give you a ballot when you arrive.

To vote using the proxy card, simply complete, sign and date the enclosed proxy card and return it promptly in the envelope provided. If you return your signed proxy card to us before the annual meeting, we will vote your shares as you direct.

To vote over the telephone, dial toll-free 1-800-690-6903 using a touch-tone phone and follow the recorded instructions. You will be asked to provide the control number from your proxy card. Your vote must be received by 11:59 p.m., Eastern Time, on May 25, 2011 to be counted.

To vote on the Internet, go to www.proxyvote.com to complete an electronic proxy card. You will be asked to provide the control number from your proxy card. Your vote must be received by 11:59 p.m., Eastern Time, on May 25, 2011 to be counted.

Beneficial Owner: Shares Registered in the Name of Broker or Bank

If you are a beneficial owner of shares registered in the name of your broker, bank, or other agent, you should have received a proxy card and voting instructions with these proxy materials from that organization rather than from us. Simply complete and mail the proxy card to ensure that your vote is counted. Alternatively, you may vote by telephone or over the Internet as instructed by your broker or bank. To vote in person at the annual meeting, you must obtain a valid proxy from your broker, bank, or other agent. Follow the instructions from your broker or bank included with these proxy materials, or contact your broker or bank to request a proxy form.

We provide Internet proxy voting to allow you to vote your shares on-line, with procedures designed to ensure the authenticity and correctness of your proxy vote instructions. However, please be aware that you must bear any costs associated with your Internet access, such as usage charges from Internet access providers and telephone companies.

How many votes do I have?

On each matter to be voted upon, you have one vote for each share of common stock you own as of March 28, 2011.

What if I return a proxy card but do not make specific choices?

If you return a signed and dated proxy card without marking any voting selections, your shares will be voted FOR the election of the nominees for director, FOR the approval, on an advisory basis, of the compensation of our named executive officers, for a once every three years advisory vote on executive compensation and FOR the ratification of Ernst & Young LLP as independent auditors of the Company for its fiscal year ending December 31, 2011. If any other matter is properly presented at the meeting or any adjournment or postponement thereof, your proxy holder (the individuals named on your proxy card) will vote your shares using his best judgment.

Who is paying for this proxy solicitation?

We will pay for the entire cost of soliciting proxies. In addition to these proxy materials, our directors and employees may also solicit proxies in person, by telephone, or by other means of communication. Directors and employees will not be paid any additional compensation for soliciting proxies. We may also reimburse brokerage firms, banks and other agents for the cost of forwarding proxy materials to beneficial owners.

What does it mean if I receive more than one proxy card?

If you receive more than one proxy card, your shares are registered in more than one name or are registered in different accounts. Please complete, sign and return each proxy card to ensure that all of your shares are voted.

Can I change my vote after submitting my proxy?

Yes. You can revoke your proxy at any time before the final vote at the meeting. If you are the record holder of your shares, you may revoke your proxy in any one of three ways:

You may timely submit before the annual meeting another properly completed proxy card with a later date, or grant a subsequent proxy by telephone or on the Internet.

You may send a timely written notice before the annual meeting that you are revoking your proxy to the Company s Secretary at Sourcefire, Inc., 9770 Patuxent Woods Drive, Columbia, Maryland 21046.

You may attend the annual meeting and vote in person. Simply attending the meeting will not, by itself, revoke your proxy.

Your most current proxy card or telephone or internet proxy is the one that is counted.

If your shares are held by your broker or bank as a nominee or agent, you should follow the instructions provided by your broker or bank.

When are stockholder proposals due for next year s annual meeting?

In accordance with Rule 14a-8 of the Exchange Act, stockholders who wish to present proposals for inclusion in the proxy materials prepared by the Company in connection with the 2012 Annual Meeting of Stockholders must submit their proposals so that they are received by the Company s Secretary at Sourcefire, Inc., 9770 Patuxent Woods Drive, Columbia, Maryland 21046 no earlier than October 8, 2011 and no later than December 7, 2011. However, in the event the date of the 2012 Annual Meeting of Stockholders is advanced or delayed by more than 30 days from the anniversary of the 2011 Annual Meeting of the Stockholders, your proposal must be delivered to the Company s Secretary at the address above by the later of (i) 90 days prior to the date of the 2012 Annual Meeting of Stockholders and (ii) 15 days following the first public announcement of the date of the 2012 Annual Meeting of Stockholders. Any such proposal must comply with the requirements of Rule 14a-8 promulgated under the Exchange Act, which lists the requirements for the inclusion of stockholder proposals in company-sponsored proxy materials.

Timely notice of any proposal, including a director nomination, that you intend to present at the 2012 Annual Meeting of Stockholders, but do not intend to have included in the proxy materials prepared by the Company in connection with the 2012 Annual Meeting of Stockholders, must be delivered in writing to the Company s Secretary at the address above not less than 90 days prior to the date of the 2012 Annual Meeting of Stockholders. In addition, your notice must set forth the information required by our Fifth Amended and Restated Bylaws with respect to each director nomination or other proposal that you intend to present at the 2012 Annual Meeting of Stockholders.

For more information, including the information required to be included in a stockholder proposal, please refer to our Fifth Amended and Restated Bylaws, filed as exhibit 3.2 to our Annual Report on Form 10-K for the fiscal year ended December 31, 2008, filed with the United States Securities and Exchange Commission (the ***SEC***) on March 16, 2009.

What is the quorum requirement?

A quorum of stockholders is necessary to hold a valid meeting. A quorum will be present if stockholders holding at least a majority of the outstanding shares are present at the meeting in person or represented by proxy. On the record date, there were 28,418,248 shares outstanding and entitled to vote. Thus, the holders of 14,209,125 shares must be present in person or represented by proxy at the meeting to have a quorum.

Your shares will be counted towards the quorum only if you submit a valid proxy (or one is submitted on your behalf by your broker, bank or other nominee) or if you vote in person at the meeting. Abstentions and broker non-votes will be counted towards the quorum requirement. If there is no quorum, the holders of a majority of shares present at the meeting in person or represented by proxy may adjourn the meeting to another date.

Abstentions: Abstentions are not counted in the tally of votes FOR or AGAINST a proposal. A WITHHELD vote is the same as an abstention. Abstentions and withheld votes are counted as shares presented and entitled to be voted.

Broker Non-Votes: Brokers or other nominees who hold shares of our common stock for a beneficial owner have the discretion to vote on routine proposals when they have not received voting instructions from the beneficial owner at least ten days prior to the Annual Meeting. A broker non-vote occurs when a broker or other nominee does not receive

voting instructions from the beneficial owner and does not have the discretion to direct the voting of the shares. Broker non-votes will be counted for purposes of calculating whether a quorum is present at the Annual Meeting, but will not be counted for purposes of determining the number of votes present in person or represented by proxy and entitled to vote with respect to a particular proposal. Thus, a broker non-vote will not impact our ability to obtain a quorum and will not otherwise affect the outcome of the vote on a proposal that requires a plurality of votes cast (Proposal 1 or 3) or the approval of a majority of the votes present in person or represented by proxy and entitled to vote (Proposals 2 or 4).

How many votes are needed to approve each proposal?

Proposal	Vote Required	Broker Discretionary Voting Allowed
Proposal 1 Election of three directors to hold office until the 2014 Annual Meeting	Plurality of Votes Cast	No
Proposal 2 Advisory vote on executive compensation	Majority of the Shares Entitled to Vote and Present in Person or Represented by Proxy	No
Proposal 3 Advisory vote on frequency of advisory vote on executive compensation	Plurality of Votes Cast	No
Proposal 4 Ratification of selection of independent auditors for fiscal year 2011	Majority of the Shares Entitled to Vote and Present in Person or Represented by Proxy	Yes

With respect to proposal 2 and 4, you may vote FOR, AGAINST or ABSTAIN. If you ABSTAIN from voting on any of these proposals, the abstention will have the same effect as an AGAINST vote.

With respect to Proposal 1, you may vote FOR all nominees, WITHHOLD your vote as to all nominees, or FOR all nominees except those specific nominees from whom you WITHHOLD your vote. The three nominees receiving the most FOR votes will be elected. A properly executed proxy marked WITHHOLD with respect to the election of one or more directors will not be voted with respect to the director or directors indicated. Proxies may not be voted for more than three directors and stockholders may not cumulate votes in the election of directors.

With respect to Proposal 3, you may vote FOR EVERY YEAR, FOR EVERY TWO YEARS, FOR EVERY THREE YEARS, or ABSTAIN.

If you abstain from voting on Proposals 1 or 3, the abstention will not have an effect on the outcome of the vote.

What proxy materials are available on the internet?

The proxy statement and annual report to stockholders, including our Form 10-K, are available at www.proxyvote.com.

How can I find out the results of the voting at the annual meeting?

Preliminary voting results will be announced at the annual meeting. Final voting results are expected to be published in a Current Report on Form 8-K filed by the Company within four business days following the annual meeting.

PROPOSAL 1

ELECTION OF DIRECTORS

Our Board of Directors is divided into three classes. Each class consists, as nearly as possible, of one-third of the total number of directors, and each class has a three-year term. Vacancies on the Board may be filled only by persons elected by a majority of the remaining directors. A director elected by the Board to fill a vacancy in a class, including a vacancy created by an increase in the number of directors, shall serve for the remainder of the full term of that class and until the director s successor is elected and qualified.

The Board of Directors currently has seven members. There are currently three (3) directors in the class whose term of office expires in 2011. Each of John C. Burris, Tim A. Guleri and Martin F. Roesch has been nominated for election as a director at the 2011 Annual Meeting. Each of Messrs. Burris, Guleri and Roesch is currently a director of the Company who was previously elected by the stockholders. If elected at the annual meeting, each of these nominees would serve until the 2014 Annual Meeting and until his successor is elected and has qualified, or, if sooner, until the director s death, resignation or removal.

Following our 2007 Annual Meeting of Stockholders, we adopted a policy to encourage our directors and nominees for director to attend our annual meetings. All of our seven current directors who were then serving attended the 2010 Annual Meeting of Stockholders.

Directors are elected by a plurality of the votes of the holders of shares present in person or represented by proxy and entitled to vote on the election of directors. The three (3) nominees receiving the highest number of affirmative votes will be elected. Shares represented by executed proxies will be voted, if authority to do so is not withheld, for the election of the three nominees named below. If any nominee becomes unavailable for election as a result of an unexpected occurrence, your shares may be voted for the election of a substitute nominee proposed by us. Each person nominated for election has agreed to serve if elected. Our management has no reason to believe that any nominee will be unable to serve.

The following is a brief biography of each nominee and each director whose term will continue after the annual meeting.

Nominees for Election for a Three-Year Term Expiring at the 2014 Annual Meeting

John C. Burris

John C. Burris, age 56, joined our Board of Directors in March 2008 and became our Chief Executive Officer in July 2008. Mr. Burris served as Senior Vice President, Worldwide Sales and Services of Citrix Systems, Inc., a publicly traded information technology company specializing in application delivery infrastructure, from January 2001 to July 2008. From July 1999 to January 2001, Mr. Burris served as Senior Vice President, Services of Citrix Systems. Prior to joining Citrix Systems, Mr. Burris was employed by Lucent Technologies, a publicly traded communications networks company, from 1994 to 1999 as Vice President and General Manager of the Gulf States region. Prior to 1994, Mr. Burris was employed in various customer service capacities for AT&T Corp., including a term as managing director for AT&T s Asia/Pacific region. Mr. Burris also serves on the board of directors of Qlik Technologies, Inc.

Mr. Burris brings extensive leadership, management, sales and corporate development experience to our Board of Directors. In addition, in his position as our Chief Executive Officer, Mr. Burris has comprehensive knowledge of our

operations.

Tim A. Guleri

Tim A. Guleri, age 46, joined our Board of Directors in June 2002 and is currently a Managing Director with Sierra Ventures. Before joining Sierra Ventures in February 2001, Mr. Guleri was the Vice Chairman and Executive Vice President with Epiphany, Inc. from March 2000 until February 2001; the Chairman, CEO and Co-founder of Octane Software Inc. from September 1997 until March 2000; Vice President of Field Operations, Product Marketing with Scopus Technology Inc. from February 1992 until February 1996; and was part of the information technology team with LSI Logic Corporation from September 1989 until September 1991. He has been a director

of: Octane Software from 1997 to 2000 (sold to Epiphany in 2000); Net6, Inc. from March 2001 to March 2004 (acquired by Citrix Systems, Inc. in 2004); Approva Corporation since April 2005; CodeGreen Networks, Inc. since March 2005; AIRMEDIA, Inc. from April 2005 to 2007 (acquired by AOL in 2007); and Greenplum, Inc. since November 2006. Mr. Guleri holds a B.S. in Electrical Engineering from Punjab Engineering College, India and an M.S. in Engineering and Operational Research from Virginia Tech.

Mr. Guleri brings to our Board of Directors industry experience in information security, leadership and management experience as a former Chief Executive Officer, and experience as a board member of multiple companies.

Martin F. Roesch

Martin F. Roesch, age 41, has served on our Board of Directors since he founded Sourcefire in January 2001 and served as our President until September 2002, and has continued to serve as our Chief Technology Officer since that time. Mr. Roesch is responsible for our technical direction and product development efforts. Mr. Roesch, who has 18 years of industry experience in network security and embedded systems engineering, is also the author and lead developer of the Snort Intrusion Prevention and Detection System that forms the foundation for the Sourcefire 3D System. Over the past 12 years, Mr. Roesch has developed various network security tools and technologies, including intrusion prevention and detection systems, honeypots, network scanners and policy enforcement systems for organizations such as GTE Internetworking and Stanford Telecommunications, Inc. Mr. Roesch holds a B.S. in Electrical and Computer Engineering from Clarkson University.

Mr. Roesch brings to our Board of Directors industry leadership and experience in developing technology as the founder of Sourcefire and our Chief Technology Officer.

The Board Of Directors Recommends
A Vote FOR Approval Of the Director Nominees Named Above.

Directors Continuing in Office Until the 2012 Annual Meeting

Steven R. Polk

Lt. Gen. Steven R. Polk (ret.), age 64, joined our Board of Directors in August 2006 and was named Chairman of the Board in February 2009. General Polk retired from the Air Force on February 1, 2006, after a distinguished career of over 37 years. His last duty assignment was as the Air Force Inspector General. General Polk is the National Commander and Chairman of the Board of the Order of Daedalians and co-chairs the Air Force Retiree Council. General Polk graduated from the United States Air Force Academy with a B.S. in aeronautical engineering. Additionally, he holds an M.S. in engineering from Arizona State University and an M.A. in national security and strategic studies from the Naval War College.

General Polk brings global leadership and management experience to our Board of Directors as well as an in-depth knowledge of the purchasing practices of the United States military.

Michael Cristinziano

Michael Cristinziano, age 46, joined our Board of Directors in March 2009. Mr. Cristinziano is Corporate Vice President, Strategic Development at Citrix Systems, where he is responsible for several corporate finance functions, including M&A strategy and execution, technology licensing, strategic venture investments and investor relations. Mr. Cristinziano also serves as a member of the Citrix CTO Office. Prior to joining Citrix Systems in 2003, Mr. Cristinziano was Managing Director for Harris Nesbitt, the U.S. investment banking arm of BMO Financial

Group, where he covered the networking and software industries. Before joining Harris Nesbitt in 1997, Mr. Cristinziano worked as a research analyst at Needham & Co. Prior to that he was a member of the technical staff at Bellcore. Mr. Cristinziano also serves on the board of directors of Bridgewater Systems Corporation. Mr. Cristinziano holds a B.S. in Electrical Engineering from Temple University, an M.S. in Systems Engineering from the University of Pennsylvania and completed post-graduate studies at Carnegie Mellon University.

Mr. Cristinziano brings industry, corporate development and investor relations experience to our Board of Directors.

Directors Continuing in Office Until the 2013 Annual Meeting

John C. Becker

John C. Becker, age 53, joined our Board of Directors in March 2008. Mr. Becker has served as Chief Executive Officer of Approva Corporation since October 2008. Previously, Mr. Becker served as Chief Executive Officer of Cybertrust, Inc., an information security services company, from November 2004 until its acquisition by Verizon Business, a business unit of Verizon Communications, in July 2007. From November 2002 to November 2004, Mr. Becker was Chairman and Chief Executive Officer of TruSecure Corporation, an information security services company, which merged with Betrusted Holdings, Inc. to form Cybertrust. From 2000 to 2002, Mr. Becker was a consultant to venture capital and technology firms. Beginning in 1995, he held a series of executive positions with AXENT Technologies, Inc., a publicly traded information security software and services company, including Executive Vice President, Chief Financial Officer and Treasurer. In 1996, Mr. Becker became President and Chief Operating Officer and a director of AXENT and was instrumental in leading AXENT to an initial public offering in 1996. In 1997, Mr. Becker was appointed as Chief Executive Officer of AXENT and became chairman of its board of directors in 1999, holding such positions until the sale of AXENT to Symantec Corporation in 2000. Prior to AXENT, he held various positions involving financial matters at Raxco Software, Marriott Corporation and MCI Communications, Inc. Mr. Becker holds a Bachelor of Science degree in Business Administration from the University of Richmond.

Mr. Becker brings leadership, management and industry experience to our Board of Directors, including experience as a Board member, Chief Executive Officer, Chief Operating Officer and Chief Financial Officer of various technology companies. In addition, our Board of Directors has determined that Mr. Becker s educational background and professional experience qualify him as an audit committee financial expert.

Arnold L. Punaro

Maj. Gen. Arnold L. Punaro (ret.), age 64, originally joined our Board of Directors in January 2007 and his term expired in May 2009. He rejoined our Board in May 2010. General Punaro is chief executive officer of the Punaro Group, LLC, a Washington-based firm offering government relations, strategic planning, federal budget and market analysis, communications, crisis and emergency management, business development and sensitive operations consulting. Previously, General Punaro served as Executive Vice President, Government Affairs, Communications and Support Operations and General Manager of Washington Operations for Science Applications International Corporation, or SAIC. He is also a Senior Fellow on Secretary of Defense Gates Defense Business Board and previously chaired the Statutory Commission on the National Guard and Reserves. Prior to joining SAIC in 1997, General Punaro worked for Senator Sam Nunn on national security matters from 1973 to 1997. During that time, General Punaro served as Senator Nunn s director of national security affairs and as staff director of the Senate Armed Services Committee. General Punaro served as the director of the Marine Corps Reserve from May 2001 until his retirement in October 2003. General Punaro also served as deputy commanding general, Marine Corps Combat Development Command (Mobilization) from August 2000 until May 2001, and as the commanding general of the 4th Marine Division headquartered in New Orleans, Louisiana from 1997 to 2000. General Punaro served on active duty as an infantry platoon commander in Vietnam where he was awarded the Bronze Star for valor and the Purple Heart. As a reserve officer, he has served in Operation Desert Shield in Saudi Arabia in December 1990, Joint Task Force Provide Promise (Forward) in the former Yugoslavia in December 1993, Operation Enduring Freedom and Operation Iraqi Freedom in May 2003 and has served as both the Headquarters Marine Corps Director of Reserve Affairs and as the Special Assistant to the Commander, U.S. European Command. Since November 2009, General Punaro has also served on the Board of Directors of DesignLine Corporation, a manufacturer of hybrid, electric,

alternative fuel and diesel mass transit buses, as well as electric trolleys, which was publicly traded until January 2010. General Punaro holds a B.S. from Spring Hill College in Mobile, Alabama, an M.A. in journalism from the University of Georgia and an M.A. in national security studies from Georgetown University.

General Punaro brings leadership and management experience to our Board of Directors gained during both his military career and as an executive of a publicly-traded company. In addition, General Punaro has extensive knowledge regarding our federal sector business.

INFORMATION REGARDING THE BOARD OF DIRECTORS AND CORPORATE GOVERNANCE

Independence of the Board of Directors

Under the NASDAQ Stock Market ***(NASDAQ***) listing standards, a majority of the members of a listed company s Board of Directors must qualify as independent, as affirmatively determined by the Board of Directors. The Board consults with the Company s counsel to ensure that the Board s determinations are consistent with relevant securities and other laws and regulations regarding the definition of independent, including those set forth in pertinent listing standards of the NASDAQ, as in effect time to time.

Consistent with these considerations, after review of all relevant identified transactions or relationships between each director, or any of his or her family members, and the Company, its senior management and its independent auditors, the Board has affirmatively determined that the following five directors are independent directors within the meaning of the applicable NASDAQ listing standards: John C. Becker, Michael Cristinziano, Tim A. Guleri, Steven R. Polk and Arnold L. Punaro. In making this determination, the Board found that none of these directors had a material or other disqualifying relationship with us. John C. Burris, our Chief Executive Officer, and Martin F. Roesch, our Chief Technology Officer, are not independent directors by virtue of their employment with us.

Meetings of the Board of Directors

The Board of Directors met nine (9) times during the last fiscal year. Each Board member attended 75% or more of the aggregate of the meetings of the Board and of the committees on which he served, held during the period for which he was a director or committee member.

As required under applicable NASDAQ listing standards, in fiscal 2010, the Company s independent directors met five (5) times in regularly scheduled executive sessions at which only independent directors were present.

Board Leadership Structure

We currently have a separate Chief Executive Officer and Chairman of the Board, with Mr. Burris serving as Chief Executive Officer and Mr. Polk serving as Chairman of the Board. Although Mr. Burris serves as a member of the Board, we believe that Mr. Polk s status as Chairman and as an independent director provides for a meaningful division of leadership between the Chief Executive Officer and the Board.

The Chief Executive Officer is responsible for setting the strategic direction for the Company and for the day-to-day leadership and performance of the Company, while the Chairman provides guidance to the Chief Executive Officer, sets the agenda for Board meetings and presides over all meetings of the Board, including executive sessions. We believe this has been an effective model for the Company. This structure ensures a greater role for the independent directors in the oversight of the Company and active participation of the independent directors in setting agendas and establishing priorities and procedures for the work of the Board.

Oversight of Risk Management

The Board has an active role, as a whole and also at the committee level, in overseeing management of the Company s risks. The Board regularly reviews information regarding the Company s strategy, finances and operations, as well as

the risks associated with each. The Audit Committee is responsible for oversight of Company risks relating to accounting matters, financial reporting and legal and regulatory compliance. The Audit Committee meets with management, including the Company s internal auditor and legal counsel, as well as the Company s independent registered public accounting firm, to review and evaluate these risks. The Audit Committee regularly reports to the full Board on its proceedings and actions, and makes recommendations as it deems appropriate. In addition, the Nominating and Governance Committee manages risks associated with the

independence of the Board and potential conflicts of interest. The Company s Compensation Committee is responsible for overseeing the management of risks relating to the Company s executive compensation plans and arrangements. While each committee is responsible for evaluating certain risks and overseeing the management of such risks, the entire Board is regularly informed through committee reports about such risks.

Information Regarding Committees of the Board of Directors

The Board has three committees: an Audit Committee, a Compensation Committee, and a Nominating and Governance Committee. The following table provides current membership and fiscal 2010 meeting information for each of the Board committees.

Name	Audit	Compensation	Nominating and Governance
John C. Becker	X*	X	
Tim A. Guleri		X *	
Steven R. Polk		X	X*
Michael Cristinziano	X		X
Arnold L. Punaro	X		X
Total meetings in fiscal 2010	12	11	7

* Committee Chairperson

Below is a description of each committee of the Board of Directors. Each of the committees has authority to engage legal counsel or other experts or consultants, as it deems appropriate to carry out its responsibilities. The Board of Directors has determined that each member of each committee meets the applicable NASDAQ rules and regulations regarding independence and that each member is free of any relationship that would impair his individual exercise of independent judgment with regard to the Company.

Audit Committee

The Audit Committee of the Board of Directors was established by the Board in accordance with Section 3(a)(58)(A) of the Securities Exchange Act of 1934 to oversee the Company s corporate accounting and financial reporting processes and audits of its financial statements. For this purpose, the Audit Committee performs several functions. The Audit Committee is responsible for the appointment, compensation, retention and oversight of the work of the independent auditors, oversees the Company s accounting and financial reporting processes and the audits of the Company s financial statements, establishes policies and procedures for review and pre-approval by the Committee of all audit services and permissible non-audit services to be performed by the Company s independent auditors, oversees the rotation of the audit partners of the Company s independent auditors as required by law, reviews and approves or rejects transactions between the Company and related persons, evaluates and confers with management regarding the adequacy and effectiveness of internal controls over financial reporting that could significantly affect the Company s financial statements, as well as the adequacy and effectiveness of the Company s disclosure controls and procedures and management s reports thereon, establishes procedures as required by law for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters and the confidential, anonymous submission by employees of the Company of concerns regarding questionable accounting or auditing matters and reviews with management and the Company s independent auditors the Company s annual audited

and quarterly interim financial statements (including disclosures made under Management s Discussion and Analysis of Financial Condition and Results of Operations) prior to the filing with the SEC of any report containing such financial statements.

The Board of Directors has determined that Mr. Becker qualifies as an audit committee financial expert under the SEC rule implementing Section 407 of the Sarbanes-Oxley Act of 2002. The Board made a qualitative assessment of Mr. Becker s level of knowledge and experience based on a number of factors, including his formal education and experience.

The Board of Directors reviews the NASDAQ listing standards definition of independence for Audit Committee members on an annual basis and has determined that all members of our Audit Committee are independent, as independence is currently defined in Marketplace Rule 5605(a)(2) of the NASDAQ Stock Market.

The Audit Committee has adopted a written charter that is available to stockholders on our website at http://investor.sourcefire.com.

Report of the Audit Committee of the Board of Directors[1]

The Audit Committee has reviewed and discussed the audited financial statements for the fiscal year ended December 31, 2010 with our management. The Audit Committee has discussed with the independent auditors the matters required to be discussed by Statement on Auditing Standards No. 114, *The Auditor s Communication with Those Charged with Governance*, as adopted by the Public Company Accounting Oversight Board (***PCAOB***) in Rule 3200T. The Audit Committee has also received the written disclosures and the letter from the independent accountants required by the applicable requirements of the PCAOB regarding the independent auditors communications with the Audit Committee concerning independence and has discussed with the independent auditors the independent auditors independence. Based on the foregoing, the Audit Committee has recommended to the Board of Directors that the audited financial statements at and for the fiscal year ended December 31, 2010 be included in our Annual Report on Form 10-K filed with the SEC for the year ended December 31, 2010.

Mr. John C. Becker, Chairman
Mr. Michael Cristinziano
Maj. Gen. Arnold L. Punaro (ret.)

(1,676

)

2,349

Interest expense, net

(134

)

(130

)

(414

)

(371

)

Income(loss) before income taxes

361 *980* *(2,090*

)

1,978

INCOME TAX EXPENSE (BENEFIT)

73 *(127*

)

33 *(105*

)

NET INCOME (LOSS)

$*288* $*1,107* $*(2,123*

)

$*2,083*

NET INCOME (LOSS) PER SHARE:

Basic

$*0.05* $*0.19* $*(0.37*

)

$*0.36*

Diluted

$*0.05* $*0.19* $*(0.37*

)

$*0.36*

SHARES USED IN CALCULATION OF NET INCOME (LOSS) PER SHARE:

Basic

5,836	*5,749*	*5,809*	*5,714*

Diluted

5,862	*5,831*	*5,809*	*5,774*

See accompanying Notes to Condensed Consolidated Financial Statements.

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CYANOTECH CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

	Nine Months Ended December 31,	
	2018	**2017**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net (loss) income	$(2,123)	$2,083
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation and amortization	1,421	1,403
Share-based compensation expense	282	369
Amortization of debt issue costs and other assets	57	52
Net (increase) decrease in assets:		
Accounts receivable	781	(791)
Inventories	(1,078)	(1,730)
Prepaid expenses and other assets	(84)	(86)
Net increase (decrease) in liabilities:		
Accounts payable	528	(76)
Accrued expenses	181	332
Customer deposits	39	(80)
Other long-term liabilities	(46)	(8)
Net cash (used in) provided by operating activities	(42)	1,468
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment in equipment and leasehold improvements	(375)	(667)
Investment in Cellana asset purchase	(100)	—
Investment in restricted cash	—	(65)
Net cash used in investing activities	(475)	(732)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net draws (payments) on line of credit	1,250	(111)
Payments on short term contract obligation	(63)	—
Payments on capitalized leases	(49)	(67)
Principal payments on long-term debt	(429)	(394)
Proceeds from long-term debt, net of costs	—	166
Withholding on restricted stock unit vesting	(32)	—
Proceeds from stock options exercised	19	26
Net cash provided by (used in) financing activities	696	(380)

Net increase in cash	*179*	*356*
Cash and restricted cash at beginning of period	*1,394*	*1,407*
Cash at end of period	$*1,573*	$*1,763*
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$*358*	$*313*
Income taxes	$*17*	$—
Purchase of Cellana assets	$*495,000*	$—
Less: Issuance of short-term obligation	*395,000*	—
Cash paid to acquire Cellana assets	$*100,000*	$—

See accompanying Notes to Condensed Consolidated Financial Statements.

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CYANOTECH CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018

(Unaudited)

_1._ ORGANIZATION AND BASIS OF PRESENTATION

Cyanotech Corporation (the “Company”), located in Kailua-Kona, Hawaii, was incorporated in the state of Nevada on *March 3, 1983* and is listed on the NASDAQ Global Select Market under the symbol “CYAN”. The Company is engaged in the production of natural products derived from microalgae for the nutritional supplements market.

The Company is an agricultural company that produces high value natural products derived from microalgae grown in complex and intricate open-pond agricultural systems on the Kona coast of Hawaii. The Company's products include Hawaiian Spirulina Pacifica, a superfood with numerous benefits, including boosting the immune system and overall cellular health; and Hawaiian BioAstin, a powerful antioxidant shown to support and maintain the body's natural inflammatory response.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information pursuant to the instructions to Form *10*-Q and Regulation S-*X* of the Securities and Exchange Commission (SEC). These interim condensed consolidated financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary to present fairly the Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Operations, and Condensed Consolidated Statements of Cash Flows for the periods presented in accordance with GAAP.

Accordingly, they do *not* include all of the information and notes required by GAAP for complete financial statements. The results of operations for the interim periods are *not* necessarily indicative of the results to be expected for the full fiscal year. The Condensed Consolidated Balance Sheet as of *March 31, 2018* was derived from the audited consolidated financial statements. These condensed consolidated financial statements and notes should be read in conjunction with the Company’s audited consolidated financial statements for the year ended *March 31, 2018,* contained in the Company’s annual report on Form *10*-K as filed with the SEC on *June 15, 2018.*

2. SIGNIFICANT ACCOUNTING POLICIES

Consolidation

The accompanying condensed consolidated financial statements include the accounts of Cyanotech Corporation and its wholly owned subsidiary, Nutrex Hawaii, Inc. ("Nutrex Hawaii" or "Nutrex", collectively the "Company"). All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosures of any contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the periods reported. Management reviews these estimates and assumptions periodically and reflects the effect of revisions in the period that they are determined to be necessary. Actual results could differ from those estimates and assumptions.

Cash and Restricted Cash

The Company considers only its monetary liquid assets with original maturities of *three* months or less as cash and cash equivalents. Proceeds from equipment loans are classified as restricted cash until drawn upon.

The following table provides a reconciliation of cash and restricted cash reported within the Company's consolidated balance sheets to the total amount presented in the consolidated statement of cash flows:

	December 31, 2018	**March 31, 2018**
	(in thousands)	
Cash	$*1,329*	$*1,407*
Restricted Cash	*65*	—
Cash and restricted cash at beginning of period	$*1,394*	$*1,407*
Cash	$*1,573*	$*1,329*
Restricted Cash	—	*65*

Cash and restricted cash at end of period	$*1,573*	$*1,394*

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Concentration of Accounts Receivable and Revenues

At *December 31, 2018, 67%* of the Company's accounts receivable was comprised of *two* customer balances of *43%* and *24%,* respectively. At *March 31, 2018, 76%* of the Company's accounts receivable was comprised of *three* customer balances of *45%, 16%* and *15%,* respectively. Two customers accounted for *66%* of total net sales for the *three* months ended *December 31, 2018,* comprised of *35%* and *31%,* respectively. Two customers accounted for *50%* of total net sales for the *three* months ended *December 31, 2017,* comprised of *26%* and *24%,* respectively. Two customers accounted for *62%* of total net sales for the *nine* months ended *December 31, 2018,* comprised of *35%* and *27%,* respectively. Two customers accounted for *47%* of total net sales for the *nine* months ended *December 31, 2017,* comprised of *30%* and *17%,* respectively.

Revenue Recognition

The Company records revenue based on the *five*-step model which includes: (*1*) identifying the contract with the customer; (*2*) identifying the performance obligations in the contract; (*3*) determining the transaction price; (*4*) allocating the transaction price to the performance obligations; and (*5*) recognizing revenue when the performance obligations are satisfied. Substantially all of the Company's revenue is generated by fulfilling orders for the purchase of our micro algal nutritional supplements to retailers, wholesalers, or direct to consumers via online channels, with each order considered to be a distinct performance obligation. These orders *may* be formal purchase orders, verbal phone orders, e-mail orders or orders received online. Shipping and handling activities for which the Company is responsible under the terms and conditions of the order are *not* accounted for as performance obligations but as fulfillment costs. These activities are required to fulfill the Company's promise to transfer the goods and are expensed when revenue is recognized. The impact of this policy election is insignificant as it aligns with our current practice.

Revenue is measured as the net amount of consideration expected to be received in exchange for fulfilling a performance obligation. The Company has elected to exclude sales, use and similar taxes from the measurement of the transaction price. The impact of this policy election is insignificant, as it aligns with our current practice. The amount of consideration expected to be received and revenue recognized includes estimates of variable consideration, which includes costs for trade promotion programs, coupons, returns and early payment discounts. Such estimates are calculated using historical averages adjusted for any expected changes due to current business conditions and experience. The Company reviews and updates these estimates at the end of each reporting period and the impact of any adjustments are recognized in the period the adjustments are identified. In assessing whether collection of consideration from a customer is probable, the Company considers the customer's ability and intent to pay that amount of consideration when it is due. Payment of invoices is due as specified in the underlying customer agreement, typically *30* days from the invoice date, which occurs on the date of transfer of control of the products to the customer. Revenue is recognized at the point in time that control of the ordered products is transferred to the customer. Generally, this occurs when the product is delivered, or in some cases, picked up from *one* of our distribution centers by the customer.

Customer contract liabilities consist of customer deposits received in advance of fulfilling an order and are shown separately on the consolidated balance sheets. During the *three*-month periods ended *December 31, 2018* and *December 31, 2017,* the Company recognized *$0* and *$20,000,* respectively, of revenue from deposits that were included in contract liabilities as of *March 31, 2018* and *March 31, 2017,* respectively. During the *nine*-month periods ended *December 31, 2018* and *December 31, 2017,* the Company recognized *$114,000* and *$91,000,* respectively, of revenue from deposits that were included in contract liabilities as of *March 31, 2018* and *March 31, 2017,* respectively. The Company's contracts have a duration of *one* year or less and therefore, the Company has elected the practical expedient of *not* disclosing revenues allocated to partially unsatisfied performance obligations.

Disaggregation of Revenue

The following table represents revenue disaggregated by product in the *three* and *nine* months ended *December 31, 2018* and *December 31, 2017 (*in thousands):

	Three months ended December 31, 2018			Nine months ended December 31, 2018		
	Astaxanthin	Spirulina	Total	Astaxanthin	Spirulina	Total
Packaged products	$*6,012*	$ *3,212*	$*9,224*	$*15,388*	$ *6,208*	$*21,596*
Bulk products	*287*	*533*	*820*	*884*	*1,663*	*2,547*
Total	$*6,299*	$ *3,745*	$*10,044*	$*16,272*	$ *7,871*	$*24,143*

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	Three months ended December 31, 2017			Nine months ended December 31, 2017		
	Astaxanthin	Spirulina	Total	Astaxanthin	Spirulina	Total
Packaged products	$*5,746*	$ *2,268*	$*8,014*	$*15,649*	$ *6,560*	$*22,209*
Bulk products	*317*	*819*	*1,136*	*748*	*3,057*	*3,805*
Total	$*6,063*	$ *3,087*	$*9,150*	$*16,397*	$ *9,617*	$*26,014*

Reclassification

Certain amounts previously reported in the fiscal *2018* consolidated financial statements have been reclassified to conform with the fiscal *2019* financial presentation. These reclassifications have *no* impact on net income.

Recently Adopted Accounting Pronouncements

In *May 2017,* the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") *2017-09, Compensation-Stock Compensation (Topic 718) Scope of Modification Accounting* ("ASU *No. 2017-09"*). ASU *No. 2017-09* will clarify and reduce both (i) diversity in practice and (ii) cost and complexity when applying the guidance in Topic *718,* to a change to the terms and conditions of a share-based payment award. This guidance became effective for fiscal years beginning after *December 15, 2017* and interim periods within those fiscal years. The amendments in ASU *No. 2017-09* are applied prospectively to awards modified on or after the adoption date. The Company adopted this standard as of *April 1, 2018* with *no* impact on its consolidated financial statements.

In *November 2016,* the FASB issued ASU *2016-18,* "*Statement of Cash Flows (Topic 230): Restricted Cash"* ("ASU *No. 2016-18"*). This update addresses the fact that diversity exists in the classification and presentation of changes in restricted cash on the statement of cash flows under Topic *230, Statement of Cash Flows*. ASU *No. 2016-18* became effective for public companies for the fiscal years beginning after *December 15, 2017,* and interim periods within those fiscal years. The Company adopted this standard as of *April 1, 2018* by using the retrospective method, which required reclassification of restricted cash in the accompanying consolidated statement of cash flows as of the beginning of the period for the *nine* months ended *December 31, 2018.*

In *August 2016,* FASB issued ASU *2016-15,* "*Statement of Cash Flows (Topic 230)*: *Classification of Certain Cash Receipts and Cash Payments"* ("ASU *No. 2016-15"*). ASU *No. 2016-15* clarifies and provides specific guidance on *eight* cash flow classification issues that are *not* currently addressed by current GAAP and thereby reduces the current diversity in practice. ASU *No. 2016-15* is effective for public business entities for annual periods, including interim periods within those annual periods, beginning after *December 15, 2017.* The Company adopted this standard as of *April 1, 2018* with *no* impact on its consolidated financial statements and related disclosures.

In *May 2014,* the FASB issued their converged standard on revenue recognition, Accounting Standards Update *No. 2014-09,* "*Revenue from Contracts with Customers (Topic 606)"*("ASU *No. 2014-09"*), updated in *December 2016* with the release of ASU *2016-20.* This standard outlines a single comprehensive model for companies to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods and services in an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods and services. In addition, the new standard requires that reporting companies disclose the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. In *August 2015,* the FASB issued ASU *No 2015-14* "*Revenue from Contracts with Customers (Topic 606*): *Deferral of the Effective Date,*" which deferred the effective date of ASU *No. 2014-09* to annual reporting periods beginning after *December 15, 2017.*

The new revenue standard is required to be applied either retrospectively to each prior reporting period presented or prospectively with the cumulative effect of initially applying the standard recognized at the date of the initial application, supplemented with certain disclosures related to the effect of adoption on previously reported amounts, if any (the modified retrospective method). The Company adopted the standard on *April 1, 2018* for contracts that were *not* completed before the adoption date, using the modified retrospective method. The Company has evaluated the effect of the standard and concluded it is *not* material to the timing or amount of revenues or expenses recognized in the Company's historical consolidated financial statements. As a result, the Company has concluded that the application of the standard does *not* have a material effect that requires a retrospective adjustment to any previously reported amounts in the Company's historical consolidated financial statements for reporting disclosure purposes.

Recently Issued Accounting Pronouncements

In *November 2018,* the FASB issued ASU *2018-18 – Collaborative Arrangements*, which clarifies that certain transactions between collaborative arrangement participants should be accounted for as revenue when the collaborative arrangement participant is a customer in the context of a unit of account and precludes recognizing as revenue consideration received from a collaborative arrangement participant if the participant is *not* a customer. This ASU will be effective for us in the *first* quarter of fiscal *2021* with early adoption permitted. This ASU requires retrospective adoption to the date we adopted ASC *606, April 1, 2018,* by recognizing a cumulative-effect adjustment to the opening balance of retained earnings of the earliest annual period presented. The Company is currently evaluating the impact of the adoption of this standard on its financial statements.

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In *August 2018,* the FASB issued ASU *2018-15,* "*Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract"* ("ASU *No. 2018-15"*), which aligns the capitalization requirements for implementation costs incurred in a hosting arrangement that is a service contract with the existing capitalization requirements for implementation costs incurred to develop or obtain internal-use software *(Subtopic 350-40).* ASU *2018-15* becomes effective for the Company in the *first* quarter of fiscal *2021* and *may* be adopted either retrospectively or prospectively. Early adoption is permitted. The Company is currently evaluating the impact of the adoption of this standard on its financial statements.

In *August 2018,* the FASB issued ASU *2018-13,* "*Fair Value Measurement - Disclosure Framework (Topic 820)"* ("ASU *No. 2018-13"*)The updated guidance improves the disclosure requirements on fair value measurements. The updated guidance is effective for fiscal years, and interim periods within those fiscal years, beginning after *December 15, 2019.* Early adoption is permitted for any removed or modified disclosures. The Company is currently assessing the timing and impact of adopting the updated provisions.

In *June 2018,* the FASB issued ASU *2018-07,* "*Compensation - Stock Compensation (Topic 718)"* ("ASU *No. 2018-07"*): Improvements to Nonemployee Share-Based Payment Accounting. ASU *No. 2018-07* expands the scope of Topic *718* to include share-based payment transactions for acquiring goods and services from non-employees, and as a result, the accounting for share-based payments to non-employees will be substantially aligned. ASU *No. 2018-07* is effective for fiscal years beginning after *December 15, 2018,* including interim periods within that fiscal year. Early adoption is permitted but *no* earlier than an entity's adoption date of Topic *606.* The Company is currently evaluating the impact this new guidance will have on its financial statements and related disclosures.

In *February 2016,* the FASB issued ASU *2016-02,* "*Leases (Topic 842)"* (*"*ASU *No. 2016-02"*). The principle objective of ASU *No. 2016-02* is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet. ASU *No. 2016-02* continues to retain a distinction between finance and operating leases but requires lessees to recognize a right-of-use asset representing its right to use the underlying asset for the lease term and a corresponding lease liability on the balance sheet for all leases with terms greater than *twelve* months. ASU *No. 2016-02* is effective for fiscal years and interim periods beginning after *December 15, 2018.* Early adoption of ASU *No. 2016-02* is permitted. Entities were required to apply the amendments at the beginning of the earliest period presented using a modified retrospective approach. This guidance is applicable to the Company's fiscal year beginning *April 1, 2019.* In *July 2018,* the FASB issued ASU *2018-10* "*Codification Improvements to Topic 842, Leases*" ("ASU *No. 2018-02"*). ASU *No. 2018-02* affects narrow aspects of the guidance issued in the amendments in ASU *No. 2016-02* including those regarding residual value guarantees, rate implicit in the lease, lessee reassessment of lease classification, lessor reassessment of lease term and purchase option, variable lease payments that depend on an index or a rate, investment tax credits, lease term and purchase option, transition guidance for amounts previously recognized in business combinations, certain transition adjustments, transition guidance for leases previously classified as capital leases under Topic *840,* transition guidance for modifications to leases previously classified as direct financing or sales-type leases under Topic *840,* transition guidance for sale and leaseback transactions, impairment of net investment in the lease, unguaranteed residual asset, effect of initial direct costs on rate implicit in the lease, and failed sale and leaseback transactions. In *July 2018,* the FASB issued ASU *No. 2018-11,* "*Leases (Topic 842): Targeted Improvements*," which provides entities with an additional (and optional) transition method to adopt the new leases standard. Under this method, an entity initially applies the new leases standard at the adoption

date and recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. Consequently, the prior comparative period's financials will remain the same as those previously presented. Entities that elect this optional transition method must provide the disclosures that were previously required. The Company expects it will elect this optional transition method. The Company has selected resources to track and record leases and is starting the assessment and valuation process by evaluating the population of leases under the revised definition of what qualifies as a leased asset, and expects to have the assessment completed by *March 2019.* The Company is the lessee under various agreements for facilities and equipment that are currently accounted for as operating and capital leases. The Company expects this guidance will have a material impact on its consolidated balance sheets due to the recognition of lease rights and obligations as assets and liabilities, respectively. The Company does *not* expect this guidance to have a material effect on its consolidated results of operations and cash flows.

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3. INVENTORIES

Inventories are stated at the lower of cost or net realizable value. Cost is determined by the *first*-in, *first*-out method. Inventories consist of the following:

	December 31, 2018	March 31, 2018
	(in thousands)	
Raw materials	$*460*	$*410*
Work in process	*4,649*	*2,602*
Finished goods	*4,828*	*5,878*
Supplies	*175*	*144*
Inventories, net	$*10,112*	$*9,034*

The Company recognizes abnormal production costs, including fixed cost variances from normal production capacity, as an expense in the period incurred. Abnormal costs related to spirulina production of *$0* and *$250,000* were charged to cost of sales for the *three* and *nine* months ended *December 31, 2018,* respectively. There were *no* abnormal production costs for the *three* and *nine* months ended *December 31, 2017.* Non-inventoriable fixed costs related to production of *$35,000* (astaxanthin) and *$176,000* (*$35,000* astaxanthin and *$141,000* spirulina) were charged to cost of sales for the *three* and *nine* months ended *December 31, 2018,* respectively. Non-inventoriable fixed costs related to spirulina production of *$4,000* and *$88,000* were charged to cost of sales for the *three* and *nine* months ended *December 31, 2017,* respectively.

4. EQUIPMENT AND LEASEHOLD IMPROVEMENTS

Equipment and leasehold improvements consist of the following:

	December 31, 2018	March 31, 2018
	(in thousands)	
Equipment	$*18,312*	$*17,935*

Leasehold improvements	*14,288*	*14,248*
Furniture and fixtures	*348*	*348*
	32,948	*32,531*
Less accumulated depreciation and amortization	(*18,767*)	(*17,346*)
Construction-in-progress	*1,002*	*549*
Equipment and leasehold improvements, net	$*15,183*	$*15,734*

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying value of such assets *may not* be recoverable. Recoverability of these assets is measured by a comparison of the carrying amount to forecasted undiscounted future cash flows expected to be generated by the asset. If the carrying amount exceeds its estimated future cash flows, then an impairment charge is recognized to the extent that the carrying amount exceeds the asset's fair value. Management has determined *no* asset impairment existed as of *December 31, 2018* and *March 31, 2018,* respectively.

5. SHORT TERM CONTRACT OBLIGATION

On *November 30, 2018* the Company completed the purchase of a *six* acre production and research facility from Cellana LLC ("Cellana") under a purchase agreement that was signed *August 31, 2018.* In accordance with the terms of the *third* amendment to the asset purchase agreement, the Company acquired the asset for *$495,000* with a cash down payment of *$100,000* leaving a short-term obligation of *$395,000* on the asset purchase.

The short -term obligation is comprised of *two* separate loans in the principal amount of *$180,000* and *$215,000.* The *first* loan of *$180,000* bears an interest rate of *6.25%* and is payable in *four* monthly installments which includes principal and interest. The loan commenced on *December 1, 2018* and matures on *March 31, 2019.* The principal amount outstanding at *December 31, 2018* was *$137,000.*

The *second* loan in the amount of *$215,000* is a non-interest bearing loan that is payable in *twelve* monthly installments comprised of *two* monthly payments of *$10,000* and *ten* monthly payments of *$19,543.* The loan commenced on *December 1, 2018* and matures on *October 15, 2019.* This contract contains a hold back of *$38,000* pending resolution of certain closing items by the seller. The principal amount outstanding at *December 31, 2018* was *$195,000.*

6. LINE OF CREDIT

On *August 30, 2016,* the Revolving Credit Agreement (the "Credit Agreement"), which the Company and First Foundation Bank ("the Bank") entered into on *June 3, 2016,* became effective after the Company and the Bank received the necessary approvals from the State of Hawaii to secure the lien on the Company's leasehold property in Kona, Hawaii. The Credit Agreement allows the Company to borrow up to *$2,000,000* on a revolving basis. Borrowings

under the Credit Agreement bear interest at the Wall Street Journal prime rate (*5.50%* at *December 31, 2018*) plus *2%,* floating. The Credit Agreement includes various covenants as defined in the Credit Agreement. The Credit Agreement also contains standard acceleration provisions in the event of a default by the Company. As of *December 31, 2018,* the Company had borrowed *$1,750,000* and had *$250,000* available on the line. The line of credit is subject to annual renewal and was renewed on *August 30, 2018* and will be subject to renewal upon expiration on *August 30, 2019.* Pursuant to the *August 30, 2018* renewal, the current ratio covenant was changed from *2.10:1* to *1.50:1* and is applicable to both the Line of Credit and Long-Term Debt with the Bank.

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The Credit Agreement grants the Bank the following security interests in the Company’s property: (a) a lien on the Company’s leasehold interest in its Kona facility; (b) an assignment of the Company’s interest in leases and rents on its Kona facility; and (c) a security interest in all fixtures, furnishings and equipment related to or used by the Company at the Kona facility. Each security interest is further subject to the terms of the Credit Agreement.

7. ACCRUED EXPENSES

Accrued expenses consist of the following:

	December 31, 2018	March 31, 2018
	(in thousands)	
Wages, commissions, bonus and profit sharing	$799	$ 707
Other accrued expenses	274	185
Total accrued expenses	$1,073	$ 892

8. LONG-TERM DEBT

Long-term debt consists of the following:

	December 31, 2018	March 31, 2018
	(in thousands)	
Long-term debt	$*6,101*	$*6,530*
Capital lease obligations	*98*	*148*
Less current maturities	*(663*)	*(655*)
Long-term debt, excluding current maturities	*5,536*	*6,023*
Less unamortized debt issuance costs	*(208*)	*(233*)
Total long-term debt, net of current maturities and unamortized debt issuance costs	$*5,328*	$*5,790*

Term Loans

On *August 14, 2012,* the Company entered into a loan agreement (the *"August 2012* Loan Agreement") that provides a term loan in an aggregate principal amount of *$5,500,000* which is secured by substantially all the Company's assets, including a mortgage on the Company's interest in its lease at the National Energy Laboratory of Hawaii Authority. The *August 2012* Loan Agreement is partially guaranteed under the provisions of the U.S. Department of Agriculture ("USDA") Rural Development Guarantee program.

In accordance with terms of the *August 2012* Loan Agreement, monthly payments of principal and interest are required until the loan's maturity on *August 14, 2032.* Interest on the loan accrues on the outstanding principal balance at an annual variable rate equal to the published Wall Street Journal prime rate (*5.50%* at *December 31, 2018*) plus *1.0%* and is adjustable on the *first* day of each calendar quarter and fixed for that quarter. At *no* time shall the annual interest rate be less than *5.50%.* The balance under the *August 2012* Loan Agreement was *$4,492,000* and *$4,648,000* at *December 31, 2018* and *March 31, 2018,* respectively.

The Loan includes a *one*-time origination and guaranty fees totaling *$214,500* and an annual renewal fee payable in the amount of *0.25%* of the USDA guaranteed portion of the outstanding principal balance as of *December 31* of each year, beginning *December 31, 2012.* The USDA has guaranteed *80%* of all amounts owing under the *August 2012* Loan Agreement. The Company is subject to financial covenants and customary affirmative and negative covenants.

On *July 30, 2015,* the Company entered into a loan agreement (the *"2015* Loan Agreement") that provides a term loan in an aggregate principal amount of *$2,500,000* and is secured by all the Company's assets. The *2015* Loan Agreement is partially guaranteed under the provisions of the USDA Rural Development Guarantee program.

In accordance with terms in the *2015* Loan Agreement, payment of principal and interest are required until its maturity on *September 1, 2022.* Interest on the loan accrues on the outstanding principal balance at an annual variable rate equal to the published Wall Street Journal prime rate (*5.50%* at *December 31, 2018*) plus *2.0%* and is adjustable on the *first* day of each calendar quarter and fixed for that quarter.

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The *2015* Loan includes a *one*-time origination and guaranty fee totaling *$113,900* and an annual renewal fee payable in the amount of *0.50%* of the USDA guaranteed portion of the outstanding principal balance as of *December 31* of each year, beginning *December 31, 2015.* The USDA has guaranteed *80%* of all amounts owing under the *2015* Loan. The Company is subject to financial covenants and customary affirmative and negative covenants.

At *no* time shall the annual interest rate be less than *6.00%.* The *2015* Loan Agreement has a prepayment penalty of *5%* for any prepayment made prior to the *first* anniversary of the date of the loan and each year thereafter the penalty is reduced by *1%* each year until the *fifth* anniversary of such date when there will *no* longer be a prepayment penalty. The balance under the *2015* Loan Agreement was *$1,475,000* and *$1,726,000* at *December 31, 2018* and *March 31, 2018,* respectively.

On *October 6, 2017,* the Company entered into an Equipment Finance Agreement (the "Equipment Agreement"), which provides up to *$175,000* of financing for equipment. The interest rate on this loan is *4.75%.* In accordance with terms in the Equipment Agreement, payment of principle and interest are required until its maturity on *October 31, 2022.* The balance under this loan was *$134,000* and *$156,000* at *December 31, 2018* and *March 31, 2018,* respectively.

Capital Leases

The Company has *three* capital leases providing for *$278,000* in equipment, secured by the equipment financed. The capital leases mature at various dates between *May 2019* and *March 2021* and are payable in *60* equal monthly payments, except for *one* which is payable in *36* equal monthly payments. The interest rates under these capital leases range from *4.18%* to *12.90%.* The aggregate balances under these leases were *$98,000* and *$148,000* at *December 31, 2018* and *March 31, 2018,* respectively.

9. CONTINGENCIES

From time to time, the Company *may* be involved in litigation and investigations relating to claims and matters arising out of its operations in the normal course of business. The Company believes that it currently is *not* a party to any legal proceedings or claims which, individually or in aggregate, would have a material effect on its consolidated financial position, results of operations or cash flows.

***10.* SHARE-BASED COMPENSATION**

The Company has share-based compensation plans, which are more fully described in Note *9,* Share-Based Compensation, to the Consolidated Financial Statements included in the Company's annual report on Form *10*-K as filed with the SEC on *June 15, 2018.*

As of *December 31, 2018,* the Company had *two* equity-based compensation plans: the *2016* Equity Incentive Plan (the *"2016* Plan") and the *2014* Independent Director Stock Option and Restricted Stock Grant Plan (the *"2014* Directors Plan"). The Company has also issued stock options, which remain outstanding as of *December 31, 2018,* under *two* equity-based compensation plans which have expired according to their terms: the *2005* Stock Option Plan (the *"2005* Plan") and the *2004* Independent Director Stock Option and Stock Grant Plan (the *"2004* Directors Plan"). These plans allowed the Company to award stock options and shares of restricted common stock to eligible employees, certain outside consultants and independent directors. *No* additional awards will be issued under the *2005* Plan or the *2004* Directors Plan.

The following table presents shares authorized, available for future grant and outstanding under each of the Company's plans:

	As of December 31, 2018		
	Authorized	**Available**	**Outstanding**
2016 Plan	*1,300,000*	*1,113,022*	*170,975*
2014 Directors Plan	*350,000*	*184,400*	*12,000*
2005 Plan	—	—	*434,400*
2004 Directors Plan	—	—	*12,000*
Total	*1,650,000*	*1,297,422*	*629,375*

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Stock Options

All stock option grants made under the equity-based compensation plans were issued at exercise prices *no* less than the Company's closing stock price on the date of grant, determined by the Board of Directors or the Compensation Committee of the Board of Directors in accordance with the provisions of the respective plans. The terms of each option grant include vesting, exercise, and other conditions set forth in a Stock Option Agreement evidencing each grant. *No* option can have a life in excess of *ten* (*10*) years. The Company records compensation expense for employee stock options based on the estimated fair value of the options on the date of grant using the Black-Scholes option-pricing model. The model requires various assumptions, including a risk-free interest rate, the expected term of the options, the expected stock price volatility over the expected term of the options, and the expected dividend yield. Compensation expense for employee stock options is recognized ratably over the vesting term. Compensation expense recognized for options issued under all Plans was *$18,000* and *$54,000* for the *three* and *nine* months ended *December 31, 2018,* respectively. Compensation expense recognized for options issued under all Plans was *$13,000* and *$47,000* for the *three* and *nine* months ended *December 31, 2017,* respectively. All stock-based compensation has been classified as general and administrative expense in the condensed consolidated statement of operations.

A summary of option activity under the Company's stock plans for the *nine* months ended *December 31, 2018* is presented below:

Option Activity	**Shares**	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Term (in years)**	**Aggregate Intrinsic Value**
Outstanding at March 31, 2018	*589,400*	$ *4.06*	*4.9*	$ *675,300*
Granted	—	$ —		
Exercised	*(6,000*)	$ *2.85*		
Forfeited	*(5,000*)	$ *5.75*		
Outstanding at December 31, 2018	*578,400*	$ *4.06*	*4.2*	$ *43,804*
Exercisable at December 31, 2018	*483,400*	$ *4.15*	*3.3*	$ *43,804*

The aggregate intrinsic value in the table above is before applicable income taxes and represents the excess amount over the exercise price optionees would have received if all options had been exercised on the last business day of the period indicated, based on the Company's closing stock price of *$3.02* for such day.

A summary of the Company's non-vested options for the *nine* months ended *December 31, 2018* is presented below:

Nonvested Options	Shares	Weighted Average Grant-Date Fair Value
Nonvested at March 31, 2018	*120,000*	$ *1.81*
Granted	—	—
Vested	*(25,000*)	*1.71*
Forfeited	—	—
Nonvested at December 31, 2018	*95,000*	$ *1.83*

As of *December 31, 2018,* total unrecognized stock-based compensation expense related to all unvested stock options was *$127,000,* which is expected to be expensed over a weighted average period of *1.6* years.

Subsequent to *December 31, 2018, 50,000* stock options were granted from the *2016* Plan at an exercise price of *$3.00* per share.

Restricted Stock

There were *no* grants of fully vested restricted stock issued to Non-Employee Directors for the *three* months ended *December 31, 2018* and *December 31, 2017.* Grants of fully vested restricted stock issued to Non-Employee Directors was *47,223* shares and *57,501* shares for the *nine* months ended *December 31, 2018* and *December 31, 2017,* respectively. Compensation expense recognized for fully vested restricted stock was *$0* and *$170,000* for the *three* and *nine* months ended *December 31, 2018,* respectively. Compensation expense recognized for fully vested restricted stock was *$0* and *$276,000* for the *three* and *nine* months ended *December 31, 2017,* respectively.

Restricted Stock Units ("RSUs")

RSUs are service-based awards granted to eligible employees under the *2016* Plan. Compensation expense recognized for RSUs issued under the *2016* Plan was *$20,000* and *$58,000* for the *three* and *nine* months ended *December 31, 2018,* respectively. Compensation expense recognized for RSUs issued under the *2016* Plan was *$15,000* and *$48,000* for the *three* and *nine* months ended *December 31, 2017,* respectively.

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On *July 13, 2018, 22,449* RSUs were awarded to employees of the Company. This award is valued at *$4.0252* per share, the closing market price of the Company's common stock on the grant date, and vests over a period of *two* years.

The following table summarizes information related to awarded RSUs:

Nonvested Restricted Stock Units	**Shares**	**Weighted Average Grant Price**
Nonvested restricted stock units at March 31, 2018	*39,675*	$ *3.89*
Granted	*23,923*	*4.10*
Vested	*(7,670*)	*3.92*
Forfeited	*(4,953*)	*4.08*
Nonvested restricted stock units at December 31, 2018	*50,975*	$ *3.97*

As of *December 31, 2018,* total unrecognized stock-based compensation expense related to unvested restricted stock units was *$140,000,* which is expected to be expensed over a weighted average period of *1.8* years.

11. INCOME TAXES

On *December 22, 2017* H.R. *1,* originally known as the Tax Cuts and Jobs Act, (the "Tax Act") was enacted. Among the significant changes to the U.S. Internal Revenue Code, the Tax Act lowers the U.S. federal corporate income tax rate ("Federal Tax Rate") from *34%* to *21%* effective *January 1, 2018.* The Company will compute its income tax expense for the *March 31, 2019* fiscal year using a Federal Tax Rate of *21%.* The *21%* Federal Tax Rate will apply to fiscal years ending *March 31, 2019* and each year thereafter. The Company completed the accounting for the income tax effects of the Tax Act as of *March 31, 2018* and determined that the amount identified as provisional in the quarter ended *December 31, 2017* was a materially correct amount. As a result, *no* measurement period adjustments have been recorded.

We utilize our estimated annual effective tax rate to determine our provision (benefit) for income taxes for interim periods. The income tax provision (benefit) is computed by multiplying the estimated annual effective tax rate by the year to date pre-tax book income (loss). We recorded an income tax expense of *$73,000* and (*$127,000*) for the *three* months ended *December 31, 2018* and *2017,* respectively. We recorded an income tax expense of *$33,000* and income tax benefit of (*$105,000*) for the *nine* months ended *December 31, 2018* and *2017,* respectively. Our effective tax rate was *20.2%* and (*1.6%*) for the *three* and *nine* months ended *December 31, 2018,* respectively, and (*13.0%*) and (*5.3%*) for the *three* and *nine* months ended *December 31, 2017,* respectively. The effective tax rate for the *three* and *nine*

months ended *December 31, 2018* differs from the statutory rate of *21%* as a result of state taxes (net of federal benefit) and the net change in valuation allowance against the net deferred tax asset the Company believes is *not* more likely than *not* to be realized.

The Company is subject to taxation in the United States and *six* state jurisdictions. The preparation of tax returns requires management to interpret the applicable tax laws and regulations in effect in such jurisdictions, which could affect the amount of tax paid by the Company. Management, in consultation with its tax advisors, files its tax returns based on interpretations that are believed to be reasonable under the circumstances. The income tax returns, however, are subject to routine reviews by the various taxing authorities. As part of these reviews, a taxing authority *may* disagree with respect to the tax positions taken by management ("uncertain tax positions") and therefore *may* require the Company to pay additional taxes. Management evaluates the requirement for additional tax accruals, including interest and penalties, which the Company could incur as a result of the ultimate resolution of its uncertain tax positions. Management reviews and updates the accrual for uncertain tax positions as more definitive information becomes available from taxing authorities, completion of tax audits, expiration of statute of limitations, or upon occurrence of other events.

As of *December 31, 2018,* there was *no* liability for income tax associated with unrecognized tax benefits. The Company recognizes accrued interest related to unrecognized tax benefits as well as any related penalties in interest income or expense in its consolidated condensed statements of operations, which is consistent with the recognition of these items in prior reporting periods.

With few exceptions, the Company is *no* longer subject to U.S. federal, state, local, and non-U.S. income tax examination by tax authorities for tax years before *2013.*

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12. EARNINGS (LOSS) PER SHARE

Basic earnings (loss) per share is computed on the basis of the weighted average number of common shares outstanding. Diluted earnings per share is computed on the basis of the weighted average number of common shares outstanding plus the potentially dilutive effect of outstanding stock options using the "treasury stock" method.

Reconciliations between the numerator and the denominator of the basic and diluted earnings per share computations for the *three* months ended *December 31, 2018* and *2017* are as follows:

	Three Months Ended December 31, 2018		
	Net Loss (Numerator)	**Shares (Denominator)**	**Per Share Amount**
	(in thousands)		
Basic income per share	$*288*	*5,836*	$ *0.05*
Effect of dilutive securities — Common stock options	—	*26*	—
Diluted income per share	$*288*	*5,862*	$ *0.05*

	Three Months Ended December 31, 2017		
	Net Income (Numerator)	**Shares (Denominator)**	**Per Share Amount**
	(in thousands)		
Basic income per share	$*1,107*	*5,749*	$ *0.19*
Effect of dilutive securities — Common stock options	—	*82*	—
Diluted income per share	$*1,107*	*5,831*	$ *0.19*

Reconciliations between the numerator and the denominator of the basic and diluted (loss) earnings per share computations for the *nine* months ended *December 31, 2018* and *2017* are as follows:

Nine Months Ended December 31, 2018		
Net Loss (Numerator)	**Shares (Denominator)**	**Per Share Amount**

	(in thousands)		
Basic and diluted loss per share	$*(2,123*)	*5,809*	$ *(0.37*)

	Nine Months Ended December 31, 2017		
	Net Income (Numerator)	Shares (Denominator)	Per Share Amount
	(in thousands)		
Basic income per share	$*2,083*	*5,714*	$ *0.36*
Effect of dilutive securities—Common stock options	—	*60*	—
Diluted income per share	$*2,083*	*5,774*	$ *0.36*

Potentially dilutive securities include *75,000* outstanding options to purchase common stock for the *three* and *nine* months ended *December 31, 2018* and *20,991* restricted stock units for the *three* and *nine* months ended *December 31, 2018.* Diluted earnings per share does *not* include the impact of *75,000* options to purchase common stock for the *three* month period ended *December 31, 2018,* as the effect of their inclusion would be anti-dilutive. As a result of the net loss for the *nine* month period ended *December 31, 2018, no* potentially dilutive securities are included in the calculation of diluted loss per share because such effect would be anti-dilutive. Diluted earnings per share does *not* include the impact of *75,000* options to purchase common stock for the *three* and *nine* month period ended *December 31, 2017,* as the effect of their inclusion would be anti-dilutive. Restricted stock units become dilutive within the period granted and remain dilutive until the units vest and are issued as common stock.

13. RELATED PARTY TRANSACTIONS AND BALANCES

During the *nine* months ended *December 31, 2018,* the Company entered into a consulting agreement with an effective date of *May 5, 2018* with a vendor that employs *one* of our independent directors. The Company's independent director is *not* named in or involved in the performance of the consulting agreement. The contract amount of *$120,000* is reflected in general and administrative expense during the *nine* months ended *December 31, 2018* and *$120,000* in payments have been made against the contract during the *nine* months ended *December 31, 2018.*

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

Overview:

We are a world leader in the production of high value natural products derived from microalgae. Incorporated in 1983, we are guided by the principle of providing beneficial, quality microalgal products for health and human nutrition in a sustainable, reliable and environmentally sensitive operation. We are GMP (Good Manufacturing Practices) certified by the Natural Products Association™, reinforcing our commitment to quality in our products, quality in our relationships (with our customers, suppliers, employees and the communities we live in), and quality of the environment in which we work. Our products include:

Hawaiian *BioAstin*® natural astaxanthin - a powerful dietary antioxidant shown to support and maintain the body's natural inflammatory response, to enhance skin, and to support eye and joint health. It has expanding applications as a human nutraceutical and functional food ingredient; and

Hawaiian *Spirulina Pacifica*® - a nutrient-rich dietary supplement used for extra energy, a strengthened immune system, cardiovascular benefits and as a source of antioxidant carotenoids

Microalgae are a diverse group of microscopic plants that have a wide range of physiological and biochemical characteristics and contain, among other things, high levels of natural protein, amino acids, vitamins, pigments and enzymes. Microalgae have the following properties that make commercial production attractive: (1) microalgae grow much faster than land grown plants, often up to 100 times faster; (2) microalgae have uniform cell structures with no bark, stems, branches or leaves, permitting easier extraction of products and higher utilization of the microalgae cells; and (3) the cellular uniformity of microalgae makes it practical to control the growing environment in order to optimize a particular cell characteristic. Efficient and effective cultivation of microalgae requires consistent light, warm temperatures, low rainfall and proper chemical balance in a very nutrient-rich environment, free of environmental contaminants and unwanted organisms. This is a challenge that has motivated us to design, develop and implement proprietary production and harvesting technologies, systems and processes in order to commercially produce human nutritional products derived from microalgae.

Our production of these products at the 96-acre facility on the Kona Coast of the island of Hawaii provides several benefits. We selected the Keahole Point location in order to take advantage of relatively consistent warm temperatures, sunshine and low levels of rainfall needed for optimal cultivation of microalgae. This location also offers us access to cold deep ocean water, drawn from an offshore depth of 2,000 feet, which we use in our *Ocean-Chill Drying* system to eliminate the oxidative damage caused by standard drying techniques and as a source of trace nutrients for microalgal cultures. The area is also designated a Biosecure Zone, with tight control of organisms allowed into the area and free of genetically modified organisms (GMO's). We believe that our technology, systems,

processes and favorable growing location generally permit year-round harvest of our microalgal products in a cost-effective manner.

Results of Operations

The following tables present selected consolidated financial data for each of the periods indicated ($ in thousands):

	Three Months Ended December 31,		**Nine Months Ended December 31,**	
	2018	**2017**	**2018**	**2017**
Net sales	$10,044	$9,150	$24,143	$26,014
Net sales increase (decrease)	9.8 %		(7.2)%	
Gross profit	$4,116	$4,240	$8,237	$11,463
Gross profit as % of net sales	41.0 %	46.3 %	34.1 %	44.1 %
Operating expenses	$3,621	$3,130	$9,913	$9,114
Operating expenses as % of net sales	36.0 %	34.2 %	41.1 %	35.0 %
Operating income (loss)	$495	$1,110	$(1,676)	$2,349
Operating income (loss) as % of net sales	4.9 %	12.1 %	(6.9)%	9.0 %
Income tax expense (benefit)	$73	$(127)	$33	$(105)
Net income (loss)	$288	$1,107	$(2,123)	$2,083

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Comparison of the Three Months Ended December 31, 2018 and 2017

Net Sales *(in thousands)*

	Three Months Ended December 31, 2018	2017	$ Change	% Change
Packaged sales				
Astaxanthin	$6,012	$5,746	$266	4.6 %
Spirulina	3,212	2,268	944	41.6 %
Total Packaged sales	$9,224	$8,014	$1,210	15.0 %
Bulk sales				
Astaxanthin	$287	$317	$(30)	(9.5)%
Spirulina	533	819	(286)	(34.9)%
Total Bulk sales	$820	$1,136	$(316)	(27.8)%
Total sales				
Astaxanthin	$6,299	$6,063	$236	3.9 %
Spirulina	3,745	3,087	658	21.3 %
Total sales	$10,044	$9,150	$894	9.8 %

The net sales increase of 9.8% for the current quarter compared to the same period last year was driven by higher spirulina sales (up 21.3%) due to a 16% improvement in spirulina production over the same period in the prior year. This resulted in a 41.6% increase in packaged spirulina sales offset by a 34.9% decrease in bulk spirulina sales. The decrease in bulk spirulina sales is attributed to the lack of inventory available for bulk customers. One customer made up 84% of the $0.7 million increase in packaged spirulina sales, this occurred in October 2018 with orders placed to build customers inventory. International sales represented 9% of net sales for the current quarter compared to 24% for the same period last year. International sales were negatively impacted by the lack of spirulina inventory available for bulk customers.

Gross Profit Our gross profit margin for the current quarter decreased 5.3 percentage points compared to the same period last year, due to increased astaxanthin cost resulting from an 18% reduction in astaxanthin production as compared to the same three month period in the prior year.

Operating Expenses Operating expenses increased $0.5 million for the current quarter compared to the same period in last year. General and administrative expenses remained consistent with the same period of the prior year. Sales and marketing expenses increased $0.4 million due to a $0.5 million increase in advertising and promotion costs, offset by

a $0.1 million decrease in outside services expense. Research and development expenses increased $0.1 million due to a reallocation of personnel resulting from changes in responsibilities.

Income Taxes We recorded income tax expense of $0.1 million for the third quarter of this fiscal year with an effective tax rate of 20.2%, compared to an income tax benefit of $0.1 million for the same period last year with an effective rate of (13.0%). Income tax expense for the quarter included a discrete tax expense of approximately $15,000 as a result of greater state tax expense and greater AMT credit benefit than was originally estimated in our tax provision for our fiscal year ended March 30, 2018. This increased the effective tax rate for this quarter by 4.1%.We continue to carry a full valuation allowance on our net deferred tax assets.

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Comparison of the Nine Months Ended December 31, 2018 and 2017

Net Sales *(in thousands)*

	Nine Months Ended December 31,		$	%
	2018	2017	Change	Change
Packaged sales				
Astaxanthin	$15,388	$15,649	$(261)	(1.7)%
Spirulina	6,208	6,560	(352)	(5.4)%
Total Packaged sales	$21,596	$22,209	$(613)	(2.8)%
Bulk sales				
Astaxanthin	$884	$748	$136	18.2 %
Spirulina	1,663	3,057	(1,394)	(45.6)%
Total Bulk sales	$2,547	$3,805	$(1,258)	(33.1)%
Total sales				
Astaxanthin	$16,272	$16,397	$(125)	(0.8)%
Spirulina	7,871	9,617	(1,746)	(18.2)%
Total sales	$24,143	$26,014	$(1,871)	(7.2)%

The net sales decrease of 7.2% for the first nine months of fiscal 2019 compared to the same period last year was driven by an 18.2% decrease in sales of our spirulina due to lower supply that was the result of the complete re-inoculation that took place in the first quarter of this fiscal year. International sales represented 14% of net sales for the current quarter compared to 23% for the same period last year. International sales were negatively impacted by the lack of spirulina inventory available for bulk customers.

Gross Profit Our gross profit margin for the first nine months of fiscal 2019 decreased 10.0 percentage points compared to the same period last year due primarily to the spirulina re-inoculation and the resulting decrease in supply. The lower spirulina production levels in both Q4 of fiscal 2018 (-63% compared to Q4 of fiscal 2017) and in Q1 of the current fiscal year (-76% compared to Q1 of fiscal 2018) has had a negative impact on our year-to-date performance. In addition to decreased sales volume, the lower production levels resulted in a $1.4 million increase in cost of goods and reduced gross profit margin by 5.8 percentage points for the first nine months of the current fiscal year. The 15% reduction in astaxanthin production resulted in a $0.8 million reduction in gross profit, or 3.3 percentage points, as compared to the prior.

Operating Expenses Operating expenses increased $0.8 million for the first nine months of fiscal 2019 compared to the same period in last year. General and administrative expenses remained consistent with the same period of the prior year. Sales and marketing expenses increased $0.5 million due to a $0.9 million increase in advertising and promotion costs, offset by a $0.4 million decrease in outside services expense. Research and development expenses increased $0.2 million due to a reallocation of personnel resulting from changes in responsibilities.

Income Taxes We recorded income tax expense of $33,000 for the first nine months of this year with an effective tax rate of 1.6%, compared to an income tax benefit of $105,000 for the same period last year with an effective rate of (5.3%). Income tax expense for the first nine months of this year included a discrete tax expense of approximately $15,000 as a result of greater state tax expense and greater AMT credit benefit than was originally estimated in our tax provision for our fiscal year ended March 30, 2018. This reduced the effective tax rate for this period by 0.7%.We continue to carry a full valuation allowance on our net deferred tax assets.

Liquidity and Capital Resources

As of December 31, 2018, we had cash of $1.6 million and working capital of $6.2 million compared to $1.3 million and $7.9 million, respectively, at March 31, 2018. On August 30, 2016, the Credit Agreement, which we and First Foundation Bank (the Bank) entered into on June 3, 2016, became effective. The Credit Agreement allows us to borrow up to $2.0 million on a revolving basis. The line of credit was renewed on August 30, 2018 and will expire on August 30, 2019. At December 31, 2018, we had borrowed $1.75 million and had $0.25 million available on the line. Along with the renewal, the bank reduced the current ratio requirement on the credit line and all term loans to 1.50:1; the former requirement was 2.10:1.

As of December 31, 2018, we had $6.0 million of term loans payable to the Bank that require the payment of principal and interest monthly through August 2032. Pursuant to the term loans, we are subject to annual financial covenants, customary affirmative and negative covenants and certain subjective acceleration clauses. We were in compliance with these financial covenants at March 31, 2018.

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Funds generated by operating activities and available cash continue to be our most significant sources of liquidity for working capital requirements, debt service and funding of maintenance levels of capital expenditures. Based upon our fiscal year 2019 operating plan and related cash flow projections and our projected consolidated financial position as of March 31, 2019, cash flows expected to be generated by operating activities and available financing are expected to be sufficient to fund our operations for at least the next twelve months, and our current ratio is expected to be in compliance with the annual term loan covenant requirement as of March 31, 2019. However, no assurances can be provided that we will achieve our operating plan and cash flow objectives for the fiscal year ended March 31, 2019 or our projected consolidated financial position as of March 31, 2019. Such estimates are subject to change based on future results and such change could cause future results to vary significantly from expected results.

Cash Flows The following table summarizes our cash flows for the periods indicated ($ in thousands):

	Nine months ended December 31	
	2018	**2017**
Total cash provided by (used in):		
Operating activities	$(42)	$1,468
Investing activities	(475)	(732)
Financing activities	696	(380)
Increase in cash	$179	$356

Cash used in operating activities for the nine months ended December 31, 2018 was the result of a net loss, offset by non-cash charges of $1.8 million and a decrease in working capital of $0.3 million. The decrease in working capital was primarily the result of a $1.1 million increase in inventory, offset by a $0.5 million increase in accounts payable and a $0.8 million decrease in accounts receivable. The $1.1 million increase in inventory is comprised primarily of a $0.9 million increase in spirulina inventory and related nutrient supplies, and a $0.3 million increase in astaxanthin inventory.

Cash used in investing activities for the nine months ended December 31, 2018 includes costs for leasehold improvements and equipment acquisitions at our Kona facility, including the cash payment for the purchase of assets from Cellana LLC.

Cash provided by financing activities for the nine months ended December 31, 2018 consists of a $1.3 million increase in our line of credit offset by $0.06 principal payments made on the short-term contract obligation to acquire the Cellana assets and by the $0.5 million in principal payments on debt in the normal course of business. The line of credit advance was used to fund operations during the re-inoculation period and is expected to be repaid through cash

flow from operating activities in future quarters.

Sources and Uses of Capital

At December 31, 2018, our working capital was $6.2 million, a decrease of $1.7 million compared to March 31, 2018. The decrease is due primarily to an increase in short term debt and accounts payable.

Our results of operations and financial condition can be affected by numerous factors, many of which are beyond our control and could cause future results of operations to fluctuate materially as it has in the past. Future operating results may fluctuate as a result of changes in sales volumes to our largest customers, weather patterns, increased competition, increased materials, nutrient and energy costs, government regulations and other factors beyond our control.

A significant portion of our expense levels are relatively fixed, so the timing of increases in expenses is based in large part on forecasts of future sales. If net sales are below expectations in any given period, the adverse impact on results of operations may be magnified by our inability to adjust spending quickly enough to compensate for the sales shortfall. We may also choose to reduce prices or increase spending in response to market conditions, which may have a material adverse effect on financial condition and results of operations.

Based upon our current operating plan, analysis of our consolidated financial position and projected future results of operations, we believe that our operating cash flows, cash balances and working capital will be sufficient to finance current operating requirements, debt service requirements, and routine planned capital expenditures, for the next twelve (12) months.

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Outlook

This outlook section contains a number of forward-looking statements, all of which are based on current expectations. Actual results may differ materially.

Our strategic direction has been to position the Company as a world leader in the production and marketing of high-value natural products from microalgae. We are vertically aligned, producing raw materials in the form of microalgae processed at our 96-acre facility in Hawaii, and integrating those raw materials into finished products. In fiscal 2019, our primary focus is on building our consumer brands, increasing our astaxanthin production volume and improving the consistency of our production for both astaxanthin and spirulina. We will continue to put emphasis on our Nutrex Hawaii consumer products to introduce them to a broader consumer market, and leverage our experience and reputation for quality, building nutritional brands which promote health and well-being. The foundation of our nutritional products is naturally cultivated Hawaiian Spirulina Pacifica® in powder and tablet form; and BioAstin® Hawaiian Astaxanthin® antioxidant in extract and softgel form. Information about our Company and our products can be viewed at www.cyanotech.com and www.nutrex-hawaii.com. Consumer products can also be purchased online at www.nutrex-hawaii.com.

We are focused on sustainability of production levels in order to promote growth in our astaxanthin and spirulina product lines. We will continue to improve and expand these lines to meet the demand of consumers. Our recent re-inoculation of our spirulina ponds was a necessary step toward sustaining long-term production levels. We will continue to promote the nutritional superiority of Hawaiian grown microalgae to maintain and expand market share. Significant sales variability between periods and even across several periods can be expected based on historical results.

Gross profit margin percentages going forward will be impacted by production volumes and continued pressure on input costs and greater competition in the market place. This could cause margins to decline in future periods. We will continue to focus on higher margin consumer products that promote health and well-being. We are dedicated to continuous improvements in process and production methods to stabilize and increase production levels for the future.

Producing the highest quality microalgae is a complex biological process which requires balancing numerous factors including microalgal strain variation, temperature, acidity, nutrient and other environmental considerations, some of which are not within our control. An imbalance or unexpected event can occur resulting in production levels below normal capacity. The allocation of fixed production overheads (such as depreciation, rent and general insurance) to inventories is determined based on normal production capacity. When our production volumes are below normal capacity limits, certain fixed production overhead costs cannot be inventoried and are recorded immediately in cost of sales. In addition, when production costs exceed historical averages, we evaluate whether such costs are one-time-period charges or an ongoing component of inventory cost.

To manage our cash resources effectively, we will continue to balance production in light of sales demand, minimizing the cost associated with build-ups in inventory when appropriate. We could experience unplanned cash outflows and may need to utilize other cash resources to meet working capital needs. A prolonged downturn in sales could impair our ability to generate sufficient cash for operations and minimize our ability to attract additional capital investment which could become necessary in order to expand facilities, enter into new markets or maintain optimal production levels.

Our future results of operations and the other forward-looking statements contained in this Outlook, in particular the statements regarding revenues, gross margin and capital spending, involve a number of risks and uncertainties. In addition to the factors discussed above, any of the following could cause actual results to differ materially: business conditions and growth in the natural products industry and in the general economy; changes in customer order patterns; changes in demand for natural products in general; changes in weather conditions; changes in health and growing conditions of our astaxanthin and spirulina products; competitive factors, such as increased production capacity from competing spirulina and astaxanthin producers and the resulting impact, if any, on world market prices for these products; government actions and increased regulations both domestic and foreign; shortage of manufacturing capacity; and other factors beyond our control. Risk factors are discussed in detail in Part II, Item 1A of this quarterly report and in Part I, Item 1A of our Form 10-K report for the year ended March 31, 2018.

We believe that our technology, systems, processes and favorable growing location generally permit year-round harvest of our microalgal products in a cost-effective manner. However, previously experienced imbalances in the highly complex biological production systems, together with volatile energy costs and rapidly changing world markets, suggest a need for continuing caution with respect to variables beyond our reasonable control. Therefore, we cannot, and do not attempt to, provide any definitive assurance with regard to our technology, systems, processes, location, or cost-effectiveness.

Off-Balance Sheet Arrangements

As of December 31, 2018, we had no off-balance sheet arrangements or obligations.

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Impact of Inflation

Inflationary factors such as increases in the costs of materials and labor directly affect the Company's operations. Most of the Company's leases provide for cost-of-living adjustments and require it to pay for insurance and maintenance expenses, all of which are subject to inflation. Additionally, the Company’s future lease cost for new facilities may include potentially escalating costs of real estate and construction. There is no assurance that the Company will be able to pass on increased costs to its customers.

Depreciation expense is based on the historical cost to the Company of its fixed assets, and is therefore potentially less than it would be if it were based on current replacement cost. While property and equipment acquired in prior years will ultimately have to be replaced at higher prices, it is expected that replacement will be a gradual process over many years.

Critical Accounting Policies and Estimates

Our critical accounting policies and estimates are disclosed in the “Management’s Discussion and Analysis of Financial Condition and Results of Operations” section of our Annual Report on Form 10-K for the year ended March 31, 2018 filed with the SEC on June 15, 2018. In the nine months ended December 31, 2018, there were changes to the application of critical accounting policies previously disclosed in our most recent Annual Report on Form 10-K related to the adoption of ASU 2014-09 on April 1, 2018, as described below.

Revenue Recognition

The Company records revenue based on the five-step model which includes: (1) identifying the contract with the customer; (2) identifying the performance obligations in the contract; (3) determining the transaction price; (4) allocating the transaction price to the performance obligations; and (5) recognizing revenue when the performance obligations are satisfied. Substantially all of the Company’s revenue is generated by fulfilling orders for the purchase of our micro algal nutritional supplements to retailers, wholesalers, or direct to consumers via online channels, with each order considered to be a distinct performance obligation. These orders may be formal purchase orders, verbal phone orders, e-mail orders or orders received online. Shipping and handling activities for which the Company is responsible under the terms and conditions of the order are not accounted for as performance obligations but as fulfillment costs. These activities are required to fulfill the Company’s promise to transfer the goods and are expensed when revenue is recognized. The impact of this policy election is insignificant as it aligns with our current practice.

Revenue is measured as the net amount of consideration expected to be received in exchange for fulfilling a performance obligation. The Company has elected to exclude sales, use and similar taxes from the measurement of the transaction price. The impact of this policy election is insignificant, as it aligns with our current practice. The amount of consideration expected to be received and revenue recognized includes estimates of variable consideration, which includes costs for trade promotion programs, coupons, returns and early payment discounts. Such estimates are calculated using historical averages adjusted for any expected changes due to current business conditions and experience. The Company reviews and updates these estimates at the end of each reporting period and the impact of any adjustments are recognized in the period the adjustments are identified. In assessing whether collection of consideration from a customer is probable, the Company considers the customer's ability and intent to pay that amount of consideration when it is due. Payment of invoices is due as specified in the underlying customer agreement, typically 30 days from the invoice date, which occurs on the date of transfer of control of the products to the customer.

Revenue is recognized at the point in time that the control of the ordered products is transferred to the customer. Generally, this occurs when the product is delivered, or in some cases, picked up from one of our distribution centers by the customer.

Item 3.   Quantitative and Qualitative Disclosures about Market Risk

There have been no material changes to our market risk during the nine months ended December 31, 2018. For additional information, refer to our Annual Report on Form 10-K for the year ended March 31, 2018.

Item 4.   Controls and Procedures

Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our chief executive officer (“CEO”) and chief financial officer (“CFO”), we have evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15(d)-15(e) of the Exchange Act as of the end of the period covered by this Report. Based on that evaluation, our CEO and CFO have concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in reports we file or submit under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms and (2) accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosures.

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Management's Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act). The Company's internal control over financial reporting is a process designed 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. Our management evaluated the effectiveness of our internal control over financial reporting as of December 31, 2018. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in "Internal Control - Integrated Framework" (2013 Framework). Based on that assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2018.

Changes to Internal Control Over Financial Reporting

On April 1, 2018, the Company adopted the new revenue recognition accounting standard, "Revenue from Contracts with Customers." As a result, we made additions and/or modifications to policies, procedures, and controls that have affected our internal control over financial reporting, including changes to accounting policies and procedures, operational processes and documentation practices.

There were no other changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the quarterly period ended December 31, 2018 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Limitations on the Effectiveness of Controls

Our management, including our CEO and CFO, do not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all errors and all fraud. A control system no matter how well designed and implemented, can provide only reasonable, not absolute, assurance that the control system's objectives 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 within a company are detected.

The inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistakes. Controls can also be circumvented by the individual acts of some persons, or by collusion of two or more people. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

This Form 10-Q should be read in conjunction with Item 9A “Controls and Procedures” of the Company’s Form 10-K for the fiscal year ended March 31, 2018, filed June 15, 2018.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time the Company may become party to lawsuits and claims that arise in the ordinary course of business relating to employment, intellectual property, and other matters. There were no significant legal matters outstanding at December 31, 2018.

Item 1A. Risk Factors

For a discussion of the risk factors relating to our business, please refer to Part I, Item 1A of our Form 10-K for the year ended March 31, 2018, which is incorporated by reference herein.

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

None.

Item 3. Defaults upon Senior Securities

None.

Item 5. Other Information

None.

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Item 6. Exhibits

a) The following exhibits are furnished with this report:

31.1	Certifications of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 signed as of February 13, 2019.
31.2	Certifications of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 signed as of February 13, 2019.
32	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 signed as of February 13, 2019.
99.1	Press Release dated February 13, 2019.
101	The following financial statements from Cyanotech Corporation's Quarterly Report on Form 10-Q for the quarter ended December 31, 2018, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) Notes to Condensed Consolidated Financial Statements.

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SIGNATURES

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

CYANOTECH CORPORATION
(Registrant)

February 13, 2019 (Date)	By: /s/ Mawae R. Morton Mawae R. Morton *Chief Executive Officer; Director*
February 13, 2019 (Date)	By: /s/ Brian B. Orlopp Brian B. Orlopp *Vice President — Finance & Administration and CFO* *(Principal Financial and Accounting Officer)*

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EXHIBIT INDEX

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