CytoDyn Inc.
Form 10-Q
January 13, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended November 30, 2016

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES ACT OF 1933
For the transition period from __________ to __________

Commission File Number: 000-49908

CYTODYN INC.

(Exact name of registrant as specified in its charter)

Delaware	**75-3056237**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer or Identification No.)**
1111 Main Street, Suite 660 Vancouver, Washington	**98660**
(Address of principal executive offices)	**(Zip Code)**

(Registrant s telephone number, including area code) (360) 980-8524

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

Large Accelerated Filer	Accelerated Filer
Non-accelerated Filer	Smaller Reporting Company

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

On December 31, 2016 there were 142,221,981 shares outstanding of the registrant s $0.001 par value common stock.

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PART I

Item 1. Financial Statements.

CytoDyn Inc.

Consolidated Balance Sheets

	November 30, 2016 (unaudited)	May 31, 2016
Assets		
Current assets:		
Cash	$ 8,811,237	$ 9,641,776
Prepaid expenses	338,912	141,714
Prepaid service fees	4,413,312	1,710,852
Total current assets	13,563,461	11,494,342
Furniture and equipment, net	17,892	24,550
Intangibles, net	2,092,239	2,267,239
Total assets	$ 15,673,592	$ 13,786,131
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 5,902,621	$ 2,467,973
Accrued liabilities and salaries	58,125	242,708
Accrued license fee	380,500	870,000
Total current liabilities	6,341,246	3,580,681
Long-term liabilities:		
Derivative liability	3,955,734	
Total long-term liabilities	3,955,734	
Total liabilities	10,296,980	3,580,681
Commitments and Contingencies		
Stockholders equity		
Series B convertible preferred stock, $0.001 par value; 400,000 shares authorized, 95,100 shares issued and outstanding at November 30, 2016 and May 31, 2016, respectively	95	95
Common stock, $0.001 par value; 350,000,000 and 250,000,000 shares authorized, 138,221,982 and 123,335,634 issued and outstanding at	138,222	123,336

November 30, 2016 and May 31, 2016, respectively				
Additional paid-in capital		113,285,930		107,307,933
Accumulated (deficit)		(108,047,635)		(97,225,914)
Total stockholders equity		5,376,612		10,205,450
Total liabilities and stockholders equity	$	15,673,592	$	13,786,131

See accompanying notes to consolidated financial statements.

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CytoDyn Inc.

Consolidated Statements of Operations

(Unaudited)

	Three Months Ended November 30,		Six Months Ended November 30,	
	2016	2015	2016	2015
Operating expenses:				
General and administrative	$ 1,679,925	$ 1,142,519	$ 3,259,988	$ 2,400,568
Research and development	4,383,636	1,661,069	8,069,109	6,970,309
Amortization and depreciation	92,556	90,191	185,140	180,382
Total operating expenses	6,156,117	2,893,779	11,514,237	9,551,259
Operating loss	(6,156,117)	(2,893,779)	(11,514,237)	(9,551,259)
Interest income	5,648	211	9,383	569
Loss on extinguishment of convertible notes				(584,177)
Change in fair value of derivative liability	1,223,466		1,223,466	646,505
Interest expense:				
Amortization of discount on convertible notes		(1,114,901)		(2,121,491)
Amortization of debt issuance costs		(362,038)		(712,377)
Amortization of discount on related party convertible notes				(94,344)
Interest related to derivative liability	(540,333)		(540,333)	
Inducement interest		(866,713)		(1,624,324)
Interest on notes payable		(27,373)		(118,709)
Total interest expense	(540,333)	(2,371,025)	(540,333)	(4,671,245)
Loss before income taxes	(5,467,336)	(5,264,593)	(10,821,721)	(14,159,607)
Provision for taxes on income				
Net loss	$ (5,467,336)	$ (5,264,593)	$ (10,821,721)	$ (14,159,607)
Basic and diluted loss per share	$ (0.04)	$ (0.06)	$ (0.08)	$ (0.18)
Basic and diluted weighted average common shares outstanding	136,023,544	84,089,964	130,185,627	78,003,528

See accompanying notes to consolidated financial statements.

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CytoDyn Inc.

Consolidated Statements of Cash Flows

(Unaudited)

	Six Months Ended November 30, 2016	Six Months Ended November 30, 2015
Cash flows from operating activities:		
Net loss	$ (10,821,721)	$ (14,159,607)
Adjustments to reconcile net loss to net cash used by operating activities:		
Amortization and depreciation	185,140	180,382
Amortization of debt issuance costs		604,628
Amortization of discount on convertible notes		2,121,491
Amortization of discount on related party notes		94,344
Interest expense associated with derivative liability	540,333	
Change in fair value of derivative liability	(1,223,466)	(646,505)
Loss on extinguishment of convertible notes		584,177
Interest expense associated with conversion and exercise inducement		757,611
Interest expense associated with extension of warrant expiration		866,713
Stock-based compensation	687,634	590,661
Changes in current assets and liabilities:		
(Increase) decrease in prepaid expenses	(2,899,658)	139,857
(Decrease) increase in accounts payable and accrued expenses	2,760,563	350,119
Net cash used in operating activities	(10,771,175)	(8,516,129)
Cash flows from investing activities:		
Furniture and equipment purchases	(3,480)	
Net cash used in investing activities	(3,480)	
Cash flows from financing activities:		
Proceeds from sale of common stock and warrants	10,729,500	12,941,248
Proceeds from warrant exercises	397,880	
Payment of principal and interest on convertible notes payable		(789,140)
Payment of offering costs	(1,183,264)	(1,433,569)
Net cash provided by financing activities	9,944,116	10,718,539
Net change in cash	(830,539)	2,202,410
Cash, beginning of period	9,641,776	1,050,060
Cash, end of period	$ 8,811,237	$ 3,252,470

Supplemental disclosure of cash flow information:				
Cash paid during the period for:				
Interest	$		$	26,890
Non-cash investing and financing transactions:				
Common stock issued upon conversion of convertible debt	$		$	7,947,342
Common stock issued or to be issued for accrued interest payable	$		$	143,479
Derivative liability associated with warrants	$	5,179,200	$	

See accompanying notes to consolidated financial statements.

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CYTODYN INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

AS OF NOVEMBER 30, 2016

(UNAUDITED)

Note 1 Organization

CytoDyn Inc. (the Company) was originally incorporated under the laws of Colorado on May 2, 2002 under the name RexRay Corporation (its previous name) and, effective August 27, 2015, reincorporated under the laws of Delaware. We are a clinical-stage biotechnology company focused on the clinical development and potential commercialization of humanized monoclonal antibodies to treat Human Immunodeficiency Virus (HIV) infection. Our lead product candidate, PRO 140, belongs to a class of HIV therapies known as entry inhibitors. These therapies block HIV from entering into and infecting certain cells.

The Company is developing a class of therapeutic monoclonal antibodies to address unmet medical needs in the areas of HIV and graft versus host disease.

Note 2 Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) and reflect all adjustments, which consist solely of normal recurring adjustments, needed to fairly present the financial results for these periods. The consolidated financial statements and notes thereto are presented as prescribed by Form 10-Q. Accordingly, certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. The accompanying consolidated financial statements should be read in conjunction with the financial statements for the fiscal years ended May 31, 2016 and 2015 and notes thereto in the Company s Annual Report on Form 10-K for the fiscal year ended May 31, 2016, filed with the Securities and Exchange Commission on July 19, 2016. Operating results for the three and six-months ended November 30, 2016 are not necessarily indicative of the results that may be expected for the entire year. In the opinion of management, all adjustments have been made, which consist only of normal recurring adjustments necessary for a fair statement of (a) the results of operations for the three and six-month periods ended November 30, 2016 and November 30, 2015, (b) the financial position at November 30, 2016 and (c) cash flows for the six-month periods ended November 30, 2016 and November 30, 2015.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, AGTI and CVM, both of which are dormant entities. All intercompany transactions and balances are eliminated in consolidation.

Reclassifications

Certain prior year amounts shown in the accompanying consolidated financial statements have been reclassified to conform to the 2016 presentation. These reclassifications did not have any effect on total current assets, total assets, total current liabilities, total liabilities, total stockholders equity, net loss or loss per share.

Going Concern

The consolidated accompanying financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. As shown in the accompanying consolidated financial statements, the Company had losses for all periods presented. The Company incurred a net loss of $10,821,721 for the six-months ended November 30, 2016 and has an accumulated deficit of $108,047,635 as of November 30, 2016. These factors, among others, raise substantial doubt about the Company s ability to continue as a going concern.

The consolidated financial statements do not include any adjustments relating to the recoverability of assets and classification of liabilities that might be necessary should the Company be unable to continue as a going concern. The Company s continuation as a going concern is dependent upon its ability to obtain additional operating capital, complete development of its product candidates, obtain U.S. Food & Drug Administration (FDA) approval, outsource manufacturing of the product candidates, and ultimately achieve initial revenues and attain profitability. The Company is currently engaging in significant research and development activities related to these product candidates, and expects to incur significant research and development expenses in the future primarily related to its clinical trials. These research and development activities are subject to significant risks and uncertainties. The Company intends to finance its future development activities and its working capital needs largely from the sale of equity and debt securities, combined with additional funding from other traditional sources. There can be no assurance, however, that the Company will be successful in these endeavors.

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Use of Estimates

The preparation of the consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash

Cash is maintained at federally insured financial institutions and, at times, balances may exceed federally insured limits. The Company has never experienced any losses related to these balances. Balances in excess of federally insured limits at November 30, 2016 and May 31, 2016 approximated $8.7 million and $9.4 million, respectively.

Identified Intangible Assets

The Company follows the provisions of FASB ASC Topic 350 Intangibles-Goodwill and Other, which establishes accounting standards for the impairment of long-lived assets such as intangible assets subject to amortization. The Company reviews long-lived assets to be held and used for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. If the sum of the undiscounted expected future cash flows over the remaining useful life of a long-lived asset group is less than its carrying value, the asset is considered impaired. Impairment losses are measured as the amount by which the carrying amount of the asset group exceeds the fair value of the asset. There were no impairment charges for the three and six-months ended November 30, 2016 and 2015. The value of the Company s patents would be significantly impaired by any adverse developments as they relate to the clinical trials pursuant to the patents acquired as discussed in Notes 7 and 9.

Research and Development

Research and development costs are expensed as incurred. Clinical trial costs incurred through third parties are expensed as the contracted work is performed. Where contingent milestone payments are due to third parties under research and development collaboration arrangements or other contractual agreements, the milestone payment obligations are expensed when the milestone conditions are probable and the amount of payment is reasonably estimable.

Pre-launch Inventory

The Company may scale-up and make commercial quantities of its product candidate prior to the date it anticipates that such product will receive final FDA approval. The scale-up and commercial production of pre-launch inventories involves the risk that such products may not be approved for marketing by the FDA on a timely basis, or ever. This risk notwithstanding, the Company may scale-up and build pre-launch inventories of product that have not yet received final governmental approval when the Company believes that such action is appropriate in relation to the commercial value of the product launch opportunity. The determination to capitalize is made once the Company (or its third party development partners) has filed a Biologics License Application that has been acknowledged by the FDA as containing sufficient information to allow the FDA to conduct its review in an efficient and timely manner and management is reasonably certain that all regulatory and legal hurdles will be cleared. This determination is based on the particular facts and circumstances relating to the expected FDA approval of the drug product being considered. As of November 30, 2016 and May 31, 2016, the Company did not have pre-launch inventory that qualified for capitalization pursuant to U.S. GAAP ASC 330   Inventory.

Fair Value of Financial Instruments

At November 30, 2016 and May 31, 2016, the carrying value of the Company s cash, accounts payable and accrued liabilities approximate their fair value due to the short-term maturity of the instruments. The Company carries derivative financial instruments at fair value as required by U.S. GAAP.

Derivative financial instruments consist of financial instruments that contain a notional amount and one or more underlying variables (e.g., interest rate, security price, variable conversion rate or other variables), require no initial net investment and permit net settlement. Derivative financial instruments may be free-standing or embedded in other financial instruments. The Company follows the provisions of FASB ASC 815 Derivatives and Hedging (ASC 815), as their instruments are recorded as a derivative liability, at fair value, and FASB ASC 480 Distinguishing Liabilities from Equity (ASC 480), as it relates to warrant liability, with changes in fair value reflected in income.

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Fair Value Hierarchy

The three levels of inputs that may be used to measure fair value are as follows:

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

Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets with insufficient volume or infrequent transactions (less active markets), or model-derived valuations in which all significant inputs are observable or can be derived principally from or corroborated with observable market data for substantially the full term of the assets or liabilities. Level 2 inputs also include non-binding market consensus prices that can be corroborated with observable market data, as well as quoted prices that were adjusted for security-specific restrictions.

Level 3. Unobservable inputs to the valuation methodology are significant to the measurement of the fair value of assets or liabilities. These Level 3 inputs also include non-binding market consensus prices or non-binding broker quotes that the Company was unable to corroborate with observable market data.

Liability measured at fair value on a recurring basis by level within the fair value hierarchy as of November 30, 2016 and May 31, 2016 is as follows:

	Fair Value Measurement at November 30, 2016 (1)		Fair Value Measurement at May 31, 2016	
	Using Level 3	Total	Using Level 3	Total
Liability:				
Derivative liability	$ 3,955,734	$ 3,955,734	$	$
Total liability	$ 3,955,734	$ 3,955,734	$	$

(1) The Company did not have any assets or liabilities measured at fair value using Level 1 or 2 of the fair value hierarchy as of November 30, 2016 and May 31, 2016.

A financial instrument s level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurements. These instruments are not quoted on an active market, so the Company uses a Binomial Lattice Model to estimate the value of the derivative liability. A Binomial Lattice Model was used because management believes it reflects all the assumptions that market participants would likely consider in negotiating the transfer of the warrant. The Company s derivative liability is classified within Level 3 of the fair value hierarchy because certain unobservable inputs were used in the valuation model.

The following is a reconciliation of the beginning and ending balances for liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) during the six months ended November 30, 2016 and the year ended May 31, 2016:

Balance at May 31, 2015	$ 2,008,907
Note conversion June 24, 2015	(521,133)
Note conversion June 24, 2015	(841,269)
Fair value adjustments	(646,505)
Balance at May 31, 2016	$
Investor warrants issued with registered direct equity offering	4,360,000
Agent warrants issued with registered direct equity offering	819,200
Fair value adjustments	(1,223,466)
Balance at November 30, 2016	$ 3,955,734

Stock-Based Compensation

U.S. GAAP requires companies to measure the cost of employee services received in exchange for the award of equity instruments based on the fair value of the award at the date of grant. The expense is to be recognized over the period during which an employee is required to provide services in exchange for the award (requisite service period) or when designated milestones have been achieved.

The Company accounts for stock-based awards established by the fair market value of the instrument using the Black-Scholes option pricing model utilizing certain weighted average assumptions including stock price volatility, expected term and risk-free interest rates, as of the grant date. The risk-free interest rate assumption is based upon observed interest rates appropriate for the expected term of the stock-based award. The expected volatility is based on the historical volatility of the Company s common stock on monthly intervals. The computation of the expected option term is based on the simplified method, as the Company issuances are considered plain vanilla options. For stock-based awards with defined vesting, the Company recognizes compensation expense over the requisite service period or when designated milestones have been achieved. The Company estimates forfeitures at the time of grant and revised, if necessary, in subsequent periods, if actual forfeitures differ from those estimates. Based on limited historical experience of forfeitures, the Company estimated future unvested forfeitures at 0% for all periods presented.

Common Stock

On March 18, 2016, at a special meeting of stockholders, a proposal was approved to increase the total number of authorized shares of common stock of the Company from 200,000,000 to 250,000,000. Subsequently, on August 24, 2016, at the Annual Meeting of Stockholders, a proposal was approved to increase the total number of authorized shares of common stock from 250,000,000 to 350,000,000.

Preferred Stock

The Company s Board of Directors is authorized to issue up to 5,000,000 shares of preferred stock without stockholder approval. As of November 30, 2016, the Company has authorized the issuance of 400,000 shares of Series B convertible preferred stock, of which 95,100 shares are outstanding. The remaining preferred shares authorized have no specified rights.

Debt Issuance Costs

During the year ended May 31, 2015, the Company incurred direct costs associated with the issuance of short-term convertible notes, as described in Note 4, and recorded approximately $708,000 of debt issuance costs and approximately $350,000 and $708,000 of related amortization for the three and six months ended November 30, 2015. There were no debt issuance costs during 2016.

Offering Costs

During the six-months ended November 30, 2016 and the year ended May 31, 2016, the Company incurred approximately $1.2 and $3.9 million in direct incremental costs associated with the sale of the equity securities, as described in Note 10. The offering costs were recorded as a component of equity when the proceeds were received.

Stock for Services

The Company periodically issues warrants to consultants for various services. The Black-Scholes option pricing model, as described more fully above, is utilized to measure the fair value of the equity instruments on the date of issuance. The Company recognizes the compensation expense associated with the equity instruments over the requisite service or vesting period.

Loss per Common Share

Basic loss per share is computed by dividing the net loss by the weighted average number of shares of common stock outstanding during the period. Diluted loss per share would include the weighted average number of shares of common stock outstanding and potentially dilutive common stock equivalents. Because of the net losses for all periods presented, the basic and diluted weighted average shares outstanding are the same since including the additional shares would have an anti-dilutive effect on the loss per share. For this reason, common stock options and warrants to purchase 64,415,987 and 44,618,007 shares of common stock were not included in the computation of basic and diluted weighted average number of shares of common stock outstanding for the six-months ended November 30, 2016 and November 30, 2015, respectively. Additionally, as of November 30, 2016, shares of Series B convertible preferred stock in the aggregate of 95,100 shares can potentially convert into 951,000 shares of common stock.

Income Taxes

Deferred taxes are provided on the asset and liability method, whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carry forwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Future tax benefits for net operating loss carry forwards are recognized to the extent that realization of these benefits is considered more likely than not. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

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The Company follows the provisions of FASB ASC 740-10 Uncertainty in Income Taxes (ASC 740-10). A reconciliation of the beginning and ending amount of unrecognized tax benefits has not been provided since there are no unrecognized benefits for all periods presented. The Company has not recognized interest expense or penalties as a result of the implementation of ASC 740-10. If there were an unrecognized tax benefit, the Company would recognize interest accrued related to unrecognized tax benefit in interest expense and penalties in operating expenses and penalties in operating expenses.

Note 3 Recent Accounting Pronouncements

Recent accounting pronouncements, other than below, issued by the FASB (including its EITF), the AICPA and the SEC did not or are not believed by management to have a material effect on the Company s present or future financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 (ASU 2016-02), *Leases (Topic 842)* effective for annual periods beginning after December 15, 2018, and interim periods within those annual periods. The ASU is to be applied using a modified retrospective approach with optional practical expedients and other special transition provisions. Early adoption is permitted. The ASU supersedes FASB ASC 840, *Leases,* and adds FASB ASC 842. It also amends and supersedes a number of other paragraphs throughout the FASB ASC. Management is currently assessing the impact the adoption of ASU 2016-02 will have on the Company s Consolidated Financial Statements.

In March 2016, the FASB issued Accounting Standards Update No. 2016-09 (ASU 2016-09), *Compensation Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Early application is permitted for reporting periods where financial statements have not yet been made available for issuance. The ASU requires different transition methods and disclosures based on the type of amendment included in the ASU. Management is currently assessing the impact the adoption of ASU 2016-09 will have on the Company s Consolidated Financial Statements.

In August 2014, the FASB issued Accounting Standards Update No. 2014-15, Presentation of Financial Statements Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity s Ability to Continue as a Going Concern (ASU 2014-15). ASU 2014-15 is intended to define management s responsibility to evaluate whether there is substantial doubt about an organization s ability to continue as a going concern and to provide related footnote disclosures. The amendments in ASU 2014-15 are effective for reporting periods beginning after December 15, 2016, with early adoption permitted. Management is currently assessing the impact the adoption of ASU 2014-15 will have on our Consolidated Financial Statements.

Note 4 Convertible Instruments

Series B Convertible Preferred Stock

During fiscal 2010, the Company issued 400,000 shares of Series B, $0.001 par value Convertible Preferred Stock (Series B) at $5.00 per share for cash proceeds totaling $2,009,000, of which 95,100 shares remain outstanding at November 30, 2016. Each share of the Series B is convertible into ten shares of the Company s $0.001 par common stock including any accrued dividends, with an effective fixed conversion price of $.50 per share. The holders of the Series B can only convert their shares to common shares provided the Company has sufficient authorized common shares at the time of conversion. Accordingly, the conversion option was contingent upon the Company increasing its authorized common shares, which occurred in April 2010, when the Company s stockholders approved an increase in the authorized shares of common stock to 100,000,000. At the commitment date, which occurred upon such stockholder approval, the conversion option related to the Series B was beneficial. The intrinsic value of the conversion option at the commitment date resulted in a constructive dividend to the Series B holders of approximately $6,000,000. The constructive dividend increased and decreased additional paid-in capital by identical amounts. The Series B has liquidation preferences over the common shares at $5.00 per share plus any accrued dividends. Dividends are payable to the Series B holders when declared by the board of directors at the rate of $.25 per share per annum. Such dividends are cumulative and accrue whether or not declared and whether or not there are any profits, surplus or other funds or assets of the Company legally available and are payable only upon conversion of the Series B in cash or shares of common stock at the Company s option. The Series B holders have no voting rights.

2013 Convertible Notes

During the year ended May 31, 2013, the Company issued $6,588,250 in aggregate original principal amount of unsecured convertible notes (the 2013 Convertible Notes) to investors for cash. Each outstanding 2013 Convertible Note was convertible at the election of the holder at any time into common shares at a fixed conversion price. At issuance, total principal of $6,208,250 was convertible at $0.75 per share, and $380,000 was convertible at $0.65 per share. The 2013 Convertible Notes were payable in full between November 30, 2013 and March 6, 2016, and bore interest at rates ranging from 5% to 10% per year, payable in cash semi-annually in arrears beginning on April 1, 2013. At November 30, 2016 and May 31, 2016, there were no convertible notes outstanding.

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In connection with the initial sale of the 2013 Convertible Notes, detachable common stock warrants to purchase a total of 8,527,984 common shares with a two-year term at exercise prices ranging from $0.75 to $2.00 per share were issued to the investors. The Company determined the fair value of the warrants at issuance using the Black-Scholes option pricing model utilizing certain weighted average assumptions, such as expected stock price volatility, term of the warrants, risk-free interest rates and expected dividend yield at the grant date.

Additionally, at the commitment date, the Company determined that the conversion feature related to the 2013 Convertible Notes was beneficial to the investors. As a result, the Company determined the intrinsic value of the conversion feature utilizing the fair value of the underlying common stock at the commitment date and the effective conversion price after discounting the 2013 Convertible Notes for the fair value of the warrants. The fair value of the warrants and the intrinsic value of the beneficial conversion feature were recorded as a debt discount to the 2013 Convertible Notes, with a corresponding increase to additional paid-in capital. The debt discount was amortized over the life of the 2013 Convertible Notes. During the six-months ended November 30, 2016 and 2015, the Company recognized approximately $ -0- and $6,800, respectively, as interest expense related to amortization of the debt discount. The unamortized discount was fully amortized upon any conversion of the 2013 Convertible Notes before maturity. Activity related to the 2013 Convertible Notes for the six-months ended November 30, 2016 and fiscal year ended May 31, 2016 was as follows:

	November 30, 2016	May 31, 2016
Face amount of Notes	$	$ 50,000
Unamortized discount		
Conversions		(50,000)
Total carrying value of Notes	$	$

During the fiscal year ended May 31, 2016 the board approved a one-year extension of expiration dates on the aforementioned detachable common stock warrants with an original term of two years, covering approximately 6.3 million shares of common stock, with an exercise price of $1.00 per share. Current expiration dates ranging from October 2015 through January 2016 were extended to October 2016 through January 2017. The extensions were effective October 1, 2015 upon the receipt of certain executed documentation from the warrant holders. Pursuant to U.S. GAAP, the Company recognized non-cash interest expense of approximately $866,700 in connection with this extension, which represented the incremental increase in the fair value of the modified warrants.

The Company determined the fair value of the new warrants using the Black-Scholes option pricing model utilizing certain weighted-average assumptions, such as expected stock price volatility, term of the warrants, risk-free rate and expected dividend yield at the commitment date.

	2016	
Expected dividend yield	0%	
Stock price volatility	64.56%	69.30%
Expected term	1 year	
Risk-free interest rate	0.33%	
Grant-date fair value	$0.15	$0.18

AVCP Convertible Notes

During the year ended May 31, 2015, the Company issued a three-month unsecured convertible promissory note (the AVCP Bridge Note and together with the AVCP Two-Year Note, the AVCP Convertible Notes) in the aggregate principal amount of $1,500,000 to Alpha Venture Capital Partners, L.P. (AVCP), an affiliate of one of the Company s directors. As described in greater detail below, the AVCP Bridge Note, along with the AVCP Two-Year Note, were subsequently converted in a transaction occurring during the year ended May 31, 2016. The principal amount of the AVCP Bridge Note plus unpaid accrued interest was convertible at the election of the holder into shares of the Company s common stock at any time prior to maturity at an initial conversion price of $1.00 per share. The AVCP Bridge Note bore simple interest of 1.2% per month, payable at maturity on May 5, 2015, and monthly thereafter, upon the Company s election to exercise a one-time option to extend the maturity by an additional three months, which the Company exercised on April 1, 2015 (extending the maturity date to August 5, 2015). Prepayment was permitted without penalty subject to the Company s obligation to pay at least three months interest on the principal amount. The conversion price was subject to (i) adjustment for stock splits and similar corporate events and (ii) reduction to a price per share that is 10% below the lowest sale price that is below $.9444 per share, for shares of common stock sold or deemed sold in future securities offerings, including sales to AVCP and its designees subject to certain exempt transactions. Without AVCP s prior written consent, the Company was not permitted to incur additional indebtedness for borrowed money, other than up to an additional $6.0 million in convertible promissory notes that may be issued to AVCP or related parties, unless such indebtedness was subordinated in right of payment to the Company s obligations under the AVCP Bridge Note and any additional notes issued to AVCP or related parties.

During the year ended May 31, 2015, the Company issued an additional two-year term unsecured convertible promissory note (the AVCP Two-Year Note) in the aggregate principal amount of $2,000,000 to AVCP, an affiliate of one of the Company s directors, as described under Note 9 below. As described in greater detail below, along with the AVCP Bridge Note, the AVCP Two-Year Note was subsequently converted in a transaction occurring during the year ended May 31, 2016. The AVCP Two-Year Note bore simple interest at the annual rate of 5%, payable quarterly. The principal balance of the AVCP Two-Year Note was due and payable in full on September 26, 2016, subject to acceleration of payment in the event of default. Prepayment was permitted without penalty. The AVCP Two-Year Note included events of default for nonpayment of principal or interest when due or other breaches of the AVCP Two-Year Note, as well as for breach of any term of the AVCP Two-Year Note and related warrant agreement. The principal amount of the AVCP Two-Year Note plus unpaid accrued interest was convertible at the election of the holder into shares of the Company s common stock at any time prior to maturity at an initial conversion price of $1.00 per share. The conversion price was subject to adjustment on the same terms, and contained similar consent rights to the issuance of additional indebtedness, as the AVCP Bridge Note above.

As a result of the private placement of approximately $4 million in convertible notes during the fourth quarter of fiscal year ended May 31, 2015, as described below, the conversion price of the AVCP Convertible Notes was reduced to $0.675 per share of common stock, which was 90% of the weighted-average price of the deemed issued shares of $0.75 related to the approximately $4 million offering of 2015 Convertible Notes described below. The decrease in the conversion price caused the number of shares of common stock issuable upon conversion of the AVCP Convertible Notes to increase from 3,500,000 to 5,185,185 shares of common stock.

The Company accounted for the AVCP Convertible Notes and related warrants, fully described below, as a financing transaction, wherein proceeds were allocated to the financial instruments issued. Prior to making the accounting allocation, the AVCP Convertible Notes and warrants were evaluated for proper classification under FASB ASC 480 Distinguishing Liabilities from Equity and ASC 815. The debt discounts associated with the notes were amortized over the term of the notes and the Company recognized approximately $ -0- and $94,000 in non-cash amortization expense for the six-months ended November 30, 2016 and November 30, 2015, respectively.

In connection with the original issuance of the two AVCP Convertible Notes, the Company issued warrants to AVCP covering 250,000 and 75,000 shares of the Company s common stock exercisable at a price of $0.50 per share on September 26, 2014 and February 6, 2015, respectively. The warrants are currently exercisable in full, include a cashless exercise feature, and will expire on December 31, 2019 and February 29, 2020, respectively. The aforementioned warrants have a term of five years from inception and an exercise price of $0.50 per share and meet the conditions for equity classification per ASC 815. The fair value of the warrants was determined using a Black-Scholes option model using the following assumptions:

	Warrants issued on September 26, 2014	Warrants issued on February 6, 2015
Risk free interest rate	1.82%	1.48%
Expected life	5 years	5 years
Expected volatility	136%	119%
Dividend yield	0.00%	0.00%

Based on the previous conclusions, the Company allocated the cash proceeds first to the derivative liability at its fair value and then to the warrants at their relative fair value, with the residual allocated to the host AVCP Convertible Notes as presented below.

On June 23, 2015, the Company, Alpha Venture Capital Management, LLC and AVCP entered into a Debt Conversion and Termination Agreement pursuant to which (i) AVCP agreed to convert the $3,535,627 in aggregate indebtedness as of June 23, 2015 under the AVCP Convertible Notes in exchange for 5,237,966 shares of the Company s common stock; (ii) subject to the conversion of the two AVCP Convertible Notes, the Company agreed to issue AVCP an additional five-year warrant covering 1,000,000 shares of common stock at an exercise price of $0.675 per share and (iii) subject to the AVCP s receipt of the common shares and warrant, the parties agreed to (a) terminate the subscription agreements; and (b) release and discharge each other party from all claims and obligations arising under the two AVCP Convertible Notes and subscription agreements. As a result of the debt conversion, during the six-months ended November 30, 2015, the Company recognized a loss on extinguishment of the AVCP Convertible Notes of approximately $584,000, a non-cash gain on the change in the fair value of the derivative liability of approximately $647,000 and non-cash inducement interest expense of approximately $758,000 arising from the aforementioned warrant.

		Year Ended May 31, 2016			
	May 31, 2015	Debt Discount	Fair Value	Conversion	May 31, 2016
AVCP Convertible notes payable	$ 2,637,618	$ 94,344	$	$ (2,731,962)	$
Compound embedded derivative	2,008,907		(646,505)	(1,362,402)	
Warrants (equity allocation)	215,732				
Accrued interest on notes payable				(35,627)	
Fair Value of Common Stock Issued				4,714,168	
Loss on conversion				(584,177)	
	$ 4,862,257	$ 94,344	$ (646,505)	$	$

Short-Term Convertible Notes

During the year ended May 31, 2015, the Company issued approximately $4.0 million of six-month unsecured convertible promissory notes (the Short-Term Convertible Notes) and related warrants to investors for cash, of which approximately $1.3 million in aggregate original principal amount remained outstanding, following the consummation of the tender offer transaction on September 21, 2015, as described below. Each Short-Term Convertible Note was originally convertible, at the election of the holder, at any time into common shares at a $0.75 per share. The Short-Term Convertible Notes bore interest of 7% per annum, payable in cash upon maturity. In connection with the issuance of the Short-Term Convertible Notes, the Company also issued warrants with a five-year term to purchase a total of 1,061,586 shares of common stock at an exercise price of $0.75. The Company determined the fair value of the warrants using the Black-Scholes option pricing model utilizing certain weighted-average assumptions, such as expected stock price volatility, term of the warrants, risk-free interest rate and expected dividend yield at the commitment date.

The Company utilized the following weighted-average assumptions to value the above investor warrants:

	2015
Expected dividend yield	0%
Stock price volatility	88.79%
Expected term	5 years
Risk-free interest rate	1.46% 1.58%
Grant-date fair value	$0.52 $0.76

Additionally, at the commitment date, the Company determined that the conversion feature related to the Short-Term Convertible Notes was beneficial to the investors. As a result, the Company determined the intrinsic value of the beneficial conversion feature utilizing the fair value of the underlying common stock at the commitment date and the effective conversion price after discounting the Short-Term Convertible Notes for the fair value of the warrants. The fair value of the warrants and the intrinsic value of the conversion feature were recorded as a debt discounts to the

Short-Term Convertible Notes, and a corresponding increase to additional paid-in capital. The debt discounts were amortized over the life of the Short-Term Convertible Notes. The Company recognized approximately $ -0- and $1,784,000 as interest expense related to the amortization of the debt during the six-months ended November 30, 2016 and 2015, respectively. There were no Short-Term Convertible Notes outstanding at May 31, 2016. The unamortized discounts were fully amortized upon any conversion of the Short-Term Convertible Notes before maturity.

During the year ended May 31, 2016, the Company tendered an offer to settle the balances of the Short-Term Convertible Notes. The Company offered to exchange the Short-Term Convertible Notes for (i) the issuance of restricted shares of common stock, for the settlement of the balance of the Short-Term Convertible Notes, principal and accrued but unpaid interest as of September 21, 2015, which was the commitment date, at a conversion price of $0.675 per share, and (ii) the amendment of the related warrants to reduce the exercise price to $0.675 per share. The offer represented a 10.0% discount to $0.75, which was the conversion price of the Short-Term Convertible Notes and exercise price of the related warrants. On September 21, 2015, the offering period and withdrawal rights for the exchange offer expired, and the Company completed the exchange offer for approximately $2.7 million in aggregate original principal amount of Short-Term Convertible Notes.

Following the consummation of the exchange offer described above, an aggregate principal amount of $525,000 and accrued but unpaid interest of $17,830 converted into 723,773 shares of common stock. The principal and interest for Short-Term Convertible Notes that were not exchanged in the exchange offer, or that are not otherwise converted pursuant to their terms, became due and

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payable between October 30, 2015 and November 15, 2015, six months from their issuance. The Company repaid the remaining aggregate principal and interest on such Short-Term Convertible Notes of approximately $789,000 on their respective maturity dates. Related to the tender offer conversions, the Company recognized approximately $330,000 in non-cash interest expense and approximately $108,000 commission expense to assist the Company in conversion of the debt at the commitment date.

Activity related to the Short-Term Convertible Notes for the six-months ended November 30, 2016, and fiscal year ended May 31, 2016 was as follows:

	November 30, 2016	May 31, 2016
Face amount of Notes	$	$ 3,981,050
Unamortized discounts		
Tender offer conversions		(2,693,800)
Conversions		(525,000)
Payments upon maturity		(762,250)
Total carrying value of Notes	$	$

Note 5 Derivative Liability:

Investor warrants

The investor warrants issued with the September 2016 registered direct equity offering, and the placement agent warrants issued in conjunction with the offering, as fully described in Note 11, contain a provision for net cash settlement in the event that there is a fundamental transaction (contractually defined as a merger, sale of substantially all assets, tender offer or share exchange). If a fundamental transaction occurs in which the consideration issued consists principally of cash or stock in a non-public company, then the warrant holder has the option to receive cash, equal to the fair value of the remaining unexercised portion of the warrant. Due to this contingent cash settlement provision, the investor and placement agent warrants require liability classification as derivatives in accordance with ASC 480 and ASC 815 and are recorded at fair value.

The following tables summarize the fair value of the derivative liability and linked common shares as of May 30, 2016, the warrant derivative liability inception date (September 15, 2016) and November 30, 2016:

	May 30, 2016	September 15, 2016	November 30, 2016
Total warrant derivative liability	$	$ 5,179,200	$ 3,955,734
Shares indexed to derivative liability		7,733,334	7,733,334

Changes in the fair value of the derivative liability, carried at fair value, are reported as Change in fair value of derivative liability in the Consolidated Statements of Operations. During the six-months ended November 30, 2016, the Company recognized a non-cash gain of approximately $1,223,500, due to changes in the fair value of the liability associated with such classified warrants.

ASC 820 provides requirements for disclosure of liabilities that are measured at fair value on a recurring basis in periods subsequent to the initial recognition. Fair values for the warrants were determined using a Binomial Lattice (Lattice) valuation model.

The Company estimated the fair value of their warrant derivative liability as of inception and November 30, 2016, using the following assumptions:

	September 15, 2016	November 30, 2016
Fair value of underlying stock	$ 0.78	$ 0.67
Risk free rate	1.20%	1.81%
Expected term (in years)	5.00	4.79
Stock price volatility	106%	103%
Expected dividend yield		
Probability of Fundamental Transaction	50%	50%
Probability of holder requesting cash payment	50%	50%

Due to the fundamental transaction provision, which could provide for early redemption of the warrants, the model also considered subjective assumptions related to the fundamental transaction provision. The fair value of the warrants will be significantly influenced by the fair value of the Company s stock price, stock price volatility, changes in interest and management s assumptions related to the fundamental transaction provision.

AVCP Notes

The following tables summarize the fair value of the derivative liability and linked common shares of the AVCP Notes, as of the derivative liability inception dates (September 26, 2014 and February 6, 2015) and fiscal year end May 31, 2016:

	September 26, 2014	February 6, 2015	May 31, 2015	May 31, 2016
Total AVCP Notes derivative liability	$ 767,038	$ 403,266	$ 2,008,907	$
Shares indexed to derivative liability	2,000,000	1,500,000	5,185,185	

Changes in the fair value of the derivative liability, carried at fair value, are reported as Change in fair value of derivative liability in the Consolidated Statements of Operations. During the six-months ended November 30, 2016 and November 30, 2015 the Company recognized a non-cash gain of approximately $ -0- and $647,000 respectively, due to the change in derivative liability related to the embedded derivative in the AVCP Notes.

ASC 815 does not permit an issuer to account separately for individual derivative terms and features embedded in hybrid financial instruments that require bifurcation and liability classification as derivative financial instruments. Rather, such terms and features must be combined together and fair valued as a single, compound embedded derivative. The Company selected a Binomial Lattice Model to value the compound embedded derivative because it believes this technique is reflective of all significant assumptions that market participants would likely consider in negotiating the transfer of this convertible note. Such assumptions include, among other inputs, stock price volatility, risk-free rates, credit risk assumptions, early redemption and conversion assumptions, and the potential for future adjustment of the conversion price due to a future dilutive financing.

Significant inputs and assumptions used in the Binomial Lattice Model for the derivative liability were as follows:

	September 26, 2014	February 6, 2015	May 31, 2015		June 23, 2015
Quoted market price on valuation date	$ 0.79	$ 0.96	$0.99		$ 0.90
Contractual conversion rate	$ 1.00	$ 1.00	$1.00		$ 1.00
Adjusted conversion price (a)	$ 0.9759	$ 1.00	$0.675		$ 0.675
Contractual term to maturity (years)	2.00	0.49	0.18	1.33	0.12
Expected volatility	123%	124%	90%	114%	48%
Contractual interest rate	5%	2%	1.5%	5.0%	1.2%
Risk-free rate	0.59%	0.045%	0.041%	0.48%	0.001%
Risk adjusted rate	2.69%	2.78%	2.80%		2.80%
Probability of event of default	5.00%	5.00%	5.00%		5.00%

(a) The adjusted conversion price input used in the Binomial Lattice Model considers both (i) the reduction of the conversion price to $0.675 on April 30, 2015, as result of a private placement offering in which Common Stock was sold for a weighted average price of $0.75 and (ii) potential adjustment to the stated conversion price due to a future dilutive issuance. This input was calculated using a probability-weighted approach which considered the likelihood of various scenarios occurring including (i) potential success or failure of various phases for PRO 140, (ii) the probability the Company will enter into a future financing and (iii) and the potential price of a future financing.

The fair value of the derivative liability is significantly influenced by the Company s trading market price of its stock, stock price volatility, changes in interest, assumptions regarding the adjusted conversion price and early redemption or conversion of the AVCP Notes.

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Note 6 Stock Options and Warrants

The Company has one active stock-based equity plan at November 30, 2016, the CytoDyn Inc. 2012 Equity Incentive Plan (the 2012 Plan) and one stock-based equity plan that is no longer active, but under which certain prior awards remain outstanding, the CytoDyn Inc. 2004 Stock Incentive Plan (the 2004 Plan and, together with the 2012 Plan, the Incentive Plans). The 2012 Plan was approved by stockholders at the Company s 2012 annual meeting to replace the 2004 Plan. The 2012 Plan was amended by stockholder approval in February 2015 to increase the number of shares available for issuance from 3,000,000 to 5,000,000 shares of common stock and in March 2016 to increase the number of shares available for issuance from 5,000,000 to 7,000,000 shares of common stock. As of November 30, 2016, the Company had 550,930 shares available for future stock-based grants under the 2012 Plan.

Stock Options

During the six-months ended November 30, 2016, the Company granted annual stock option awards to directors to purchase a total of 300,000 shares of common stock with an exercise price of $1.09 per share. These option awards vest quarterly over one year and have a ten-year term. The grant date fair value related to these options was $0.78 per share. An additional stock option covering 100,000 shares of common stock was granted to a director. The option has an exercise price of $0.68 and vests 25% immediately with the remainder ratably over one year. The grant date fair value related to the option award was $0.53 per share.

During the six-months ended November 30, 2016, the Company granted options covering an aggregate of 1,050,000 shares of common stock to executive management and certain employees with exercise prices of $1.09 and $1.10 per share. The options vest annually over three years, have a ten-year term and grant date fair values of $0.75 and $0.76 per share, respectively.

Warrants

During the six-months ended November 30, 2016, in connection with private equity offerings, as fully described in Note 10, the Company issued common stock warrants covering 182,375 shares of common stock to investors. The warrants have a five-year term and an exercise price of $1.35 per share. During the six months ended November 30, 2016, holders of warrants covering 774,097 shares of common stock exercised the right to purchase such shares at either $0.50 or $0.75 per share and the Company received proceeds of approximately $398,000. Additionally, warrants covering 138,864 shares with an exercise price of $0.75 per share were exercised pursuant to a cashless exercise provision.

During the six-months ended November 30, 2016, in connection with a registered direct equity offering completed in September 2016, as fully described in Note 11, the Company issued common stock warrants covering 6,666,667 shares of common stock to investors. The investor warrants have a five-year term and an exercise price of $1.00 per share. In connection with this offering, the Company also issued common stock warrants covering 1,066,667 shares of common stock to the placement agent. The placement agent warrants have a five-year term and an exercise price of $0.825 per share.

Compensation expense related to stock options and warrants for the three and six-months ended November 30, 2016 and November 30, 2015 was approximately $335,000 and $688,000 and $239,000 and $591,000, respectively. The grant date fair value of options and warrants vested during the three and six-month periods ended November 30, 2016 and November 30, 2015 was approximately $279,000 and $530,000 and $123,000 and $324,000, respectively. As of November 30, 2016, there was approximately $1,124,000 of unrecognized compensation expense related to share-based payments for unvested options, which is expected to be recognized over a weighted average period of

1.83 years.

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The following table represents stock option and warrant activity as of and for the six-months ended November 30, 2016:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Options and warrants outstanding May 31, 2016	63,307,150	$ 0.83	3.20	$ 9,863,492
Granted	9,365,709	1.00		
Exercised	(912,961)	0.55		
Forfeited/expired/cancelled	(7,343,911)	1.12		
Options and warrants outstanding November 30, 2016	64,415,987	0.83	3.98	83,000
Outstanding exercisable November 30, 2016	61,352,320	$ 0.82	3.77	$ 79,000

Note 7 Acquisition of Patents

As discussed in Note 8 below, the Company consummated an asset purchase on October 16, 2012, and paid $3,500,000 for certain assets, including intellectual property, certain related licenses and sublicenses, FDA filings and various forms of the PRO 140 drug substance. The Company followed the guidance in Financial Accounting Standards Topic 805 to determine if the Company acquired a business. Based on the prescribed accounting, the Company acquired assets and not a business. As of November 30, 2016, the Company has recorded and is amortizing $3,500,000 of intangible assets in the form of patents. The Company estimates the acquired patents have an estimated life of ten years. Subsequent to the acquisition date, the Company has continued to expand, amend and file new patents central to its current clinical trial strategies, which, in turn, have extended the protection period for certain methods of using PRO 140 and formulations comprising PRO 140 out through at least 2026 and 2031, respectively, in various countries.

The following presents intangible assets activity:

	November 30, 2016	May 31, 2016
Gross carrying amounts	$ 3,500,000	$ 3,500,000
Accumulated amortization	(1,443,750)	(1,268,750)
Total amortizable intangible assets, net	2,056,250	2,231,250
Patents currently not amortized	35,989	35,989
Carrying value of intangibles, net	$ 2,092,239	$ 2,267,239

Amortization expense related to patents was approximately $87,500 and $175,000 for the three and six-months ended November 30, 2016 and 2015. The estimated aggregate future amortization expense related to the Company s intangible assets with finite lives is estimated at approximately $350,000 per year for the next five years.

Note 8 License Agreements

During the year ended May 31, 2016, the Company executed a license agreement with a third-party licensor covering the licensor s system know-how technology with respect to the Company s use of proprietary cell lines to manufacture new PRO 140 material. In connection with this license agreement, the Company became the primary obligor of an additional £600,000 (approximately US$807,000 utilizing then-current exchange rates), which was timely paid by June 30, 2016. During the year ended May 31, 2016, the Company accrued an additional expense of £600,000 (approximately US$870,000 utilizing then-current exchange rates) in connection with the June 30, 2016 obligation. Future annual license fees and royalty rate will vary depending on whether the Company manufactures PRO 140, utilizes the third-party licensor as a contract manufacturer, or utilizes an independent party as a contract manufacturer. The licensor does not charge an annual license fee of £300,000 (approximately US$380,000) when it serves as the manufacturer. The Company has accrued the annual license fee of approximately $380,000, as of November 30, 2016.

Note 9 Commitments and Contingencies

Under the Asset Purchase Agreement, dated July 25, 2012, between the Company and Progenics Pharmaceuticals, Inc. (Progenics) (the Asset Purchase Agreement), the Company acquired from Progenics its rights to the HIV viral-entry inhibitor drug candidate PRO 140 (PRO 140), a humanized anti-CCR5 monoclonal antibody, as well as certain other related assets, including the existing inventory of bulk PRO 140 drug product, intellectual property, certain related licenses and sublicenses, and U.S. Food and Drug administration (FDA) regulatory filings. On October 16, 2012, the Company paid to Progenics $3,500,000 in cash to close the transaction. The Company is also required to pay Progenics the following milestone payments and royalties: (i) $1,500,000 at the time of the first dosing in a U.S. Phase 3 trial or non-US equivalent, which was paid during the year ended May 31, 2016; (ii) $5,000,000 at the time of the first U.S. new drug application approval by the FDA or other non-U.S. approval for the sale of PRO 140; and (iii) royalty payments of up to 5% on net sales during the period beginning on the date of the first commercial sale of PRO 140 until the later of (a) the expiration of the last to expire patent included in the acquired assets, and (b) 10 years, in each case determined on a country-by country basis. During the year ended May 31, 2016, the Company paid $1.5 million of such milestones owed to Progenics as a result of the first dosing in a U.S. Phase 3 trial. To the extent that such milestone payments and royalties are not timely made, under the terms of the Asset Purchase Agreement, Progenics has certain repurchase rights relating to the assets sold to the Company thereunder.

Payments to the third-party licenser for system know-how technology (see Note 8) and to Progenics are in addition to payments due under a Development and License Agreement, dated April 30, 1999 (the PDL License), between Protein Design Labs (now AbbVie Inc.) (PDL) and Progenics, which was assigned to the Company in the Asset Purchase Agreement, pursuant to which the Company has an exclusive worldwide license to develop, make, have made, import, use, sell, offer to sell or have sold products that incorporate the humanized form of the PRO 140 antibody developed by PDL under the agreement and must pay additional milestone payments and royalties as follows: (i) $1,000,000 upon initiation of a Phase 3 clinical trial, which was paid during the year ended May 31, 2016; (ii) $500,000 upon filing a Biologic License Application with the FDA or non-U.S. equivalent regulatory body; (iii) $500,000 upon FDA approval or approval by another non-U.S. equivalent regulatory body; and (iv) royalties of up to 7.5% of net sales for the longer of 10 years and the date of expiration of the last to expire licensed patent. Additionally, the PDL License provides for an annual maintenance fee of $150,000 until royalties paid exceed that amount. During the year ended May 31, 2016, the Company paid $1 million of such milestones. To the extent that such milestone payments and royalties are not timely made, under the terms of the PDL License, AbbVie Inc. has certain termination rights relating to the Company s license of PRO 140 thereunder. Pursuant to the foregoing Asset Purchase Agreement and PDL License, the Company accrued an expense of $2,500,000 as of May 31, 2015 in connection with the anticipated milestone payments related to the first patient dosing in a Phase 3 clinical trial, all of which was paid during the year ended May 31, 2016, as described above.

The Company has entered into project work orders, as amended, for each of its clinical trials with its clinical research organization (CRO) and related laboratory vendors. Under the terms of these agreements, the Company incurs execution fees for direct services costs, which are recorded as a current asset. In the event the Company were to terminate any trial, it may incur certain financial penalties which would become payable to the CRO. Conditioned upon the form of termination of any one trial, the financial penalties may range from an approximate low of $0.1 million to an approximate high of $0.6 million. In the remote circumstance that the Company would terminate all clinical trials, the collective financial penalties may range from an approximate low of $0.4 million to an approximate high of $1.4 million.

During the six-months ended November 30, 2016, the Company entered into agreements with commercial manufacturing companies. Under the terms of the agreements, the Company accrued approximately $2.1 million of execution fees for process validation and

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manufacturing activities, which is reflected as a current asset, as of November 30, 2016. In the event the Company were to terminate any of the agreements, it may incur certain financial penalties which would become payable to the manufacturers. Conditioned on the timing of termination, the financial penalties may range from an approximate low of $1.0 million to an approximate high of $3.0 million.

Note 10 Private Securities Offerings

During the year ended May 31, 2016, the Company conducted a series of private equity offerings (the Equity Offerings), in which accredited investors purchased unregistered common stock at either $0.75 or $1.00 per share with warrant coverage of 50% or 25%, respectively, based on the number of shares of common stock purchased. Pursuant to the Equity Offerings, the Company sold a total of 48,659,338 shares of common stock, for aggregate gross proceeds of approximately $37.6 million and issued warrants with a five-year term covering 23,254,230 shares of common stock. In conjunction with the Equity Offerings, the Company paid an aggregate cash fee of approximately $3.9 million to the placement agent and issued warrants covering an aggregate of 4,960,314 shares of common stock to the placement agent as additional compensation. The placement agent warrants had aggregate Black-Scholes valuations of approximately $2.7 million at issuance.

In June 2016, the Company conducted a private equity offering, in which accredited investors purchased unregistered common stock at $1.00 per share with warrant coverage of 25%, based on the number of shares of common stock purchased. Pursuant to the offering, the Company sold a total of 729,500 shares of common stock for aggregate gross proceeds of $729,500 and issued to the investors warrants with a five-year term covering 182,375 shares of common stock with an exercise price of $1.35 per share.

Note 11 Registered Direct Equity Offering

In September 2016, the Company entered into Securities Purchase Agreements with certain institutional investors for the sale of 13,333,334 shares of common stock at a purchase price of $0.75 per share in a registered direct equity offering (the Registered Offering), pursuant to a registration statement on Form S-3. The investors in this Registered Offering also received warrants to purchase 6,666,667 shares of common stock with an exercise price of $1.00 per share and a five-year term. The Company received net proceeds from the offering of approximately $9 million after placement fees of 8% of the gross proceeds and various expenses. In addition, the placement agent received warrants covering 1,066,667 shares (or 8% of total shares sold to investors) with a per share exercise price of $0.825 and a five-year term.

A summary of the cash proceeds of the offering is shown below:

Gross proceeds from sale of common stock	$ 10,000,000
Placement agent fees and expenses	1,010,000
Total net proceeds	$ 8,990,000

As fully described in Note 5 above, the investor warrants and the placement agent warrants issued in conjunction with the Registered Offering are required to be accounted for in accordance with ASC 480 and ASC 815.

A summary of the ASC 480 allocation of the proceeds of the offering is as follows:

Allocated to common stock and additional paid in capital	$ 6,334,417
Allocated to warrant liabilities	2,655,583
Total net proceeds	$ 8,990,000

Closing costs included 1,066,667 warrants valued at $819,200 for placement agent fees. Based upon the estimated fair value of the stock and warrants in the units, the Company allocated $241,986 to financing expense and $577,214 as stock issuance costs.

Note 12 Employee Benefit Plan

The Company has an employee savings plan (the Plan) pursuant to Section 401(k) of the Internal Revenue Code (the Code), covering all of its employees. The Company makes a qualified non-elective contribution of 3%, which consequently vests immediately. In addition, participants in the Plan may contribute a percentage of their compensation, but not in excess of the maximum allowed under the Code. During the three and six-months ended November 30, 2016 and 2015, the Company incurred an expense of approximately $9,800 and $18,600 and $5,700 and $5,700, respectively, for qualified non-elective contributions.

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Note 13 Related Party Transactions

On January 19, 2016, the Company entered into an amendment to its existing Consulting Agreement with Denis R. Burger, Ph.D., dated February 21, 2014, as previously amended November 3, 2014 (the Consulting Agreement). The Amendment names Dr. Burger, who is currently a member of the Board of Directors, to the non-executive position of Chief Science Officer and increases Dr. Burger s advisory responsibilities in that capacity. The Amendment also increases the compensation payable to Dr. Burger under the Consulting Agreement to $20,000 per month, which is in addition to any fees that Dr. Burger currently earns as a director. The Amendment was approved by the Audit Committee of the Board of Directors.

On May 10, 2016, Jordan G. Naydenov, a director with the Company, participated in the private equity offerings, as fully described in Note 9 above. Mr. Naydenov invested $1 million and received 1 million shares of common stock and a warrant covering 250,000 shares of common stock at an exercise price of $1.35. The terms and conditions of Mr. Naydenov s investment were identical to those offered to all other investors in the offering.

The Audit Committee of the Board of Directors, comprised of independent directors, reviews and approves all related party transactions. The above terms and amounts are not necessarily indicative of the terms and amounts that would have been incurred had comparable transactions been entered into with independent parties.

Note 14 Subsequent Events

On December 12, 2016, the Company entered into Securities Purchase Agreements with certain investors for the sale by the Company of up to 4,000,000 shares of common stock, at a purchase price of $0.75 per share in a registered direct equity offering. The investors in this offering also received common stock warrants covering 2,000,000 shares of common stock. The aggregate gross and net proceeds for the sale of the common stock and warrants in the offering was $3.0 million. Subject to certain ownership limitations, the warrants are exercisable commencing on the issuance date at an exercise price of $1.00 per share of common stock, subject to adjustments as provided under the terms of the warrants. The warrants are exercisable for five years from the date of issuance.

The Company determined to extend the expiration dates of certain warrants to May 31, 2017, covering an aggregate of 6,310,667 shares of common stock. The warrants were originally issued in connection with the sale of the 2013 Convertible Notes, as identified in Note 4. The warrants currently have an exercise price of $1.00 per share, and all but two warrants were exercisable through October 2016. One warrant, for the purchase of 186,667 shares of common stock, was exercisable through December 2016 and one warrant, for the purchase of 160,000 shares of common stock, is exercisable until January 15, 2017. The extended expiration date on all of these warrants is May 30, 2017. The Company s offer to extend the expiration dates of such warrants to May 31, 2017 expired on January 11, 2017 and was subject to the execution of a release of claims by each of the warrantholders.

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

This filing, contains forward-looking statements. The words anticipate, believe, expect, intend, predict, plan, estimate, project, continue, could, may, and similar terms and expressions are intended to identify forward-looki statements. These statements include, among others, information regarding future operations, future capital expenditures and future net cash flows. Such statements reflect current views with respect to future events and financial performance and involve risks and uncertainties, including, without limitation, regulatory initiatives and compliance with governmental regulations, the ability to raise additional capital, the results of clinical trials for the Company s drug candidates, and various other matters, many of which are beyond the Company s control. Should one or more of these risks or uncertainties occur, or should underlying assumptions prove to be incorrect, actual results may vary materially and adversely from those anticipated, believed, estimated, or otherwise indicated. Consequently, all of the forward-looking statements made in this filing are qualified by these cautionary statements and there can be no assurance of the actual results or developments.

The following discussion and analysis of the Company s financial condition and results of operations should be read in conjunction with the other sections of this Quarterly Report, including the Company s financial statements and related notes appearing elsewhere herein. To the extent not otherwise defined herein, capitalized terms shall have the same meanings as in such financial statements and related notes. This discussion and analysis contains forward-looking statements including information about possible or assumed results of the Company s financial condition, operations, plans, objectives and performance that involve risk, uncertainties and assumptions. The actual results may differ materially from those anticipated and set forth in such forward-looking statements.

Results of Operations

Clinical Trials Update

Phase 2b Extension Study for HIV, as Monotherapy. As previously disclosed, there are 11 trial participants in the extension study who successfully passed 37 weeks of therapy and were not discontinued. Currently, 10 out of those 11 trial participants have now surpassed two years of suppressed viral load with PRO 140 as a single agent therapy. This extension study remains ongoing.

Phase 3 Trial for HIV, as Combination Therapy. A pivotal 25-week trial for PRO 140 as a combination therapy to existing HAART drug regimens originally designed for 300 patients. Several patients have completed this trial and have transitioned to a roll-over protocol, as requested by the treating physicians to enable the patients to continue with a suppressed viral load. Previously, the FDA agreed to reduce the number of patients in this study from 300 to 150 patients. In October 2016, the FDA agreed to additional protocol modifications, including a further reduction in patients for this trial from 150 down to 30 patients and lowered the primary endpoint for viral load reduction from a viral load of 0.7log to viral load of 0.5log. Based upon these new protocol modifications, management projects that the total estimated costs for this trial will range from $8 million to $9 million.

Phase 3 Investigative Trial for HIV, as Long-term Monotherapy. A strategic trial including 300 patients to assess the treatment strategy of using PRO 140 subcutaneously as a long-acting single-agent maintenance therapy for 48 weeks in patients with suppressed viral load with CCR5-tropic HIV-1 infection. The primary endpoint is the number of patients who can maintain suppressed viral load under a PRO 140 monotherapy replacing their HAART regimen for 48 weeks. The secondary endpoint is the number of weeks a patient is off of their ART regimen. Enrollment of the first several patients was announced in December 2016 and is expected to accelerate, as experienced in the previous Phase 2b monotherapy trial. Management estimates the total cost of this trial to range from $15 million to $17 million.

Phase 2 Trial for Graft versus Host Disease. This Phase 2, randomized, double-blind, placebo-controlled, multi-center 100-day study with 60 patients is designed to evaluate the feasibility of the use of PRO 140 as an add-on therapy to standard GvHD prophylaxis treatment for prevention of acute GvHD in adult patients with acute myeloid leukemia (AML) or myelodysplastic syndrome (MDS) undergoing allogeneic hematopoietic stem cell transplantation (HST). Enrollment of the first patient is expected in the first half of calendar 2017. Management estimates the cost of this trial to be approximately $3.5 million to $4 million.

Rollover Study. This study is designed for patients who successfully complete the Phase 3 Combination Therapy trial and the treating physicians request a continuation of PRO 140 therapy for their patients. If this study enrolls 30 patients from the Phase 3 trial and all patients remain in the Rollover study for one year, management estimates the cost of this study to be approximately $3.5 million to $4 million.

Results of Operations for the three months ended November 30, 2016 and 2015 are as follows:

For the three months ended November 30, 2016 and November 30, 2015, the Company had no activities that produced revenues from operations.

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For the three months ended November 30, 2016, the Company incurred a net loss of approximately $5.5 million, as compared to a net loss of approximately $5.3 million for the corresponding period in 2015. The moderately higher net loss of approximately $0.2 million was attributable to increases in research and development expenses of approximately $2.7 million and general and administrative expenses of approximately $0.5 million, which were offset in part by a reduction in non-cash interest expense of approximately $1.8 million and a non-cash unrealized gain of approximately $1.2 million arising from a reduction in derivative liability associated with certain warrants.

For the three months ended November 30, 2016 and November 30, 2015, operating expenses totaled approximately $6.2 million and $2.9 million, respectively, consisting of research and development, general and administrative expenses and amortization and depreciation. The increase in operating expenses of approximately $3.3 million reflected increased research and development of approximately $2.7 million, coupled with increased general and administrative expenses of approximately $0.5 million.

General and administrative expenses, which totaled approximately $1.7 million for the three months ended November 30, 2016, were comprised of salaries and benefits, non-cash stock-based compensation expense, professional fees, insurance and various other expenses. The increase in general and administrative expenses of approximately $0.5 million for the three months ended November 30, 2016 over the comparable period a year ago was due to higher salaries owing, in part, to increased number of employees and increases for certain professional fees and corporate insurance coverages.

Research and development expenses, which totaled approximately $4.4 million for the three months ended November 30, 2016, increased approximately $2.7 million over the same 2015 period. This increase was attributable to higher clinical trial expenses, combined with an expansion of the Company s chemistry, manufacturing and controls (or CMC) activities in connection with the preparation of a biologics license application (BLA) for submission to the FDA. The Company expects research and development expenses to trend higher, as the two ongoing Phase 3 trials with PRO 140 continue, and the Company expects to incur certain additional expenses as the Company continues to expand activities related to manufacturing PRO 140 material for future use that conforms with current good manufacturing practices (or cGMP) established by the FDA.

For the three months ended November 30, 2016, the Company recognized a reduction in derivative liability of approximately $1.2 million, which is associated with certain warrants. This non-cash unrealized gain, or benefit, was offset by non-cash interest expense of approximately $0.5 million, as compared to $2.4 million of non-cash interest expense incurred in the comparable quarter of 2015, as all outstanding debt was converted or repaid during the year ended May 31, 2016. The Company continues to evaluate the need for additional financing as described under the heading Liquidity and Capital Resources below.

The future trends of all expenses are expected to be primarily driven by the future outcomes of clinical trials and the correlative effect on research and development expenses, especially FDA regulatory requirements. Additional expenses are anticipated to be incurred in connection with the manufacturing of new commercial grade PRO 140, along with the necessary regulatory processes to confirm its qualification for future sale, if approved. The Company s ability to continue to fund operating expenses will depend on its ability to raise additional capital. See in particular, Item 1A Risk Factors in the Annual Report on Form 10-K for the year ended May 31, 2016.

Results of Operations for the six months ended November 30, 2016 and 2015 are as follows:

For the six-months ended November 30, 2016, the Company had a net loss of $10.8 million, as compared to a net loss of approximately $14.2 million for the similar 2015 period. The approximate decrease of $3.4 million in net loss for 2016 from 2015 was primarily attributable to a decline in interest expense of approximately $4.1 million, coupled with an increase in the benefit of a reduction in derivative liability of approximately $0.6 million, offset in part by increases in general and administrative expenses of approximately $0.9 million and research and development expenses of approximately $1.1 million.

For the six months ended November 30, 2016 and November 30, 2015, operating expenses totaled approximately $11.5 million and $9.6 million, respectively, consisting primarily of research and development, general and administrative expenses and amortization and depreciation. The increase in operating expenses of approximately $1.9 million over the comparable 2015 period reflected higher general and administrative expenses of approximately $0.9 million together with increased research and development of approximately $1.1 million.

General and administrative expenses, which totaled approximately $3.3 million for the six months ended November 30, 2016, were comprised of salaries and benefits, non-cash stock-based compensation expense, professional fees, insurance and various other expenses. The increase in general and administrative expenses of approximately $0.9 million for the six months ended November 30, 2016 over the comparable 2015 period was due to higher total compensation expenses combined with increases for professional fees and corporate insurance coverages.

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Research and development expenses, which totaled approximately $8.1 million for the six months ended November 30, 2016, increased approximately $1.1 million over the same 2015 period. This increase was attributable to higher clinical trial expenses, combined with an expansion of the Company s CMC activities in connection with the preparation of a BLA. The Company expects research and development expenses to trend higher, as the two ongoing Phase 3 trials with PRO 140 continue, and the Company expects to incur certain additional expenses as the Company continues to expand activities related to manufacturing cGMP PRO 140 material for future use

For the six months ended November 30, 2016 the Company recognized an unrealized gain, or a non-cash benefit from a decline in derivative liability of approximately $1.2 million, as compared to an approximate benefit of $0.6 million in the comparable 2015 period. Interest expense for the six months ended November 30, 2016 of approximately $0.5 million dropped approximately $4.1 million compared to the same six-month period a year ago, as all outstanding debt was converted or repaid during the year ended May 31, 2016 and no inducement interest expense was incurred during the current six-month period. The Company continues to evaluate the need for additional financing as described under the heading Liquidity and Capital Resources below.

The future trends of all expenses will be primarily driven by the future outcomes of clinical trials and the correlative effect on research and development expenses, especially FDA regulatory requirements, in addition to the manufacturing of new commercial grade PRO 140, along with the necessary regulatory processes to confirm its qualification for future sale, if approved. The Company s ability to continue to fund operating expenses will depend on its ability to raise additional capital. See in particular, Item 1A Risk Factors in the Annual Report on Form 10-K for the year ended May 31, 2016.

Liquidity and Capital Resources

The Company s cash position at November 30, 2016 decreased approximately $0.8 million to approximately $8.8 million, as compared to a balance of approximately $9.6 million as of May 31, 2016. The net decrease in cash for the six-months ended November 30, 2016 was attributable to net cash provided by financing activities of approximately $9.9 million, offset by net cash used in operating activities of approximately $10.8 million used in operating activities.

As of November 30, 2016, the Company had positive working capital of approximately $7.2 million compared to positive working capital of approximately $7.9 million at May 31, 2016, a decrease of approximately $0.7 million attributable primarily to growth in accounts payable.

Net cash used in operating activities totaled approximately $10.8 million during the six-months ended November 30, 2016, which reflects an increase of approximately $2.3 million of net cash used in operating activities over the six-months ended November 30, 2015. The increase in net cash used in operating activities was due to the effect on working capital owing to a comparable increases in current assets and current liabilities totaling approximately $5.7 million, offset in part by a decline in the net loss of approximately $3.3 million and a substantial reduction in interest expense for the six months ended November 30, 2016.

Net cash used in investing activities was immaterial for both six month periods.

Net cash provided by financing activities of approximately $9.9 million during the six months ended November 30, 2016 declined approximately $0.8 million compared to $10.7 million during the six months ended November 30, 2015. The decline in net cash provided from financing activities was attributable to an approximate reduction in net proceeds from the sale of common stock and warrants of approximately $2.0 million, offset by approximate proceeds from the exercise of warrants of $0.4 million in the current six month period and payments to retire debt of approximately $0.8 million during the six months ended November 30, 2015.

As reported in the accompanying financial statements, for the six-months ended November 30, 2016 and November 30, 2015, the Company incurred net losses of approximately $10.8 million and $14.1 million, respectively. The Company has no activities that produced revenue in the periods presented and has sustained operating losses since inception. The Company s ability to continue as a going concern is dependent upon its ability to raise additional capital, commence operations and achieve a level of profitability. Since inception, the Company has financed its activities principally from the sale of public and private equity securities and proceeds from convertible notes payable and related party notes payable. The Company intends to finance its future operating activities and its working capital needs largely from the sale of equity securities and perhaps debt securities, combined with additional funding from other traditional financing sources. The sale of equity and convertible debt securities may result in dilution to stockholders and those securities may have rights senior to those of common shares. If the Company raises additional funds through the issuance of preferred stock, convertible debt securities or other debt financing, these activities or other debt could contain covenants that would restrict the Company s operations. Any other third-party funding arrangements could require the Company to relinquish valuable rights. The Company will require additional capital beyond its currently anticipated needs. On August 26, 2016, the Company filed a registration statement on Form S-3 universal shelf registration statement covering $100 million of securities. On September 9, 2016, the registration statement was declared effective. The Company intends to utilize this shelf registration statement to raise additional capital through the sale of its securities. Additional capital, if available, may not be available on reasonable terms. Please refer to the risk factors under Item 1.A. to the Company s Annual Report on Form 10-K.

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The Company has not generated revenue to date, and will not generate product revenue in the foreseeable future. The Company expects to continue to incur operating losses as it proceeds with clinical trials with respect to PRO 140 and continue to advance it through the product development and regulatory process. The future trends of all expenses will be driven by the future outcomes of the clinical trials and their correlative effect on research and development expenses, especially FDA regulatory requirements, in addition to the manufacturing of new commercial grade PRO 140, along with the necessary regulatory processes to confirm its qualification for future sale, if approved. The Company will require a significant amount of additional capital in the future to fulfill BLA requirements related to manufacturing PRO 140 for commercial use. In connection with this undertaking, the Company recently entered into an arrangement with a new third party contract manufacturing organization (CMO) to provide process transfer, validation and manufacturing services for PRO 140. Management believes its new CMO will best serve the Company s strategic objectives for the anticipated BLA filing and, if approved, the long-term commercial manufacturing capabilities for PRO 140. This new CMO undertaking is anticipated to require approximately $25 million of additional capital over the next two calendar years.

Under the Asset Purchase Agreement (the Asset Purchase Agreement), dated July 25, 2012, between the Company and Progenics Pharmaceuticals, Inc. (Progenics), the Company acquired from Progenics its proprietary HIV viral-entry inhibitor drug candidate PRO 140 (PRO 140), a humanized anti-CCR5 monoclonal antibody, as well as certain other related assets, including the existing inventory of bulk PRO 140 drug product, intellectual property, certain related licenses and sublicenses, and U.S. Food and Drug administration (FDA) regulatory filings. On October 16, 2012, the Company paid $3,500,000 in cash to Progenics to close the acquisition transaction. The Company is also required to pay Progenics the following milestone payments and royalties: (i) $1,500,000 at the time of the first dosing in a U.S. Phase 3 trial or non-US equivalent, which was paid during the three months ended February 29, 2016; (ii) $5,000,000 at the time of the first US new drug application approval by the FDA or other non-U.S. approval for the sale of PRO 140; and (iii) royalty payments of up to five percent (5%) on net sales during the period beginning on the date of the first commercial sale of PRO 140 until the later of (a) the expiration of the last to expire patent included in the acquired assets, and (b) 10 years, in each case determined on a country-by country basis. Payments to Progenics are in addition to payments due under a Development and License Agreement, dated April 30, 1999 (the PDL License), between Protein Design Labs (now AbbVie Inc.) and Progenics, which was assigned to us in the PRO 140 transaction, pursuant to which the Company must pay additional milestone payments and royalties as follows: (i) $1,000,000 upon initiation of a Phase 3 clinical trial, which was paid during the three months ended February 29, 2016; (ii) $500,000 upon filing a Biologic License Application with the FDA or non-U.S. equivalent regulatory body; (iii) $500,000 upon FDA approval or approval by another non-U.S. equivalent regulatory body; and (iv) royalties of up to 7.5% of net sales for the longer of 10 years and the date of expiration of the last to expire licensed patent. Additionally, the PDL License provides for an annual maintenance fee of $150,000 until royalties paid exceed that amount.

As of the date of this filing, it is management s conclusion that the probability of achieving the subsequent future scientific research milestones is not reasonably determinable, thus the future milestone payments payable to Progenics and its sub-licensors are deemed contingent consideration and, therefore are not currently accruable.

<u>Off-Balance Sheet Arrangements</u>

The Company does not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on its financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

Item 3. Quantitative and Qualitative Disclosures about Market Risk.

Not Applicable.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

As of November 30, 2016, under the supervision and with the participation of the Company s Chief Executive Officer and Chief Financial Officer, management has evaluated the effectiveness of the design and operations of the Company s disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934). Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company s disclosure controls and procedures were not effective as of November 30, 2016, as a result of material weaknesses in internal control over financial reporting because of inadequate segregation of duties over authorization, review and recording of transactions, as well as the financial reporting of such transactions. Management continues to implement controls and procedures, and continues to remediate the material weaknesses noted above. With the assistance of a third party consultant, management has completed a detailed best-practices risk assessment of all general ledger accounts in its financial accounting system and is in the process of completing its documentation of all internal controls. The Company s third party consultant has also commenced testing of the effectiveness of the internal control framework for the second fiscal quarter ending November 30, 2016. Despite the existence of a limited number of material weaknesses, management believes the financial information presented herein is materially correct and fairly presents the financial position and operating results of the quarter ended November 30, 2016 in accordance with U.S. GAAP.

Internal Control Over Financial Reporting

Changes in Control Over Financial Reporting

Although changes in the Company s internal control over financial reporting occurred during the quarter ended November 30, 2016, management believes that such changes did not materially affect, or are not reasonably likely to materially affect, the Company s internal control over financial reporting. Notwithstanding the foregoing, the Company continued to document its framework of internal controls and its third party consultant initiated a review of the sufficiency of the control environment and has commenced testing the effectiveness of such controls as of November 30, 2016, with the objective to provide management and the audit committee of the board of directors with an interim report regarding the Company s progress to remediate material weaknesses previously identified and reported. It is management s goal to fully remediate all material weaknesses by the end of the May 31, 2017 fiscal year.

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PART II

Item 1. Legal Proceedings.

None.

Item 1A. Risk Factors.

There have been no material changes in the risk factors applicable to us from those identified in the Annual Report on Form 10-K filed with the SEC on July 19, 2016.

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

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not Applicable.

Item 5. Other Information.

None.

Item 6. Exhibits.

(a) Exhibits:

4.1	Form of Warrant Agreement (September 2016 Offering) (incorporated by reference to Exhibit 4.1 to the Registrants Current Report on Form 8-K filed September 12, 2016).
10.1	Form of Securities Purchase Agreement (September 2016 Offering) (incorporated by reference to Exhibit 10.1 to the Registrants Current Report on Form 8-K filed September 12, 2016).
31.1*	Rule 13a-14(a) Certification by CEO of Registrant.
31.2 *	Rule 13a-14(a) Certification by CFO of the Registrant.
32.1 *	Certification of CEO of the Registrant pursuant to 18 U.S.C. Section 1350.
32.2 *	Certification of CFO of the Registrant pursuant to 18 U.S.C. Section 1350.
101.INS *	XBRL Instance Document.
101.SCH *	XBRL Taxonomy Extension Schema Document.

101.CAL *	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF *	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB *	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE *	XBRL Taxonomy Extension Presentation Linkbase Document.

* Filed herewith.

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SIGNATURES

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

	CYTODYN INC.
	(Registrant)
Dated: January 13, 2017	/s/ Nader Z. Pourhassan Nader Z. Pourhassan President and Chief Executive Officer
Dated: January 13, 2017	/s/ Michael D. Mulholland Michael D. Mulholland Chief Financial Officer, Treasurer and Corporate Secretary

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EXHIBIT INDEX

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101.LAB *	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE *	XBRL Taxonomy Extension Presentation Linkbase Document.

* Filed herewith.

: Times New Roman; FONT-SIZE: 10pt">The Company’s subsidiary, GOGAS, issued an option and warrants. The GOGAS stock option was issued in June 2011 and is exercisable until April 9, 2015 at an exercise price of $5.0 million. The GOGAS warrants were issued in November 2010 and expired on November 12, 2011. The Company’s subsidiary, GEIC, issued a stock option in April 2010 that was exchanged in June 2011 for the GOGAS stock option. At March 31, 2012, the fair value of the GOGAS stock option was nil.

The fair value of outstanding derivative instruments recorded as assets in the accompanying consolidated balance sheets were as follows:

Asset Derivatives	Balance Sheet Location	March 31, 2012	December 31, 2011
		(in thousands)	
Derivatives not designated or not qualifying as hedging instruments:			
Energy contracts and options	Other current assets	$ 27	$ 446

The fair value of outstanding derivative instruments recorded as liabilities in the accompanying consolidated balance sheets were as follows:

Liability Derivatives	Balance Sheet Location	March 31, 2012	December 31, 2011
		(in thousands)	

Derivatives not designated or not qualifying as hedging instruments:					
Energy contracts and options	Other current liabilities	$	—	$	938

The effects of derivative instruments on the consolidated statements of operations were as follows:

Derivatives not designated or not qualifying as hedging instruments	Location of (Gain) Loss Recognized on Derivatives	Amount of (Gain) Loss Recognized on Derivatives Three Months Ended March 31, 2012	2011
		(in thousands)	
Energy contracts and options	Direct cost of revenues	$ (510)	$ (120)
GOGAS warrants	Selling, general and administrative expense	—	(85)
Total		$ (510)	$ (205)

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At March 31, 2012 and December 31, 2011, the Company's energy contracts and options were all traded on the New York Mercantile Exchange which mitigated the Company's exposure to credit loss from nonperformance by the counterparty.

On October 31, 2011, MF Global, the Company’s former clearing broker, filed for bankruptcy protection. On that date, IDT Energy held $1.65 million of cash on deposit with MF Global in support of hedging positions related to IDT Energy’s commodity supply. Assets held by MF Global were placed under the control of the court appointed bankruptcy trustee to be released as deemed appropriate. In November 2011, the Company transferred its hedging securities to an alternative clearing broker. In October 2011, the Company recognized a $0.45 million loss, relating to its cash deposit with MF Global, based on management’s best estimate of the unrecoverable amount. As of March 31, 2012, the remaining balance of $0.35 million is included in ”Other current assets” in the Company’s consolidated balance sheet, as such cash was not readily available for withdrawal. The Company believes that the $0.35 million due from the bankrupt broker is collectible.

Note 4—Investment in American Shale Oil, LLC

The Company accounts for its 50% ownership interest in AMSO, LLC using the equity method since the Company has the ability to exercise significant influence over its operating and financial matters, although it does not control AMSO, LLC. AMSO, LLC is a variable interest entity, however, the Company has determined that it is not the primary beneficiary, as the Company does not have the power to direct the activities of AMSO, LLC that most significantly impact AMSO, LLC’s economic performance.

AMSO has agreed to fund AMSO, LLC’s expenditures as follows: 20% of the initial $50 million of expenditures, 35% of the next $50 million in approved expenditures and 50% of approved expenditures in excess of $100 million. AMSO has also agreed to fund 40% of the costs of the one-time payment for conversion of AMSO, LLC’s research, development and demonstration lease to a commercial lease, in the event AMSO, LLC’s application for conversion is approved. The remaining amounts are to be funded by Total S.A. (“Total”). As of March 31, 2012, the cumulative contributions of AMSO and Total to AMSO, LLC were $52.8 million. Through December 31, 2011, AMSO was allocated 20% of the net loss of AMSO, LLC. AMSO’s portion of the loss of AMSO, LLC increased in December 2011 from 20% to 35%, per the agreement with Total. AMSO’s allocated share of the net loss of AMSO, LLC is included in “Equity in the net loss of AMSO, LLC” in the accompanying consolidated statements of operations.

The following table summarizes the change in the balance of the Company’s investment in AMSO, LLC:

	Three Months Ended March 31,	
	2012	2011
	(in thousands)	
Balance, beginning of period	$(685)	$ 1,522
Capital contributions	1,139	1,428
Equity in the net loss of AMSO, LLC	(839)	(669)
Balance, end of period	$(385)	$ 2,281

At March 31, 2012 and December 31, 2011, the liability for equity loss in AMSO, LLC was included in the consolidated balance sheet in “Accrued expenses.”

In accordance with the agreement between the parties, AMSO was committed to a total investment of $10.0 million in AMSO, LLC, all of which, as of March 31, 2012, has been invested. AMSO remains obligated to fund its share of the expenditures it approves beyond the initial $10.0 million investment. AMSO's share of AMSO, LLC's budget for the year ending December 31, 2012 is $3.2 million. At March 31, 2012, AMSO had funded $1.0 million of its share of the 2012 budget. There are also a number of other situations where AMSO's funding obligation could increase further.

Total can increase AMSO's initial required funding commitment of $10.0 million up to an additional $8.75 million if Total notifies AMSO of its commitment to continue to fund the pilot test up to an agreed upon commitment level. To date, AMSO has not received such notification from Total. Additionally, even if AMSO were to withdraw its interest in AMSO, LLC, it will remain liable for its share of expenditures for safety and environmental reclamation related to events occurring prior to its withdrawal.

Total may terminate its obligations to make capital contributions and withdraw as a member of AMSO, LLC. If Total withdraws as a member of AMSO, LLC, AMSO may also terminate its obligations to make capital contributions and withdraw as a member of AMSO, LLC. Although, subject to certain situations, AMSO and Total are not obligated to make additional contributions beyond their respective shares, they could dilute or forfeit their ownership interests in AMSO, LLC if they fail to contribute their respective shares for additional funding.

At March 31, 2012, the Company's maximum exposure to additional loss as a result of its required investment in AMSO, LLC was $1.8 million, based on AMSO, LLC's 2012 budget. The Company's maximum exposure to additional loss could increase based on the situations described above. The maximum exposure at March 31, 2012 was determined as follows:

	(in thousands)
AMSO's total committed investment in AMSO, LLC	$13,211
Less: cumulative capital contributions to AMSO, LLC	(10,993)
Less: liability for equity loss in AMSO, LLC at March 31, 2012	(385)
Maximum exposure to additional loss	$1,833

Summarized unaudited statements of operations of AMSO, LLC are as follows:

	Three Months Ended March 31, 2012	2011
	(in thousands)	
Operating expenses:		
General and administrative	$ 122	$ 168
Research and development	2,274	3,178
Total operating expenses	2,396	3,346
Loss from operations and net loss	$ (2,396)	$ (3,346)

Note 5—Equity

Changes in the components of equity were as follows:

	Three Months Ended March 31, 2012 Attributable to Genie	Noncontrolling Interests	Total
	(in thousands)		
Balance, December 31, 2011	$127,338	$(7,039)	$120,299
Dividends declared ($0.033 per share)	(758)	—	(758)
Restricted Class B common stock purchased from employees	(133)	—	(133)
Exercise of stock options	5	—	5
Stock-based compensation	683	—	683
Grants of equity of subsidiary	(518)	518	—
Comprehensive income:			
Net income	604	599	1,203
Other comprehensive income	34	—	34
Comprehensive income	638	599	1,237
Balance, March 31, 2012	$127,255	$(5,922)	$121,333

Dividend Payments

On January 5, 2012, the Company paid a cash dividend of $0.05 per share to shareholders of record at the close of business on December 22, 2011 of the Company's Class A common stock and Class B common stock. The aggregate dividends paid were $1.1 million. On April 3, 2012, the Company paid a cash dividend of $0.033 per share to shareholders of record at the close of business on March 26, 2012 of the Company's Class A common stock and Class B common stock. The dividend paid on April 3, 2012 was for the two-month period of November and December 2011 that represents the period between the end of the Company's prior fiscal quarter and the beginning of the new fiscal quarter in connection with the change in the Company's fiscal year to a calendar year, and represented a pro-rated dividend of 2/3rd of the normal quarterly dividend. The aggregate dividends paid were $0.8 million.

The Company will pay an ordinary dividend of $0.05 per share on May 30, 2012 to stockholders of the Company's Class A and Class B common stock as of the record date of May 21, 2012. The Company currently intends to continue to pay a quarterly dividend of $0.05 per share on its Class A common stock and Class B common stock, subject to the approval of the Company's Board of Directors.

Grants of Equity of Subsidiaries

On March 28, 2012, the Compensation Committee of the Company's Board of Directors approved the grant of equity interests in certain subsidiaries of the Company to Howard Jonas, the Chairman of the Company's Board of Directors. The Compensation Committee approved the following grants to Mr. Jonas: (1) deferred stock units for 50.56 shares of common stock of IDT Energy (representing 2.5% of the equity in IDT Energy on a fully diluted basis), (2) 0.25 ordinary shares of IEI (representing 0.25% of the equity in IEI on a fully diluted basis), (3) 3.05 ordinary shares of an early stage exploration venture in Israel, Genie Israel Oil & Gas, Ltd. ("GIOG") (representing 0.30% of the equity in GIOG on a fully diluted basis), and (4) shares representing 0.25% of the Company's entity that will seek to develop oil shale opportunities in an Asian country ("the Asian Venture").

In addition, the Compensation Committee approved grants of interests representing 1.13% of the equity in IDT Energy, 1.23% of the equity in IEI, 1.68% of the equity in GIOG and 1.00% in the Asian Venture to certain of the Company's officers and employees.

At March 31, 2012, the Company recorded a reduction in “Additional paid-in capital” and an increase in “Noncontrolling interests” of $0.5 million for the issuance of the grants of 1.13% of the equity in IDT Energy to officers and employees. The Company will record additional adjustments to “Additional paid-in capital” and “Noncontrolling interests” as the remainder of these equity grants are issued. The Company is in the process of estimating the fair value of the grants of these equity interests on the date of the grant, which is expected to be in the range of approximately $3.0 million to $3.7 million. The estimated fair value will be recognized as compensation cost on a straight-line basis over the vesting period. The Company did not recognize compensation cost related to these grants of equity interests in the three months ended March 31, 2012.

Stock Repurchase Program

On December 8, 2011, the Board of Directors of the Company approved a stock repurchase program for the repurchase of up to an aggregate of 20 million shares of the Company’s Class B common stock for up to an aggregate of $20 million. At March 31, 2012, no repurchases had been made and 20 million shares remained available for repurchase under the stock repurchase program.

2011 Stock Option and Incentive Plan

The Company adopted its 2011 Stock Option and Incentive Plan (“Incentive Plan”) to provide incentives to executives, employees, directors and consultants of the Company. Incentives available under the Incentive Plan may include restricted stock, stock options, stock appreciation rights, limited rights, and deferred stock units. The Incentive Plan is administered by the Company’s Compensation Committee. At March 31, 2012, the Company had 0.5 million shares of Class B common stock available for awards under its Incentive Plan.

Stock-Based Compensation

On November 3, 2011, the Company granted certain of its employees and directors 186 thousand restricted shares of the Company’s Class B common stock and 356 thousand options to purchase shares of the Company’s Class B common stock. In addition, on November 3, 2011, the Company granted nonemployee individuals that provide services to the Company, 52 thousand restricted shares of the Company’s Class B common stock and 52 thousand options to purchase shares of the Company’s Class B common stock. The restricted shares and options, which were granted under the Company’s Incentive Plan, vest over the expected service period, subject to forfeiture based on service conditions. The options have a term of 10 years and an exercise price of $6.85 equal to the fair market value of the underlying shares on the grant date. The fair value of the restricted stock and options on the date of the grant was estimated at $1.6 million and $1.8 million, respectively, which will be recognized over the service period. The fair value of the options on the grant date was estimated using a Black-Scholes valuation model and the following assumptions: (1) expected volatility of 67% based on historical volatility of comparable companies and other factors, (2) a discount rate of 1.06% – 1.62%, (3) expected life of 6 - 7 years and (4) zero dividend yield. In addition, in January or March 2012, each of the four non-employee members of the Company’s Board of Directors received 2,920 restricted shares of the Company’s Class B common stock, which vested immediately upon grant. The fair value of the restricted shares was determined based on the closing price of the Company’s Class B common stock on the date of grant. The Company recognized compensation cost related to the vesting of these shares and options of $0.4 million in the three months ended March 31, 2012.

As part of the Spin-Off, holders of restricted Class B common stock of IDT received, in respect of those restricted shares, one restricted share of the Company's Class B common stock for every restricted share of IDT that they owned as of the record date for the Spin-Off. Such restricted shares of the Company's Class B common stock are restricted under the same terms as the IDT restricted stock in respect of which they were issued. The restricted shares of the Company's Class B common stock received in the Spin-Off are subject to forfeiture on the same terms, and their restrictions will lapse at the same time, as the corresponding IDT shares. The unrecognized compensation cost relating to the Company's restricted shares at March 31, 2012 was $2.3 million, which is expected to be recognized over the remaining vesting period that ends in December 2013. The Company recognized compensation cost related to the vesting of these shares of $0.3 million and $0.2 million in the three months ended March 31, 2012 and 2011, respectively.

In order to equitably adjust the value of the options to purchase IDT Class B common stock that were outstanding on the Spin-Off date, IDT proportionately reduced the exercise price of each such option based on the trading price of IDT following the Spin-Off. Further, each option holder shared ratably in a pool of 50 thousand options to purchase shares of the Company's Class B common stock with an exercise price of $6.85 equal to the market value on the issuance date and an expiration date equal to the expiration of the corresponding IDT options held by such option holder. The options to purchase shares of the Company were issued under the Company's Incentive Plan. The adjustment to the exercise price of the options to purchase IDT shares and the issuance of the 50 thousand options to purchase the Company's shares were accounted for as a modification. No incremental charge was required as a result of the modification.

In October 2009, GEIC granted common stock representing 0.5% of its outstanding shares at the time to a consultant for consulting services through July 2011. The share award vested over the related service period. In the three months ended March 31, 2011, the Company recorded stock-based compensation of $0.1 million related to this grant.

Variable Interest Entity

In 2011, an employee of IDT until his employment was terminated effective December 30, 2011, incorporated Citizens Choice Energy, LLC ("CCE"), which is a REP that resells electricity and natural gas to residential and small business customers in the State of New York. Tari Corporation ("Tari") is the sole owner of CCE. In addition, DAD Sales, LLC ("DAD"), which is 100% owned by Tari, uses its network of door-to-door sales agents to obtain customers for CCE. The Company provided CCE and DAD with substantially all of the cash required to fund their operations. The Company determined that at the present time it has the power to direct the activities of CCE and DAD that most significantly impact their economic performance and it has the obligation to absorb losses of CCE and DAD that could potentially be significant to CCE and DAD on a stand-alone basis. The Company therefore determined that it is the primary beneficiary of both CCE and DAD, and as a result, the Company consolidates CCE and DAD with its IDT Energy segment.

The Company does not own any interest in CCE or DAD and thus the net income or loss incurred by CCE and DAD has been attributed to noncontrolling interests in the accompanying consolidated statements of operations. CCE's net income in the three months ended March 31, 2012 was $1.0 million and CCE's net loss in the three months ended March 31, 2011 was $47 thousand. DAD's net loss in the three months ended March 31, 2012 and 2011 was $0.2 million and nil, respectively. In the three months ended March 31, 2012 and 2011, the Company provided CCE and DAD with net funding of $0.1 million and nil, repectively, in order to finance their operations.

Summarized combined balance sheets of CCE and DAD are as follows:

	March 31, 2012	December 31, 2011
	(in thousands)	
Assets		
Cash and cash equivalents	$1,682	$763
Restricted cash	4	81
Trade accounts receivable	3,023	2,766
Prepaid expenses	161	70
Other current assets	139	413
Fixed assets, net	51	57
Other assets	452	282
Total assets	$5,512	$4,432

Liabilities and members’ interests		
Current liabilities	$1,694	$1,631
Due to IDT Energy	5,947	5,820
Noncontrolling interests	(2,129)	(3,019)
Total liabilities and noncontrolling interests	$5,512	$4,432

The assets of CCE and DAD may only be used to settle obligations of CCE and DAD, and may not be used for other consolidated entities. The liabilities of CCE and DAD are non-recourse to the general credit of the Company’s other consolidated entities.

In April 2012, IDT Energy and CCE entered into an Asset Purchase Agreement pursuant to which IDT Energy shall, upon the satisfaction of many conditions, acquire all of CCE’s customer accounts, accounts receivable, trade names and other customer-related assets in exchange for the discharge and release of CCE’s debt and payment obligations to IDT Energy. The closing conditions include customary conditions as well as the discharge or satisfactory resolution of certain claims pending against CCE, and IDT Energy is under no obligation to assume any liability related thereto. At March, 31, 2012, the amount of CCE debt to be discharged was $4.8 million. In addition, in April 2012, IDT Energy entered into a Consulting Agreement with Tari for customer networking services and other sales related services. Finally, in April 2012, IDT Energy and DAD entered into a Client Agreement whereby DAD will use its network of door-to-door sales agents to obtain customers for IDT Energy in exchange for cash commissions.

Note 6—Earnings Per Share

Basic earnings per share is computed by dividing net income attributable to all classes of common stockholders of the Company by the weighted average number of shares of all classes of common stock outstanding during the applicable period. Diluted earnings per share is computed in the same manner as basic earnings per share, except that the number of shares is increased to include restricted stock still subject to risk of forfeiture (non-vested) and to assume exercise of potentially dilutive stock options using the treasury stock method, unless the effect of such increase is anti-dilutive. The earnings per share for the period prior to the Spin-Off were calculated as if the number of shares outstanding at the Spin-Off were outstanding during the period.

The weighted-average number of shares used in the calculation of basic and diluted earnings per share attributable to the Company’s common stockholders consists of the following:

	Three Months Ended March 31,	
	2012	2011
	(in thousands)	
Basic weighted-average number of shares	21,000	20,365
Effect of dilutive securities:		
Stock options	15	—
Non-vested restricted Class B common stock	1,945	1,977
Diluted weighted-average number of shares	22,960	22,342

In November 2010, an entity affiliated with Lord (Jacob) Rothschild purchased a 5.0% equity interest in GOGAS for $10.0 million paid in cash. Also in November 2010, Rupert Murdoch purchased a 0.5% equity interest in GOGAS for $1.0 million paid with a promissory note. The note is secured by a pledge of the shares issued in exchange for the note. The note accrues interest at 1.58% per annum, and the principal and accrued interest is due and payable on November 15, 2015. In connection with this purchase, the entity affiliated with Lord Rothschild has a one time option through November 12, 2017 to exchange its GOGAS shares for shares of the Company with equal fair value as determined by the parties. The number of shares issuable in such an exchange is not currently determinable. If this option is exercised, the shares issued by the Company may dilute the earnings per share in future periods.

Note 7—Related Party Transaction

Up until the Spin-Off, IDT, the Company’s former parent company, charged the Company for certain transactions and allocated routine expenses based on company specific items. The allocated amounts also included charges for utilizing the net operating loss of IDT, as the Company was included in IDT’s consolidated federal income tax return in all periods through the date of the Spin-Off. In addition, IDT controlled the flow of the Company’s treasury transactions. Following the Spin-off, IDT charges the Company for services it provides pursuant to the Transition Services Agreement. In the three months ended March 31, 2012 and 2011, IDT charged the Company $0.7 million and $0.6 million, respectively, which was included in “Selling, general and administrative” expense in the consolidated statements of operations. In addition, in the three months ended March 31, 2011, IDT charged the Company $4.0 million for utilizing the net operating loss of IDT, which was included in “Provision for income taxes” in the consolidated statement of operations.

Pursuant to the Transition Services Agreement, the Company provides specified administrative services to certain of IDT’s foreign subsidiaries. In the three months ended March 31, 2012, the Company charged IDT $20 thousand for these services, which reduced the Company’s “Selling, general and administrative” expense. At March 31, 2012, the Company had a receivable from IDT of $20 thousand, which was included in “Other current assets” in the consolidated balance sheet.

Note 8—Business Segment Information

The Company owns 99.3% of its subsidiary, GEIC, which owns 98.9% of IDT Energy and 92% of GOGAS. The Company has two reportable business segments: IDT Energy, an REP supplying electricity and natural gas to residential and small business customers in the Northeastern United States, and Genie Oil and Gas, which is pioneering technologies to produce clean and affordable transportation fuels from the world's abundant oil shales and other unconventional fuel resources. The Genie Oil and Gas segment consists of (1) a 50% interest in AMSO, LLC, the Company’s oil shale initiative in Colorado, and (2) an 89% interest in IEI, the Company’s oil shale initiative in Israel. Corporate costs include unallocated compensation, consulting fees, legal fees, business development expenses and other corporate-related general and administrative expenses. Corporate does not generate any revenues, nor does it incur any direct cost of revenues.

The Company’s reportable segments are distinguished by types of service, customers and methods used to provide their services. The operating results of these business segments are regularly reviewed by the Company’s chief operating decision maker.

The accounting policies of the segments are the same as the accounting policies of the Company as a whole. The Company evaluates the performance of its business segments based primarily on operating income (loss). There are no significant asymmetrical allocations to segments.

Operating results for the business segments of the Company are as follows:

(in thousands)	IDT Energy	Genie Oil and Gas	Corporate	Total
Three Months Ended March 31, 2012				
Revenues	$ 57,505	$ —	$ —	$ 57,505
Income (loss) from operations	7,370	(3,096)	(1,581)	2,693
Research and development	—	2,091	2	2,093
Equity in the net loss of AMSO, LLC	—	839	—	839
Three Months Ended March 31, 2011				
Revenues	$ 63,426	$ —	$ —	$ 63,426
Income (loss) from operations	9,858	(3,127)	(256)	6,475
Research and development	—	2,300	—	2,300
Equity in the net loss of AMSO, LLC	—	669	—	669

Note 9—Legal Proceedings

On August 15, 2010, the Israel Union for Environmental Defense (the "Union") filed a petition with the Supreme Court of Israel against various ministries of the State of Israel and the Jerusalem Regional Committee for Planning and Construction, and naming IEI, as a respondent. The petition seeks an order of the Court requiring the respondents to explain the grant of the oil shale exploratory license to IEI and setting aside or cancelling the license. The Union claims that the license was granted without following all requirements imposed by applicable law, particularly regarding environmental impact and compliance with zoning, land use and similar laws and plans. IEI filed its response on December 12, 2010. On April 29, 2011, the state attorney for Israel submitted its response on behalf of the named ministries and is defending the case on both the validity of the license and the planning procedure. The Court rejected the Union's request for an injunction and scheduled a hearing on the case for October 29, 2012. IEI believes that it followed the requirements imposed by the Ministry of National Infrastructures (the agency that issued the license) and that it is in compliance with applicable laws and regulatory requirements. If the petition were granted, it would likely have a significant adverse effect on IEI's oil shale venture.

In addition to the foregoing, the Company may from time to time be subject to other legal proceedings that have arisen in the ordinary course of business and have not been finally adjudicated. Although there can be no assurance in this regard, none of the other legal proceedings to which the Company is a party will have a material adverse effect on the Company's results of operations, cash flows or financial condition.

Note 10—Commitments and Contingencies

Purchase and Other Commitments

The Company had purchase and other commitments of $0.2 million as of March 31, 2012.

Tax Audits

The Company is subject to audits in various jurisdictions for various taxes, including income tax and utility excise tax. Specifically, IDT Energy has the following audits in process: (1) New York State income tax for fiscal 2007, fiscal 2008 and fiscal 2009, (2) New York City utility tax audit on electricity sales for the period from June 1, 2007 through December 31, 2008, and (3) New York State sales and use tax for the period from June 2003 though August 2009. In June 2011, IDT Energy received a Notice of Proposed Tax Adjustments from the New York City Finance Department related to the utility tax audit that included aggregate assessments of tax, interest and penalties of $7.2 million. In addition, IDT Energy's potential exposure for utility tax, interest and penalties for the period from January 1, 2009 through March 31, 2012 is an additional $8.5 million. As of March 31, 2012, the Company had accrued $4.4 million for the New York City utility tax audit, $2.6 million related to New York State income tax audit, and $0.8 million for the New York State sales and use tax audit. The Company's reasonably possible liability related to the New York City utility tax audit, above the amount that has been accrued, range from nil to $5.9 million. The Company's reasonably possible exposure related to the New York State income tax audit, above the amount that has been accrued, range from nil to $4.2 million. The Company's reasonably possible liability related to the New York State sales and use tax audit, above the amount that has been accrued, range from nil to $1.1 million.

At March 31, 2012, the Company has accrued for the estimated loss from these audits for which it is probable that a liability has been incurred, however amounts asserted by taxing authorities or the amount ultimately assessed against the Company could be greater than the accrued amounts. Accordingly, additional provisions may be recorded in the future as revised estimates are made or underlying matters are settled or resolved. Imposition of assessments as a result of tax audits could have an adverse effect on the Company's results of operations, cash flows and financial condition.

Other Contingencies

In June 2009, IDT Energy entered into a Preferred Supplier Agreement with BP Energy Company and BP Corporation North America Inc. (collectively “BP”), pursuant to which BP is IDT Energy’s preferred provider of electricity and natural gas. IDT Energy’s obligations to BP are secured by a first security interest in deposits or receivables from utilities in connection with their purchase of IDT Energy’s customer receivables, and in any cash deposits or letters of credit posted in connection with any collateral accounts with BP. IDT Energy’s ability to purchase electricity and natural gas under this agreement is subject to satisfaction of certain conditions including the maintenance of certain covenants. The Company is in compliance with such covenants. As of March 31, 2012, cash and cash equivalents of $0.5 million and trade accounts receivable of $27.2 million were pledged to BP as collateral for the payment of IDT Energy’s trade accounts payable to BP of $8.5 million as of March 31, 2012.

Note 11—Recently Adopted Accounting Standards and Recently Issued Accounting Standards Not Yet Adopted

On January 1, 2012, the Company adopted the accounting standard update to achieve common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards (“IFRS”). The amendments in this update (1) clarify the application of certain existing fair value measurement and disclosure requirements and (2) change certain principles or requirements for measuring fair value or disclosing information about fair value measurements. The adoption of these amendments did not impact the Company’s financial position, results of operations or cash flows.

Also on January 1, 2012, the Company adopted the accounting standard update to simplify how an entity tests goodwill for impairment. The amendments in the update allow an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity will no longer be required to calculate the fair value of a reporting unit (Step 1) unless the entity determines, based on a qualitative assessment, that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. The adoption of these amendments did not impact the Company’s financial position, results of operations or cash flows.

In December 2011, an accounting standard update was issued to enhance disclosures and provide converged disclosures in U.S. GAAP and IFRS about financial instruments and derivative instruments that are either offset on the statement of financial position or subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset on the statement of financial position. Entities will be required to provide both net and gross information for those assets and liabilities in order to enhance comparability between entities that prepare their financial statements on the basis of U.S. GAAP and entities that prepare their financial statements on the basis of IFRS. The Company is required to adopt this standard update on January 1, 2013. The Company is evaluating the impact that this standard update will have on its consolidated financial statements.

Note 12—Revolving Line of Credit

As of April 23, 2012, the Company and IDT Energy entered into a Loan Agreement with JPMorgan Chase Bank for a revolving line of credit for up to a maximum principal amount of $25.0 million. The proceeds from the line of credit may be used to provide working capital and for the issuance of letters of credit. The Company agreed to deposit cash in a money market account at JPMorgan Chase Bank as collateral for the line of credit equal to the greater of (a) $10.0 million or (b) the sum of the amount of letters of credit outstanding plus the outstanding principal under the revolving note. The Company is not permitted to withdraw funds or exercise any authority over the required balance in the collateral account. The principal outstanding will bear interest at the lesser of (a) the LIBOR rate multiplied by the statutory reserve rate established by the Board of Governors of the Federal Reserve System plus 1.0% per annum, or (b) the maximum rate per annum permitted by whichever of applicable federal or Texas laws permit the higher interest rate. Interest is payable at least every three months and all outstanding principal and any accrued and unpaid interest is due on the maturity date of April 30, 2013. The Company paid a facility fee of $37,500 and will pay a quarterly unused commitment fee of 0.08% per annum commencing on July 15, 2012 on the difference between $25.0 million and the average daily outstanding principal balance of the note. In addition, as of April 23, 2012, GEIC issued a Corporate Guaranty to JPMorgan Chase Bank whereby GEIC unconditionally guarantees the full payment of all indebtedness of the Company and IDT Energy under the Loan Agreement.

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

The following information should be read in conjunction with the accompanying consolidated financial statements and the associated notes thereto of this Quarterly Report, and the audited consolidated financial statements and the notes thereto and our Management's Discussion and Analysis of Financial Condition and Results of Operations for the year ended July 31, 2011 contained in our Registration Statement on Form 10, as filed with the U.S. Securities and Exchange Commission (or SEC).

As used below, unless the context otherwise requires, the terms "the Company," "Genie," "we," "us," and "our" refer to Genie Energy Ltd., a Delaware corporation, and its subsidiaries, collectively.

On January 30, 2012, our Board of Directors changed our fiscal year end from July 31 to December 31. This change better aligns our financial reporting with our operational and budgeting cycle and with other industry participants. We reported the results for our transitional period in a Transition Report on Form 10-Q for the five months from August 1, 2011 to December 31, 2011. Going forward, our fiscal quarters will end on the last day of March, June, September and December each year.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including statements that contain the words "believes," "anticipates," "expects," "plans," "intends," and similar words and phrases. These forward-looking statemen are subject to risks and uncertainties that could cause actual results to differ materially from the results projected in any forward-looking statement. In addition to the factors specifically noted in the forward-looking statements, other important factors, risks and uncertainties that could result in those differences include, but are not limited to, those discussed under "Risk Factors" in our Registration Statement on Form 10 as well as under Item 1A to Part II "Risk Factors" in this Quarterly Report on Form 10-Q. The forward-looking statements are made as of the date of this report and we assume no obligation to update the forward-looking statements, or to update the reasons why actual results could differ from those projected in the forward-looking statements. Investors should consult all of the information set forth in this report and the other information set forth from time to time in our reports filed with the Securities Exchange Act of 1934, including our Registration Statement on Form 10, which included our consolidated financial statements for the year ended July 31, 2011.

Overview

We own 99.3% of our subsidiary, Genie Energy International Corporation, or GEIC, which owns 98.9% of IDT Energy and 92% of Genie Oil and Gas, Inc., or GOGAS. Our principal businesses consist of:

- IDT Energy, a retail energy provider, or REP, supplying electricity and natural gas to residential and small business customers in the Northeastern United States; and

- Genie Oil and Gas, which is pioneering technologies to produce clean and affordable transportation fuels from the world's abundant oil shales and other unconventional fuel resources, which consists of (1) American Shale Oil Corporation, or AMSO, which holds and manages a 50% interest in American Shale Oil, L.L.C., or AMSO, LLC, our oil shale initiative in Colorado, and (2) an 89% interest in Israel Energy Iniatives, Ltd., or IEI, our oil shale initiative in Israel.

Genie was incorporated in January 2011. References to us in the following discussion are made on a consolidated basis as if we existed and owned IDT Energy and Genie Oil and Gas in all periods discussed.

We were formerly a subsidiary of IDT Corporation, or IDT. On October 28, 2011, we were spun-off by IDT and became an independent public company through a pro rata distribution of our common stock to IDT's stockholders (the "Spin-Off"). As a result of the Spin-Off, each of IDT's stockholders received: (i) one share of our Class A common stock for every share of IDT's Class A common stock held of record on October 21, 2011 (the "Record Date"), and (ii) one share of our Class B common stock for every share of IDT's Class B common stock held of record on the Record Date. On October 28, 2011, 1.6 million shares of our Class A common stock, and 21.1 million shares of our Class B common stock were issued and outstanding.

Prior to the Spin-Off, IDT made a capital contribution of $82.2 million to us. In addition, in connection with the capital contribution received from IDT, the amount due from IDT as of the date of the Spin-Off of $2.1 million was forgiven.

We entered into various agreements with IDT prior to the Spin-Off including a Separation and Distribution Agreement to effect the separation and provide a framework for our relationship with IDT after the Spin-Off, and a Transition Services Agreement, which provides for certain, services to be performed by us and IDT to facilitate our transition into a separate publicly-traded company. These agreements provide for, among other things, (1) the allocation between us and IDT of employee benefits, taxes and other liabilities and obligations attributable to periods prior to the Spin-Off, (2) transitional services to be provided by IDT relating to human resources and employee benefits administration, (3) the allocation of responsibilities relating to employee compensation and benefit plans and programs and other related matters, (4) finance, accounting, tax, internal audit, facilities, investor relations and legal services to be provided by IDT to us following the Spin-Off and (5) specified administrative services to be provided by us to certain of IDT's foreign subsidiaries. We expect to incur quarterly incremental costs (including for services to be provided by IDT and others) of approximately $1.5 million, including stock-based compensation, as a result of operating as a separate public company.

In addition, we entered into a Tax Separation Agreement with IDT, which sets forth the responsibilities of us and IDT with respect to, among other things, liabilities for federal, state, local and foreign taxes for periods before and including the Spin-Off, the preparation and filing of tax returns for such periods and disputes with taxing authorities regarding taxes for such periods.

Seasonality and Weather

IDT Energy's revenues are impacted by, among other things, the weather and the seasons. Weather conditions have a significant impact on the demand for natural gas for heating and electricity for air conditioning. Typically, colder winters and hotter summers create higher demand and consumption for natural gas and electricity, respectively. Milder winters and/or summers will reduce the demand for natural gas and electricity, respectively. Natural gas revenues typically increase in the first quarter due to increased heating demands and electricity revenues typically increase in the third quarter due to increased air conditioning use. Approximately 50% and 53% of IDT Energy's natural gas revenues were generated in the first quarter of 2011 and 2010, respectively, when demand for heating is highest. Although the demand for electricity is not as seasonal as natural gas, approximately 35% and 36% of IDT Energy's electricity revenues were generated in the third quarter of 2011 and 2010, respectively. As a result, our revenues and operating income are subject to material seasonal variations, and the interim financial results are not necessarily indicative of the estimated financials results for the full year.

Concentration of Customers and Associated Credit Risk

IDT Energy reduces its customer credit risk through its participation in purchase of receivable, or POR, programs for a significant portion of its receivables. Under these programs, utility companies provide billing and collection services, purchase IDT Energy's receivables and assume all credit risk without recourse to IDT Energy. IDT Energy's primary credit risk is therefore nonpayment by the utility companies. Certain of the utility companies represent significant portions of our consolidated revenues and consolidated gross trade accounts receivable balance and such concentrations increase our risk associated with nonpayment by those utility companies. We monitor the timely collections from our significant utility companies in an effort to reduce our credit risk.

The following table summarizes the percentage of consolidated revenues from utility companies that equal or exceed 10% of our consolidated revenues in the period presented (no other single customer accounted for more than 10% of our consolidated revenues in these periods):

	Three Months Ended March 31, 2012		Three Months Ended March 31, 2011	
Con Edison	29.7	%	35.8	%
National Grid USA	15.3	%	18.9	%
National Grid dba Keyspan	10.1	%	15.3	%

The following table summarizes the percentage of consolidated gross trade accounts receivable by utility companies that equal or exceed 10% of our consolidated gross trade accounts receivable at March 31, 2012 and December 31, 2011:

	March 31, 2012		December 31, 2011	
Con Edison	33.3	%	33.8	%

National Grid USA	14.4	%	17.2	%
National Grid dba Keyspan	10.3	%	11.1	%

Investment in American Shale Oil, LLC

We account for our 50% ownership interest in AMSO, LLC using the equity method since we have the ability to exercise significant influence over its operating and financial matters, although we do not control AMSO, LLC. AMSO, LLC is a variable interest entity, however, we have determined that we are not the primary beneficiary.

AMSO has agreed to fund AMSO, LLC's expenditures as follows: 20% of the initial $50 million of expenditures, 35% of the next $50 million in approved expenditures and 50% of approved expenditures in excess of $100 million. AMSO has also agreed to fund 40% of the costs of the one-time payment for conversion of AMSO, LLC's research, development and demonstration lease to a commercial lease, in the event AMSO, LLC's application for conversion is approved. The remaining amounts are to be funded by Total S.A., or Total. Through December 31, 2011, AMSO was allocated 20% of the net loss of AMSO, LLC. AMSO's portion in the loss of AMSO, LLC increased in December 2011 from 20% to 35%, per our agreement with Total. AMSO's allocated share of the net loss of AMSO, LLC is included in "Equity in the net loss of AMSO, LLC" in the accompanying consolidated statements of operations.

In accordance with the agreement between the parties, AMSO was committed to a total investment of $10.0 million in AMSO, LLC, all of which, as of March 31, 2012, has been invested. AMSO remains obligated to fund its share of the expenditures it approves beyond the initial $10.0 million investment. AMSO's share of AMSO, LLC's budget for the year ending December 31, 2012 is $3.2 million. At March 31, 2012, AMSO had funded $1.0 million of its share of the 2012 budget. There are also a number of other situations where AMSO's funding obligation could increase further.

Total can increase AMSO's initial required funding commitment of $10.0 million up to an additional $8.75 million if Total notifies AMSO of its commitment to continue to fund the pilot test up to an agreed upon commitment level. To date, AMSO has not received such notification from Total. Additionally, even if AMSO were to withdraw its interest in AMSO, LLC, it will remain liable for its share of expenditures for safety and environmental preservation related to events occurring prior to its withdrawal.

Total may terminate its obligations to make capital contributions and withdraw as a member of AMSO, LLC. If Total withdraws as a member of AMSO, LLC, AMSO may also terminate its obligations to make capital contributions and withdraw as a member of AMSO, LLC. Although, subject to certain situations, AMSO and Total are not obligated to make additional contributions beyond their respective shares, they could dilute or forfeit their ownership interests in AMSO, LLC if they fail to contribute their respective shares for additional funding.

At March 31, 2012, our maximum exposure to additional loss as a result of our required investment in AMSO, LLC was $1.8 million, based on AMSO, LLC's 2012 budget. Our maximum exposure to additional loss could increase based on the situations described above. The maximum exposure at March 31, 2012 was determined as follows:

		(in millions)	
AMSO's total committed investment in AMSO, LLC	$	13.2	
Less: cumulative capital contributions to AMSO, LLC		(11.0	)
Less: liability for equity loss in AMSO, LLC at March 31, 2012		(0.4	)
Maximum exposure to additional loss	$	1.8	

Critical Accounting Policies

Our consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America, or U.S. GAAP. Our significant accounting policies are described in Note 1 to the consolidated financial statements included in our Registration Statement on Form 10, which includes our financial statements for the year ended July 31, 2011. The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses as well as the disclosure of contingent assets and liabilities. Critical accounting policies are those that require application of management's most subjective or complex judgments, often as a result of matters that are inherently uncertain and may change in subsequent periods. Our critical accounting policies include those related to the allowance for doubtful accounts, goodwill and income taxes. Management bases its estimates and judgments on historical experience and other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. For additional discussion of our critical accounting policies, see our Management's Discussion and Analysis of Financial Condition and Results of Operations in our Registration Statement on Form 10, as filed with the SEC.

Results of Operations

We evaluate the performance of our operating business segments based primarily on income (loss) from operations. Accordingly, the income and expense line items below income (loss) from operations are only included in our discussion of the consolidated results of operations.

Three Months Ended March 31, 2012 Compared to Three Months Ended March 31, 2011

IDT Energy Segment

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	Three months ended March 31, 2012	Three months ended March 31, 2011	Change $	Change %
		(in millions)		
Revenues:				
Electric	$ 31.7	$ 31.4	$ 0.3	1.1 %
Natural gas	25.8	32.0	(6.2)	(19.5)
Total revenues	57.5	63.4	(5.9)	(9.3)
Direct cost of revenues	39.5	46.3	(6.8)	(14.7)
Gross profit	18.0	17.1	0.9	5.1
Selling, general and administrative	10.6	7.2	3.4	45.9
Income from operations	$ 7.4	$ 9.9	$ (2.5)	(25.2)%

Revenues. IDT Energy’s electricity revenues increased in the three months ended March 31, 2012 compared to the same period in 2011 as a result of a significant increase in consumption, partially offset by a decrease in the average rate charged to customers. Electric consumption increased 44.5%, and the average electric rate charged to customers decreased 30.0%. The increase in electric consumption was the result of an increase in meters enrolled coupled with an increase in average consumption per meter. The decrease in the average electric rate charged to customers was primarily the result of a decrease in the underlying commodity cost.

IDT Energy's natural gas revenues decreased in the three months ended March 31, 2012 compared to the same period in 2011 primarily due to unusually warm weather in the three months ended March 31, 2012 which reduced the demand for natural gas for heat. As measured by heating degree days, a measure of outside air temperature designed to reflect the energy required for heating, New York State was 24% warmer in the three months ended March 31, 2012 than in the same period in 2011. The unseasonably warm weather contributed to decreases in both the per unit rate charged and in consumption per meter, which decreased 14.4% and 16.7%, respectively. The decline in demand for heat as well as increased domestic production of natural gas and relatively high storage gas inventories caused a decrease in the underlying natural gas cost, which allowed us to decrease the average natural gas rate charged to customers. The decline in the average natural gas rate charged to customers was also the result of discounted promotional rates for new customers. The decline in consumption was partially offset by an increase in meters served.

IDT Energy’s customer base as measured by meters enrolled consisted of the following:

	March 31, 2012	December 31, 2011	September 30, 2011	June 30, 2011	March 31, 2011
			(in thousands)		
Meters at end of quarter:					
Electricity customers	289	254	247	224	210
Natural gas customers	186	184	183	172	167
Total meters	475	438	430	396	377

Gross meter acquisitions in the three months ended March 31, 2012 were 108,000 compared to 49,000 in the same period in 2011. Net meters enrolled increased by 37,000 or 8.6% in the three months ended March 31, 2012, compared to an increase of 9,000 meters or 2.5% in the three months ended March 31, 2011, as gross meter acquisitions were partially offset by customer churn. Average monthly churn increased from 4.6% in the three months ended March 31, 2011 to 6.4% in the three months ended March 31, 2012 primarily because of the continued acceleration in customer acquisitions and increased competition in some key utility markets.

The average rates of annualized energy consumption, as measured by residential customer equivalents, or RCEs, are presented in the chart below. An RCE represents a natural gas customer with annual consumption of 100 mmbtu or an electricity customer with annual consumption of 10 MWh. Because different customers have different rates of energy consumption, RCEs are an industry standard metric for evaluating the consumption profile of a given retail customer base. The 23.9% RCE increase at March 31, 2012 compared to March 31, 2011 reflects primarily the increase in electric meters enrolled as well as, to a lesser degree, a shift in IDT Energy's electricity customer base to customers with higher consumption per meter. A significant portion of IDT Energy's incremental growth in RCEs was from recent expansion into electric-only utilities' territories, with higher electric consumption per meter than IDT Energy's legacy customer base. This increase was partially offset by decreases in natural gas RCEs due to consumption declines associated with the warmer than normal weather over the measurement period.

	March 31, 2012	December 31, 2011	September 30, 2011	June 30, 2011	March 31, 2011
			(in thousands)		
RCEs at end of quarter:					
Electricity customers	176	153	142	135	119
Natural gas customers	82	95	100	99	89
Total RCEs	258	248	242	234	208

Direct Cost of Revenues. IDT Energy's direct cost of revenues consisted of electricity cost of $20.2 million and $20.7 million in the three months ended March 31, 2012 and 2011, respectively, and the cost of natural gas of $19.3 million and $25.6 million in the three months ended March 31, 2012 and 2011, respectively. Direct cost of revenues for electricity decreased 2.8% in the three months ended March 31, 2012 compared to the same period in 2011 as the 32.7% decrease in the average unit cost was partially offset by an increase of 44.5% in consumption. Direct cost of revenues for natural gas decreased 24.3% in the three months ended March 31, 2012 compared to the same period in 2011 primarily due to the 19.5% decrease in the average unit cost as well as the 6.0% decrease in consumption.

IDT Energy's gross margins increased to 31.4% in the three months ended March 31, 2012 compared to 27.1% in the same period in 2011. Comprising these figures were gross margins on electricity sales of 36.5% in the three months ended March 31, 2012 compared to 34.0% in the same period in 2011 and gross margins on natural gas sales of 25.0% in the three months ended March 31, 2012 compared to 20.3% in the same period in 2011. Gross margins on both electricity and natural gas sales increased as the cost of the underlying commodity declined more sharply than the decrease in the average rate charged to customers. In both cases gross margin was helped by IDT Energy's ability to lag decreases in its average rate charged to customers as the cost of the commodity declined. IDT Energy's gross margins fluctuate with the commodity price environment and IDT Energy does not expect the current level to be sustainable in the long run.

Selling, General and Administrative. The increase in selling, general and administrative expenses in the three months ended March 31, 2012 compared to the same period in 2011 was primarily due to an increase in customer acquisition costs. These costs increased an aggregate of $2.7 million, representing 79.3% of the total increase in selling, general and administrative expenses. Customer acquisition costs increased primarily due to the significant increase in the number of new customers acquired as a result of the expansion into new territories. As a percentage of total IDT Energy revenues, selling, general and administrative expenses increased from 11.5% in the three months ended March 31, 2011 to 18.5% in the three months ended March 31, 2012 primarily because of the significant increase in costs related to customer acquisitions mentioned above coupled with the decline in revenues.

Genie Oil and Gas Segment

Genie Oil and Gas does not currently generate any revenues, nor does it incur any direct cost of revenues.

	Three months ended March 31, 2012	2011	Change $	%
		(in millions)		
General and administrative	$0.2	$0.1	$0.1	5.5 %
Research and development	2.1	2.3	(0.2)	(9.1)
Equity in the net loss of AMSO, LLC	0.8	0.7	0.1	25.4

Loss from operations	$(3.1)	$(3.1)	$—	(1.0)%

General and Administrative. General and administrative expenses in the three months ended March 31, 2012 increased slightly compared to the same period in 2011 as a result of increases in depreciation expense and stock-based compensation.

Research and Development. Research and development expenses in the three months ended March 31, 2012 and 2011 were related to the operations of IEI in Israel and our global exploration and technology development efforts. IEI completed its two-year resource appraisal study in 2011, the results of which support our expectations about the commercial potential of the oil shale in our Shfela basin license area. The findings from across the license area are consistent with previous estimates of oil equivalent in place within the Basin and indicate that the oil shale deposit is well suited for commercial development. Research and development expenses in the three months ended March 31, 2012 decreased compared to the same period in 2011 as the reduction in drilling activity in IEI was partially offset by an increase in other development efforts.

IEI made significant progress on the design and other preparatory work required for pilot plant construction, while continuing to work with regulatory authorities to obtain the permits required before pilot construction can begin. IEI believes that those permits will be issued during the current calendar year, and continues to plan for pilot test construction to begin next year if not delayed by permitting, regulatory action or pending litigation. The pilot test will provide a basis for determining the technical, environmental and economic viability of IEI's proposed process for extracting oil and gas from the oil shale resource. The basic design of the pilot plant has been completed, and detailed engineering work has begun. Pilot test operations could begin as early as 2013, barring additional delays related to permitting, regulatory action or pending litigation. We expect continued, significant increases in the expenses reflecting the costs of facility construction, drilling and operations of the IEI pilot test as well as further staffing to support engineering and scientific operations and business development activities. We expect IEI's pilot test to require approximately $25 million to $30 million over the next two to three years.

Equity in the Net Loss of AMSO, LLC. In the three months ended March 31, 2012, AMSO, LLC continued with late-stage preparations for its pilot test. The pilot test is intended to confirm the accuracy of several of the key underlying assumptions of AMSO, LLC's proposed in-situ heating and retorting process. In January 2012, AMSO, LLC initiated a fully integrated commissioning test of the above and below ground facilities to determine whether they were ready for pilot test operations. The test showed certain details to the facilities that must be corrected prior to proceeding with the pilot test and identified weaknesses in certain diagnostic equipment. Fixes to all identified issues are in progress, and we expect to be able to proceed with the pilot as early as June 2012. The equipment design and construction issues have no bearing on the underlying technology or ultimate success of the project. Rather, they are part of the normal process of research and development. Additional delays are possible before AMSO, LLC is able to operate its pilot test over a sustained period. Upon successful completion of the pilot test, AMSO, LLC expects to design and implement a larger scale demonstration project to further test its process and operations under commercial conditions, and assess scalability to commercial production levels. Upon completion of a successful demonstration, AMSO, LLC intends to submit an application to convert its research, development and demonstration lease into a commercial lease.

AMSO's equity in the net loss of AMSO, LLC increased in the three months ended March 31, 2012 compared to the same period in 2011 as a result of the increase beginning in December 2011 in AMSO's share of the loss of AMSO, LLC from 20% to 35%, in accordance with our agreement with Total, although AMSO, LLC's net loss decreased to $2.4 million in the three months ended March 31, 2012 from $3.3 million in the three months ended March 31, 2011. AMSO, LLC's net loss decreased as the costs associated with the pilot test facility construction were substantially completed prior to the current period.

Corporate

Corporate does not generate any revenues, nor does it incur any direct cost of revenues. Corporate costs include unallocated compensation, consulting fees, legal fees, business development expenses and other corporate-related general and administrative expenses.

	Three months ended March 31,		Change	
	2012	2011	$	%
	(in millions)			
General and administrative expenses and loss from operations	$1.6	$0.3	$1.3	516.5 %

The increase in general and administrative expenses in the three months ended March 31, 2012 as compared to the same period in 2011 was due primarily to increases in compensation, consulting fees and stock-based compensation.

We expect to incur quarterly incremental costs (including for services to be provided by IDT and others) of approximately $1.5 million, including stock-based compensation, for operating as a separate public company. We therefore expect our general and administrative expenses to increase compared to periods prior to the Spin-Off because of these additional costs.

Consolidated

Selling, General and Administrative. Up until the Spin-Off, IDT, our former parent company, charged us for certain transactions and allocated routine expenses based on company specific items. In addition, IDT controlled the flow of our treasury transactions. Following the Spin-off, IDT charges us for services it provides pursuant to the Transition Services Agreement. In the three months ended March 31, 2012 and 2011, IDT charged us $0.7 million and $0.6 million, respectively, which was included in “Selling, general and administrative” expense in the accompanying consolidated statements of operations.

On March 28, 2012, the Compensation Committee of our Board of Directors approved the grant of equity interests in certain of our subsidiaries to Howard Jonas, the Chairman of our Board of Directors. The Compensation Committee approved the following grants to Mr. Jonas: (1) deferred stock units for 50.56 shares of common stock of IDT Energy (representing 2.5% of the equity in IDT Energy on a fully diluted basis), (2) 0.25 ordinary shares of IEI (representing 0.25% of the equity in IEI on a fully diluted basis), (3) 3.05 ordinary shares of an early stage exploration venture in Israel, Genie Israel Oil & Gas, Ltd., or GIOG (representing 0.30% of the equity in GIOG on a fully diluted basis), and (4) shares representing 0.25% of our entity that will seek to develop oil shale opportunities in an Asian country, referred to as our Asian Venture.

In addition, the Compensation Committee approved grants of interests representing 1.13% of the equity in IDT Energy, 1.23% of the equity in IEI, 1.68% of the equity in GIOG and 1.00% in the Asian Venture to certain of our officers and employees.

We are in the process of estimating the fair value of the grants of these equity interests on the date of the grant, which is expected to be in the range of approximately $3.0 million to $3.7 million. The estimated fair value will be recognized as compensation cost on a straight-line basis over the vesting period. We did not recognize compensation cost related to these grants of equity interests in the three months ended March 31, 2012.

On November 3, 2011, we granted certain of our employees and directors 186 thousand restricted shares of our Class B common stock and 356 thousand options to purchase shares of our Class B common stock. In addition, on November 3, 2011, we granted nonemployee individuals that provide services to us, 52 thousand restricted shares of our Class B common stock and 52 thousand options to purchase shares of our Class B common stock. The restricted shares and options vest over the expected service period, subject to forfeiture based on service conditions. The options have a term of 10 years and an exercise price of $6.85 equal to the fair market value of the underlying shares on the grant date. The fair value of the restricted stock and options on the date of the grant was estimated at $1.6 million and $1.8 million, respectively, which will be recognized over the service period. The fair value of the options on the grant date was estimated using a Black-Scholes valuation model. In addition, in January or March 2012, each of the four non-employee members of our Board of Directors received 2,920 restricted shares of our Class B common stock, which vested immediately upon grant. The fair value of the restricted shares was determined based on the closing price of our Class B common stock on the date of grant. We recognized compensation cost related to the vesting of these shares and options of $0.4 million in the three months ended March 31, 2012, which is included in our "Selling, general and administrative" expense in the accompanying consolidated statements of operations.

As part of the Spin-Off, holders of restricted Class B common stock of IDT received, in respect of those restricted shares, one restricted share of our Class B common stock for every restricted share of IDT that they owned as of the record date for the Spin-Off. Such restricted shares of our Class B common stock are restricted under the same terms as the IDT restricted stock in respect of which they were issued. The restricted shares of our Class B common stock received in the Spin-Off are subject to forfeiture on the same terms, and their restrictions will lapse at the same time, as the corresponding IDT shares. The unrecognized compensation cost relating to our restricted shares at March 31, 2012 was $2.3 million, which is expected to be recognized over the remaining vesting period that ends in December 2013. We recognized compensation cost related to the vesting of these shares of $0.3 million and $0.2 million in the three months ended March 31, 2012 and 2011, respectively, which is included in our "Selling, general and administrative" expense in the accompanying consolidated statements of operations.

The following is a discussion of our consolidated income and expense line items below income from operations.

	Three months ended March 31,		Change	
	2012	2011	$	%
	(in millions)			
Income from operations	$2.7	$6.5	$(3.8)	(58.4)%
Interest expense and financing fees, net	(0.7)	(0.5)	(0.2)	(27.8)
Other (expense) income, net	—	0.2	(0.2)	(106.1)
Provision for income taxes	(0.8)	(3.8)	3.0	79.1
Net income	1.2	2.4	(1.2)	(49.5)
	(0.6)	0.3	(0.9)	nm

Net (income) loss attributable to noncontrolling interests				
Net income attributable to Genie	$0.6	$2.7	$(2.1)	(78.0)%

nm—not meaningful

Interest Expense and Financing Fees, net. The increase in interest expense and financing fees, net in the three months ended March 31, 2012 compared to the similar period in 2011 was primarily due to an increase in finance charges under the Preferred Supplier Agreement between IDT Energy and BP Energy Company and BP Corporation North America Inc. (collectively BP), pursuant to which BP is IDT Energy’s preferred provider of electricity and natural gas. The BP finance charges increased to $0.7 million in the three months ended March 31, 2012 compared to $0.6 million in the similar period in 2011.

Other (Expense) Income, net. Other (expense) income, net in the three months ended March 31, 2012 and 2011 consisted of foreign currency transaction (losses) gains of $(14) thousand and $0.2 million, respectively.

Provision for Income Taxes. The provision for income taxes in the three months ended March 31, 2012 decreased compared to the similar period in 2011 due primarily to the decrease in pre-tax income. Prior to the Spin-Off, we were included in the consolidated federal income tax return of IDT. Our income taxes are presented for periods prior to the Spin-Off on a separate tax return basis. In the three months ended March 31, 2011, IDT charged us $4.0 million for utilizing its net operating loss, which was included in “Provision for income taxes” in the accompanying consolidated statement of operations.

Net (Income) Loss Attributable to Noncontrolling Interests. The change in the net (income) loss attributable to noncontrolling interests in the three months ended March 31, 2012 compared to the similar period in 2011 primarily relates to 100% of the net income (loss) incurred by Citizen’s Choice Energy, LLC, or CCE, which is a variable interest entity that is consolidated in our IDT Energy segment. We do not have any ownership interest in CCE, therefore all net income or loss incurred by CCE has been attributed to noncontrolling interests. CCE’s net income in the three months ended March 31, 2012 was $1.0 million compared to net loss of $47 thousand in the three months ended March 31, 2011. CCE’s customer base and revenues had grown significantly by the three months ended March 31, 2012 compared to the similar period in 2011 when CCE commenced operations.

Liquidity and Capital Resources

General

Historically, we have satisfied our cash requirements primarily through a combination of our existing cash and cash equivalents, IDT Energy’s cash flow from operating activities, and operational funding from IDT. We currently expect that our operations in the next twelve months and the balance of cash, cash equivalents and restricted cash that we held as of March 31, 2012 of $101.9 million will be sufficient to meet our currently anticipated cash requirements for at least the twelve months ending March 31, 2013.

As of March 31, 2012, we had working capital (current assets less current liabilities) of $111.6 million.

The service agreements between IDT and us include additional services to be provided, on an interim basis, as a separate publicly-traded company. Such services include transitional services to be provided by IDT relating to human resources and employee benefits administration, finance, accounting, tax, internal audit, facilities, investor relations and legal services, as well as specified administrative services to be provided by us to certain of IDT’s foreign subsidiaries. Charges for these additional services were not included in our historical consolidated financial statements since they were not applicable for periods that we were not a separate public company. We estimate that the additional costs (including for services to be provided by IDT and others) related to being a publicly-traded company and being separated from IDT, will be approximately $1.5 million quarterly, including stock-based compensation.

IEI holds an exclusive Shale Oil Exploration and Production License awarded in July 2008 by the Israeli Ministry of National Infrastructures. Under the terms of the license, IEI is to conduct a geological appraisal study across the license area, characterize the resource and select a location for a pilot plant in which it will demonstrate its in-situ technology. Pilot test drilling and construction is expected to begin in 2013 if not delayed by permitting, regulatory action or pending litigation. Pilot test operations could begin as early as 2013. We expect to use the cash that we currently have to finance the pilot test construction and operations. In addition, we are considering financing IEI’s operations through sales of equity interests in IEI. Finally, we may finance our operations through sales of equity interests in GOGAS or the Company. We expect IEI’s pilot test to require investments of approximately $25 million to $30 million over the next two to three years.

	Three months ended March 31, 2012		2011
	(in millions)		
Cash flows provided by (used in):			
Operating activities	$ 1.5		$ 1.8
Investing activities	(0.6)		(1.3)
Financing activities	(1.3)		3.2
(Decrease) increase in cash and cash equivalents	$ (0.4)		$ 3.7

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Operating Activities

Our cash flow from operations varies significantly from quarter to quarter and from year to year, depending on our operating results and the timing of operating cash receipts and payments, specifically trade accounts receivable and trade accounts payable, including payments relating to IEI's research and development activities.

CCE and DAD Sales, LLC, or DAD, are consolidated variable interest entities. Tari Corporation, or Tari, is the sole owner of both CCE and DAD. We determined that we have the power to direct the activities of CCE and DAD that most significantly impact their economic performance, and we have the obligation to absorb losses of CCE and DAD that could potentially be significant to CCE and DAD on a stand-alone basis. We therefore determined that we are the primary beneficiary of both CCE and DAD, and as a result, we consolidate CCE and DAD with our IDT Energy segment. We provided CCE and DAD with all of the cash required to fund their operations. In the three months ended March 31, 2012 and 2011, we provided CCE and DAD with net funding of $0.1 million and nil, respectively, in order to finance their operations. In April 2012, IDT Energy and CCE entered into an Asset Purchase Agreement pursuant to which IDT Energy shall, upon the satisfaction of many conditions, acquire all of CCE's customer accounts, accounts receivable, trade names and other customer-related assets in exchange for the discharge and release of CCE's debt and payment obligations to IDT Energy. The closing conditions include customary conditions as well as the discharge or satisfactory resolution of certain claims pending against CCE, and IDT Energy is under no obligation to assume any liability related thereto. At March 31, 2012, the amount of CCE debt to be discharged was $4.8 million. In addition, in April 2012, IDT Energy entered into a Consulting Agreement with Tari for customer networking services and other sales related services. Finally, in April 2012, IDT Energy and DAD entered into a Client Agreement whereby DAD will use its network of door-to-door sales agents to obtain customers for IDT Energy in exchange for cash commissions.

We are subject to audits in various jurisdictions for various taxes, including income tax and utility excise tax. Specifically, IDT Energy has the following audits in process: (1) New York State income tax for fiscal 2007, fiscal 2008 and fiscal 2009, (2) New York City utility tax audit on electricity sales for the period from June 1, 2007 through December 31, 2008, and (3) New York State sales and use tax for the period from June 2003 though August 2009. In June 2011, IDT Energy received a Notice of Proposed Tax Adjustments from the New York City Finance Department related to the utility tax audit that included aggregate assessments of tax, interest and penalties of $7.2 million. In addition, IDT Energy's potential exposure for utility tax, interest and penalties for the period from January 1, 2009 through March 31, 2012 is an additional $8.5 million. As of March 31, 2012, we have accrued $4.4 million for the New York City utility tax audit, $2.6 million related to New York State income tax audit and $0.8 million for the New York State sales and use tax audit. We believe that our reasonably possible liability related to the New York City utility tax audit, above the amount that has been accrued, range from nil to $5.9 million. We believe that our reasonably possible exposure related to the New York State income tax audit, above the amount that has been accrued, range from nil to $4.2 million. We belive that our reasonably possible liability related to the New York State sales and use tax audit, above the amount that has been accrued, range from nil to $1.1 million. At March 31, 2012, we have accrued for the estimated loss from these audits for which it is probable that a liability has been incurred, however amounts asserted by taxing authorities or the amount ultimately assessed against us could be greater than the accrued amounts. Accordingly, additional provisions may be recorded in the future as revised estimates are made or underlying matters are settled or resolved. Imposition of assessments as a result of tax audits could have an adverse effect on our results of operations, cash flows and financial condition.

We are no longer eligible to utilize IDT's net operating loss to offset our taxable income for periods following the Spin-Off and, as a result, will have to pay our federal income taxes to the U.S. Treasury instead of to IDT.

Investing Activities

Our capital expenditures were $12 thousand in the three months ended March 31, 2012 compared to $3 thousand in the three months ended March 31, 2011. We currently anticipate that our total capital expenditures for the twelve months ending March 31, 2013 will be approximately $0.2 million. We did not have any material commitments for capital expenditures at March 31, 2012.

In the three months ended March 31, 2012 and 2011, cash used for capital contributions to AMSO, LLC was $1.1 million and $1.4 million, respectively. Costs for research and development activities in IEI and AMSO, LLC are charged to expense when incurred.

Restricted cash and cash equivalents decreased $0.5 million and $0.1 million in the three months ended March 31, 2012 and 2011, respectively.

In June 2009, IDT Energy entered into a Preferred Supplier Agreement with BP, pursuant to which BP is IDT Energy's preferred provider of electricity and natural gas. IDT Energy's obligations to BP are secured by a first security interest in deposits or receivables from utilities in connection with their purchase of IDT Energy's customer receivables, and in any cash deposits or letters of credit posted in connection with any collateral accounts with BP. IDT Energy's ability to purchase electricity and natural gas under this agreement is subject to satisfaction of certain conditions including the maintenance of certain covenants. We are in compliance with such covenants. As of March 31, 2012, cash and cash equivalents of $0.5 million and trade accounts receivable of $27.2 million were pledged to BP as collateral for the payment of IDT Energy's trade accounts payable to BP of $8.5 million as of March 31, 2012.

Financing Activities

On January 5, 2012, we paid a cash dividend of $0.05 per share on our Class A common stock and Class B common stock. The aggregate dividends paid were $1.1 million. On April 3, 2012, we paid a cash dividend of $0.033 per share to shareholders of record at the close of business on March, 26, 2012 of our Class A common stock and Class B common stock. The dividend paid on April 3, 2012 was for the two-month period of November and December 2011 that represents the period between the end of our prior fiscal quarter and the beginning of the new fiscal quarter in connection with the change in our fiscal year to a calendar year, and represents a pro-rated dividend of 2/3rd of the normal quarterly dividend. The aggregate dividend paid was $0.8 million. We will pay an ordinary dividend of $0.05 per share on May 30, 2012 to stockholders of our Class A and Class B common stock as of the record date of May 21, 2012. We currently intend to continue to pay a quarterly dividend of $0.05 per share on our Class A common stock and Class B common stock, subject to the approval of our Board of Directors.

On December 8, 2011, our Board of Directors approved a stock repurchase program for the repurchase of up to an aggregate of 20 million shares of our Class B common stock for up to an aggregate of $20 million. At March 31, 2012, no repurchases have been made and 20 million shares remained available for repurchase under the stock repurchase program.

Up until the Spin-Off, IDT, our former parent company, provided us with the cash required to fund our working capital requirements and our investments in our Genie Oil and Gas segment, when necessary. We used any excess cash provided by IDT Energy's operations to repay IDT. In the three months ended March 31, 2011, expenses paid by IDT on our behalf and net cash transfers received from IDT were an aggregate of $3.2 million.

We received proceeds from the exercise of our stock options of $5 thousand in the three months ended March 31, 2012.

In the three months ended March 31, 2012, we paid $0.1 million to repurchase 16,593 shares of our Class B common stock that were tendered by employees of ours to satisfy the employees' tax withholding obligations in connection with the lapsing of restrictions on awards of restricted stock. Such shares are repurchased by us based on their fair market value on the trading day immediately prior to the vesting date.

As of April 23, 2012, we and IDT Energy entered into a Loan Agreement with JPMorgan Chase Bank for a revolving line of credit for up to a maximum principal amount of $25.0 million. The proceeds from the line of credit may be used to provide working capital and for the issuance of letters of credit. We agreed to deposit cash in a money market account at JPMorgan Chase Bank as collateral for the line of credit equal to the greater of (a) $10.0 million or (b) the sum of the amount of letters of credit outstanding plus the outstanding principal under the revolving note. We are not permitted to withdraw funds or exercise any authority over the required balance in the collateral account. The principal outstanding will bear interest at the lesser of (a) the LIBOR rate multiplied by the statutory reserve rate established by the Board of Governors of the Federal Reserve System plus 1.0% per annum, or (b) the maximum rate per annum permitted by whichever of applicable federal or Texas laws permit the higher interest rate. Interest is payable at least every three months and all outstanding principal and any accrued and unpaid interest is due on the maturity date of April 30, 2013. We paid a facility fee of $37,500 and will pay a quarterly unused commitment fee of 0.08% per annum commencing on July 15, 2012 on the difference between $25.0 million and the average daily outstanding principal balance of the note. In addition, as of April 23, 2012, GEIC issued a Corporate Guaranty to JPMorgan Chase Bank whereby GEIC unconditionally guarantees the full payment of all indebtedness of ours and IDT Energy under the Loan Agreement.

Changes in Trade Accounts Receivable and Inventory

Gross trade accounts receivable increased to $27.6 million at March 31, 2012 from $24.1 million at December 31, 2011 reflecting the seasonal increase in our revenues.

Inventory of natural gas decreased to $1.0 million at March 31, 2012 from $4.1 million at December 31, 2011 primarily due to the sales of natural gas during the winter heating season.

Contractual Obligations

The following table quantifies our future contractual obligations as of March 31, 2012:

Payments Due by Period

(in millions)	Total	Less than 1 year	1—3 years	4—5 years	After 5 years
Commitment to invest in AMSO, LLC (1)	$ 2.2	$ 2.2	$ —	$ —	$ —
IDT Energy's forward contracts	0.1	0.1	—	—	—
Purchase and other obligations	0.2	0.2	—	—	—
Operating leases	0.4	0.2	0.2	—	—
TOTAL CONTRACTUAL OBLIGATIONS (2)	$ 2.9	$ 2.7	$ 0.2	$ —	$ —

(1) AMSO's total committed investment in AMSO, LLC is subject to certain situations where the amounts could be greater. The timing of AMSO's payments is based on the current budget and other projections and is subject to change.

(2) The above table does not include our unrecognized income tax benefits for uncertain tax positions at March 31, 2012 of $2.6 million due to the uncertainty of the amount and/or timing of any such payments. Uncertain tax positions taken or expected to be taken on an income tax return may result in additional payments to tax authorities. We are not currently able to reasonably estimate the timing of any potential future payments. If a tax authority agrees with the tax position taken or expected to be taken or the applicable statute of limitations expires, then additional payments will not be necessary.

Off-Balance Sheet Arrangements

We do not have any “off-balance sheet arrangements,” as defined in relevant SEC regulations that are reasonably likely to have a current or future effect on our financial condition, results of operations, liquidity, capital expenditures or capital resources, other than the following.

IDT Energy has performance bonds issued through an insurance company for the benefit of various states in order to comply with the states’ financial requirements for retail energy providers. At March 31, 2012, IDT Energy had aggregate performance bonds of $0.8 million outstanding.

In connection with our Spin-Off in October 2011, we and IDT entered into various agreements prior to the Spin-Off including a Separation and Distribution Agreement to effect the separation and provide a framework for our relationship with IDT after the Spin-Off, and a Tax Separation Agreement, which sets forth the responsibilities of us and IDT with respect to, among other things, liabilities for federal, state, local and foreign taxes for periods before and including the Spin-Off, the preparation and filing of tax returns for such periods and disputes with taxing authorities regarding taxes for such periods. Pursuant to Separation and Distribution Agreement, among other things, we indemnify IDT and IDT indemnifies us for losses related to the failure of the other to pay, perform or otherwise discharge, any of the liabilities and obligations set forth in the agreement. Pursuant to the Tax Separation Agreement, among other things, IDT indemnifies us from all liability for taxes of IDT with respect to any taxable period, and we indemnify IDT from all liability for taxes of ours with respect to any taxable period, including, without limitation, the ongoing tax audits related to our business.

Recently Issued Accounting Standards Not Yet Adopted

On January 1, 2012, we adopted the accounting standard update to achieve common fair value measurement and disclosure requirements in U.S. GAAP and International Financial Reporting Standards, or IFRS. The amendments in this update (1) clarify the application of certain existing fair value measurement and disclosure requirements and (2) change certain principles or requirements for measuring fair value or disclosing information about fair value measurements. The adoption of these amendments did not impact our financial position, results of operations or cash flows.

Also on January 1, 2012, we adopted the accounting standard update to simplify how an entity tests goodwill for impairment. The amendments in the update allow an entity to first assess qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity will no longer be required to calculate the fair value of a reporting unit (Step 1) unless the entity determines, based on a qualitative assessment, that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. The adoption of these amendments did not impact our financial position, results of operations or cash flows.

In December 2011, an accounting standard update was issued to enhance disclosures and provide converged disclosures in U.S. GAAP and IFRS about financial instruments and derivative instruments that are either offset on the statement of financial position or subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are offset on the statement of financial position. Entities will be required to provide both net and gross information for those assets and liabilities in order to enhance comparability between entities that prepare their financial statements on the basis of U.S. GAAP and entities that prepare their financial statements on the basis of IFRS. We are required to adopt this standard update on January 1, 2013. We are evaluating the impact that this standard update will have on our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risks

Our primary market risk exposure is the price applicable to our natural gas and electricity purchases and sales. The sales price of our natural gas and electricity is primarily driven by the prevailing market price. Hypothetically, if our gross profit per unit in the three months ended March 31, 2012 had remained the same as in the three months ended March 31, 2011, our gross profit from electricity sales would have increased by $3.8 million in the three months ended March 31, 2012 and our gross profit from natural gas sales would have decreased by $0.3 million in that period.

The energy markets have historically been very volatile, and we can reasonably expect that electricity and natural gas prices will be subject to fluctuations in the future. In an effort to reduce the effects of the volatility of the price of electricity and natural gas on our operations, we have adopted a policy of hedging electricity and natural gas prices from time to time, at relatively lower volumes, primarily through the use of forward contracts and put and call options. While the use of these hedging arrangements limits the downside risk of adverse price movements, it also limits future gains from favorable movements. We do not apply hedge accounting to these contracts and options, therefore the mark-to-market change in fair value is recognized in direct cost of revenue in our consolidated statements of operations.

The summarized volume of IDT Energy’s outstanding electricity call options as of March 31, 2012 was as follows:

Commodity	Settlement Dates	Volume
Electricity	From May 2012 to August 2012	139,200 MWh

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Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures. Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended), as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of March 31, 2012.

Changes in Internal Control over Financial Reporting. There were no changes in our internal control over financial reporting during the quarter ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Legal proceedings in which we are involved are more fully described in Note 9 to the Consolidated Financial Statements included in Item 1 to Part I of this Quarterly Report on Form 10-Q.

Item 1A. Risk Factors

There are no material changes from the risk factors previously disclosed in our Registration Statement on Form 10 that became effective on October 25, 2011, other than the following:

We could be harmed by network disruptions, security breaches, or other significant disruptions or failures of our IT infrastructure and related systems.

To be successful, we need to continue to have available a high capacity, reliable and secure network. We face the risk, as does any company, of a security breach, whether through cyber attack, malware, computer viruses, sabotage, or other significant disruption of our IT infrastructure and related systems. We face a risk of a security breach or disruption from unauthorized access to our proprietary or classified information on our systems. Certain of our personnel operate in jurisdictions that could be a target for cyber-attacks. The secure maintenance and transmission of our information is a critical element of our operations. Our information technology and other systems that maintain and transmit our information, or those of service providers or business partners, may be compromised by a malicious third party penetration of our network security, or that of a third party service provider or business partner, or impacted by advertent or inadvertent actions or inactions by our employees, or those of a third party service provider or business partner. As a result, our information may be lost, disclosed, accessed or taken without our consent.

Although we make significant efforts to maintain the security and integrity of these types of information and systems, there can be no assurance that our security efforts and measures will be effective or that attempted security breaches or disruptions would not be successful or damaging, especially in light of the growing sophistication of cyber attacks and intrusions. We may be unable to anticipate all potential types of attacks or intrusions or to implement adequate security barriers or other preventative measures.

Network disruptions, security breaches and other significant failures of the above-described systems could (i) disrupt the proper functioning of these networks and systems and therefore our operations; (ii) result in the unauthorized access to, and destruction, loss, theft, misappropriation or release of our proprietary, confidential, sensitive or otherwise valuable information, including trade secrets, which others could use to compete against us or for disruptive, destructive or otherwise harmful purposes and outcomes; (iii) require significant management attention or financial resources to remedy the damages that result or to change our systems; or (iv) result in a loss of business, damage our reputation or expose us to litigation. Any or all of which could have a negative impact on our results of operations, financial condition and cash flows.

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

The following table provides information with respect to purchases by us of our shares during the first quarter of 2012:

	Total Number of Shares Purchased	Average Price per Share	Total Number of Shares Purchased as part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs (1)
January 1–31, 2012 (2)	16,593	$8.04	—	20,000,000
February 1–29, 2012	—	$—	—	20,000,000
March 1–31, 2012	—	$—	—	20,000,000
Total	16,593	$8.04	—	

(1) Under our existing stock repurchase program, approved by our Board of Directors on December 8, 2011, we are authorized to repurchase up to an aggregate of 20 million shares of our Class B common stock.

(2) Consists of 16,593 shares of Class B common stock that were tendered by employees of ours to satisfy the employees' tax withholding obligations in connection with the lapsing of restrictions on awards of restricted stock. Such shares are repurchased by us based on their fair market value on the trading day immediately prior to the vesting date.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

Item 6. Exhibits

Exhibit Number	Description
31.1*	Certification of Chief Executive Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer pursuant to 17 CFR 240.13a-14(a), as adopted pursuant to §302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to §906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document
101.SCH*	XBRL Taxonomy Extension Schema Document
101.CAL*	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Linkbase Document.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.

* Filed herewith.

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SIGNATURES

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

Genie Energy Ltd.

May 15, 2012 By: /s/ Claude Pupkin
Claude Pupkin
Chief Executive Officer

May 15, 2012 By: /s/ Avi Goldin
Avi Goldin
Chief Financial Officer

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