

**DYADIC INTERNATIONAL, INC.**

A Delaware Corporation

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SIC Code: 2836

Federal EIN: 45-0486747

**Issuer's Quarterly Report**

**For the three and nine months ended September 30, 2016**

**ISSUER'S EQUITY SECURITIES**

**COMMON STOCK**

\$0.001 Par Value Per Share

100,000,000 Shares Authorized

38,808,724 Shares Issued as of September 30, 2016

34,460,620 Shares Outstanding as of September 30, 2016

**OTCQX: DYAI**

**Dyadic International, Inc. is responsible for the content of this Quarterly Report. The securities described in this document are not registered with, and the information contained in this Quarterly Report has not been filed with, or approved by, the U.S. Securities and Exchange Commission.**

All references to "the Company," "the Issuer," "Dyadic," "we," "us" or "our" refers to Dyadic International, Inc. and its consolidated subsidiaries, unless the context otherwise indicates.

## **TABLE OF CONTENTS**

Item 1	<a href="#"><u>The Exact Name of the issuer and the address and telephone number of the issuer's principal executive offices</u></a>	<a href="#"><u>3</u></a>
Item 2	<a href="#"><u>Shares Outstanding</u></a>	<a href="#"><u>4</u></a>
Item 3	<a href="#"><u>Unaudited Interim Consolidated Financial Statements:</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Consolidated Balance Sheets as of September 30, 2016 (unaudited) and December 31, 2015</u></a>	<a href="#"><u>5</u></a>
	<a href="#"><u>Consolidated Statements of Operations for the three and nine months ended September 30, 2016 and 2015 (unaudited)</u></a>	<a href="#"><u>6</u></a>
	<a href="#"><u>Consolidated Statement of Stockholders' Equity and Comprehensive Loss for the nine months ended September 30, 2016 (unaudited)</u></a>	<a href="#"><u>7</u></a>
	<a href="#"><u>Consolidated Statements of Cash Flows for the nine months ended September 30, 2016 and 2015 (unaudited)</u></a>	<a href="#"><u>8</u></a>
	<a href="#"><u>Notes to the Consolidated Financial Statements (unaudited)</u></a>	<a href="#"><u>8</u></a>
Item 4	<a href="#"><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></a>	<a href="#"><u>22</u></a>
Item 5	<a href="#"><u>Legal Proceedings</u></a>	<a href="#"><u>28</u></a>
Item 6	<a href="#"><u>Defaults Upon Senior Securities</u></a>	<a href="#"><u>28</u></a>
Item 7	<a href="#"><u>Other Information</u></a>	<a href="#"><u>29</u></a>
Item 8	<a href="#"><u>Exhibits</u></a>	<a href="#"><u>30</u></a>
Item 9	<a href="#"><u>Certifications</u></a>	<a href="#"><u>31</u></a>

## Special Cautionary Note Regarding Forward-Looking Statements

Information (other than historical facts) set forth in this Quarterly Report contains forward-looking statements within the meaning of the Federal Securities Laws, which involve a number of risks and uncertainties that could cause our actual results to differ materially from those reflected in the forward-looking statements. Forward-looking statements generally can be identified by use of the words “expect,” “should,” “intend,” “anticipate,” “will,” “project,” “may,” “might,” “potential” or “continue” and other similar terms or variations of them or similar terminology. Dyadic International, Inc., and its subsidiaries cautions readers that any forward-looking information is not a guarantee of future performance and that actual results could differ materially from those contained in the forward-looking information. Such statements reflect the current views of our management with respect to our operations, results of operations and future financial performance. Forward-looking statements involve a number of risks, uncertainties or other factors within and/or beyond Dyadic’s control. These factors include, but are not limited to, (1) general economic, political and market conditions; (2) our ability to carry out and implement our biopharmaceutical research and business plans and strategic initiatives; (3) our ability to retain and attract employees, consultants, directors and advisors; (4) our ability to implement and successfully carry out Dyadic’s and third parties research and development efforts; (5) our ability to obtain new license and research agreements; (6) our ability to maintain our existing access to, and/or expand access to third party contract research organizations in order to carry out our research projects for ourselves and third parties; (7) competitive pressures and reliance on key customers and collaborators; (8) the outcome of the current litigation by Dyadic against its former counsel, as well as our reliance on qualified employees and professionals, including scientific, accounting and business personnel, economic, political and market conditions and price fluctuations, government and industry regulation, U.S. and global competition, upgrade financial staffing, implement and monitor internal controls, and comply with financial reporting requirements, and other factors. We caution you that the foregoing list of important factors is not exclusive. The forward-looking statements are based on our beliefs, assumptions and expectations of future performance, taking into account the information currently available to us. These statements are only predictions based upon our current expectations and projections about future events. There are important factors that could cause our actual results, level of activity, performance or achievements to differ materially from the results, level of activity, performance or achievements expressed or implied by the forward-looking statements. Moreover, we operate in a highly regulated, competitive and rapidly changing environment. Our competitors have far greater resources, infrastructure and market presence than we do which makes it difficult for us to enter certain markets, and/or to gain or maintain customers. New risks emerge from time to time and it is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. Before investing in our common stock, investors should carefully read the information set forth under the caption “Risk Factors” described in this Quarterly Report for the three and nine months ended September 30, 2016 and our December 31, 2015 Annual Report filed with the OTC Markets on March 29, 2016.

You should not rely upon forward-looking statements as predictions of future events. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee that the future results, levels of activity, performance and events and circumstances reflected in the forward-looking statements will be achieved or occur. Except as required by law, we undertake no obligation to publicly update any forward-looking statements for any reason after the date of this Quarterly Report to conform these statements to actual results or to changes in our expectations.

We qualify all of our forward-looking statements by these cautionary statements. In addition, with respect to all of our forward-looking statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

### ***Item 1 The exact name of the issuer and the address and telephone number of the issuer’s principal executive offices.***

The name of the issuer is Dyadic International, Inc. The address and telephone number of the issuer’s principal executive office is as follows:

The address of the issuer is: 140 Intracoastal Pointe Drive, Suite 404  
Jupiter, Florida 33477

The telephone and facsimile is: Telephone: (561) 743-8333  
Facsimile: (561) 743-8343

The issuer's website: Dyadic's corporate website, [www.dyadic.com](http://www.dyadic.com), contains general information about us and our products and services. We also maintain [www.dyadic.nl](http://www.dyadic.nl). The information contained on or accessible from such websites shall not be deemed incorporated by reference herein.

Investor relations contact: Thomas L. Dubinski  
Chief Financial Officer  
140 Intracoastal Pointe Drive, Suite 404  
Jupiter, Florida 33477  
Telephone: (561) 743-8333  
Facsimile: (561) 743-8343  
Email: [tdubinski@dyadic.com](mailto:tdubinski@dyadic.com)

***Item 2 Shares outstanding***

As of September 30, 2016, Dyadic had two classes of capital stock authorized, common stock and preferred stock. Our common stock is traded on the OTCQX U.S. Premier, a tier of the OTC marketplace. There were no shares of preferred stock outstanding as of the end of each reported period. The trading symbol for Dyadic's common stock assigned by the Financial Industry Regulatory Authority, Inc. is "DYAI."

The CUSIP number for our common stock is 26745T-10-1.

None of Dyadic's common stock has been registered under the Securities Act of 1933, as amended (the "Securities Act") or qualified under any state securities laws, although we are continuing to explore when, if, and under what circumstances to register or qualify one, or both classes of our securities. Certain shares of our common stock are currently eligible for resale in the public market pursuant to the exemption from registration offered by Rule 144 under the Securities Act ("Rule 144"). The remaining outstanding shares of our common stock are "restricted securities" within the meaning of Rule 144, and may be eligible for resale in the future.

**Common Stock**

Dyadic's common stock has a par value of \$0.001 per share. The following table shows our common stock share ownership as of September 30, 2016:

(i)	Number of shares authorized	100,000,000
(ii)	Number of shares issued	38,808,724
(iii)	Number of shares outstanding	34,460,620
(iv)	Number of shares held in treasury	4,348,104
(v)	Number of shares freely tradable	19,948,098
(vi)	Total number of holders of record	50

There are greater than 1,602 beneficial shareholders owning at least 100 shares of the Company's common stock.

**Preferred Stock**

Dyadic's preferred stock has a par value of \$0.0001 per share. The following table shows our preferred stock share ownership as of September 30, 2016:

(i)	Number of shares authorized	5,000,000
(ii)	Number of shares outstanding	—
(iii)	Number of shares freely tradable	—
(iv)	Total number of holders of record	—

*Item 3 Unaudited interim consolidated financial statements*

**Financial Statements**

**DYADIC INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED BALANCE SHEETS**

	<b>September 30, 2016</b>	<b>December 31, 2015</b>
	(Unaudited)	(Audited)
<b>ASSETS</b>		
Current Assets:		
Cash and Cash Equivalents	\$ 5,827,998	\$ 68,601,138
Short-term Investment Securities	44,112,658	—
Accounts Receivable, Net	10,177	78,952
Prepaid Expenses and Other Current Assets	454,763	490,750
<b>Total Current Assets</b>	<b>50,405,596</b>	<b>69,170,840</b>
Long-term Investment Securities	5,961,723	—
Escrowed Funds from Sale of Assets	7,363,977	7,361,182
Other Assets	118,789	135,403
<b>Total Assets</b>	<b>\$ 63,850,085</b>	<b>\$ 76,667,425</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Accounts Payable	\$ 137,935	\$ 630,230
Accrued Expenses	421,650	2,113,672
Deferred Research and Development Obligation	36,422	129,018
<b>Total Liabilities</b>	<b>596,007</b>	<b>2,872,920</b>
Stockholders' Equity:		
Preferred Stock, \$.0001 Par Value:		
Authorized Shares - 5,000,000; None Issued and Outstanding	—	—
Common Stock, \$.001 Par Value:		
Authorized Shares - 100,000,000; Issued and Outstanding - 38,808,724 and 34,460,620, respectively, as of September 30, 2016; and 40,298,324 and 40,298,324, respectively, as of December 31, 2015	38,809	40,299
Additional Paid-In Capital	90,263,272	92,157,374
Treasury Stock, Shares Held at Cost - 4,348,104 and 0, respectively	(6,788,353)	—
Stock Subscriptions Receivable	—	(40,625)
Stock to be Issued	—	350,553
Accumulated Deficit	(20,259,650)	(18,713,096)
<b>Total Stockholders' Equity</b>	<b>63,254,078</b>	<b>73,794,505</b>
<b>Total Liabilities and Stockholder's Equity</b>	<b>\$ 63,850,085</b>	<b>\$ 76,667,425</b>

The Accompanying Notes are an Integral Part of these Unaudited Consolidated Financial Statements

**DYADIC INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

	<b>Three Months Ended September 30,</b>		<b>Nine Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
<b>REVENUES:</b>				
Research and Development Revenue	\$ —	\$ 213,485	\$ 101,836	\$ 285,721
<b>COSTS AND EXPENSES (INCOME):</b>				
Costs of Goods Sold	—	34,993	98,822	92,145
General and Administrative	939,195	1,000,641	2,923,127	3,217,837
Research and Development	369,359	—	963,673	—
Foreign Currency Transaction (Gain) Loss, Net	(46,897)	(23,136)	(78,568)	105,521
Total Expenses	1,261,657	1,012,498	3,907,054	3,415,503
<b>LOSS FROM CONTINUING OPERATIONS BEFORE OTHER INCOME (EXPENSE)</b>	<b>(1,261,657)</b>	<b>(799,013)</b>	<b>(3,805,218)</b>	<b>(3,129,782)</b>
<b>Other Income (Expense):</b>				
Settlement of Litigation, Net	—	2,170,000	2,100,000	2,170,000
Interest Income	146,930	2,638	344,012	8,725
Interest Expense	—	—	(909)	—
Total Other Income	146,930	2,172,638	2,443,103	2,178,725
<b>INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES</b>	<b>(1,114,727)</b>	<b>1,373,625</b>	<b>(1,362,115)</b>	<b>(951,057)</b>
Income Tax Expense from Continuing Operations	(50,694)	—	(184,439)	—
<b>NET INCOME (LOSS) FROM CONTINUING OPERATIONS</b>	<b>(1,165,421)</b>	<b>1,373,625</b>	<b>(1,546,554)</b>	<b>(951,057)</b>
<b>NET INCOME FROM DISCONTINUED OPERATIONS, NET OF TAXES</b>	<b>—</b>	<b>536,601</b>	<b>—</b>	<b>2,057,410</b>
<b>NET INCOME (LOSS)</b>	<b>\$ (1,165,421)</b>	<b>\$ 1,910,226</b>	<b>\$ (1,546,554)</b>	<b>\$ 1,106,353</b>
<b>BASIC NET INCOME (LOSS) PER SHARE:</b>				
Basic Net Income (Loss) from Continuing Operations per Share	\$ (0.03)	\$ 0.04	\$ (0.04)	\$ (0.02)
Basic Net Income from Discontinued Operations per Share	—	0.02	—	0.05
Basic Net Income (Loss) per Share	<u>\$ (0.03)</u>	<u>\$ 0.06</u>	<u>\$ (0.04)</u>	<u>\$ 0.03</u>
<b>DILUTED NET INCOME (LOSS) PER SHARE:</b>				
Diluted Net Income (Loss) from Continuing Operations per Share	\$ (0.03)	\$ 0.04	\$ (0.04)	\$ (0.02)
Diluted Net Income from Discontinued Operations per Share	—	0.02	—	0.05
Diluted Net Income (Loss) per Share	<u>\$ (0.03)</u>	<u>\$ 0.06</u>	<u>\$ (0.04)</u>	<u>\$ 0.03</u>
<b>Weighted-Average Number of Shares:</b>				
Basic	36,185,164	34,247,456	37,514,315	34,219,493
Diluted	36,185,164	34,418,151	37,514,315	34,410,770

The Accompanying Notes are an Integral Part of these Unaudited Consolidated Financial Statements

**DYADIC INTERNATIONAL, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE LOSS**  
**(Unaudited)**

	<u>Common Stock</u>		<u>Treasury Stock</u>		<u>Additional Paid-In Capital</u>	<u>Stock Subscriptions</u>	<u>Stock to Be Issued</u>	<u>Accumulated Deficit</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>	<u>Shares</u>	<u>Amount</u>					
Balance at December 31, 2015	40,298,324	\$ 40,299	—	\$ —	\$ 92,157,374	\$ (40,625)	\$ 350,553	\$ (18,713,096)	\$ 73,794,505
Stock-based Compensation	96,774	97			538,374				538,471
Vesting of Restricted Stock	219,776	219			349,959		(350,178)		—
Exercise of Warrants	2,500	3			372		(375)		—
Exercise of Stock Options	263,586	263			(263)				—
Sale of Common Stock	64,516	65			99,935				100,000
Repayment of Stock Subscriptions						40,625			40,625
Purchases of Common Stock	(2,136,752)	(2,137)	(4,348,104)	(6,788,353)	(2,882,479)				(9,672,969)
Net Loss and Other Comprehensive Loss								(1,546,554)	(1,546,554)
Balance at September 30, 2016	<u>38,808,724</u>	<u>\$ 38,809</u>	<u>(4,348,104)</u>	<u>\$(6,788,353)</u>	<u>\$ 90,263,272</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$(20,259,650)</u>	<u>\$ 63,254,078</u>

The Accompanying Notes are an Integral Part of these Unaudited Consolidated Financial Statements

**DYADIC INTERNATIONAL, INC. AND SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

	<b>Nine Months Ended September 30,</b>	
	<b>2016</b>	<b>2015</b>
	(Unaudited)	(Unaudited)
<b>OPERATING ACTIVITIES</b>		
Net loss from continuing operations	\$ (1,546,554)	\$ (951,057)
Net income from discontinued operations, net of income tax expense	—	2,057,410
Net income (loss)	(1,546,554)	1,106,353
Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities		
Amortization of premium on held-to-maturity securities	613,052	—
Premium on held-to-maturity securities	(1,985,433)	—
Stock based compensation expense	538,471	365,819
Foreign currency transaction loss	(14,689)	—
Changes in operating assets and liabilities:		
Accounts receivable	64,164	—
Prepaid expenses and other current assets	35,469	24,500
Other assets	16,614	—
Accounts payable	(478,781)	(438,628)
Accrued expenses	(1,685,718)	78,647
Deferred research and development obligation	(92,596)	98,737
Net cash (used in) provided by continuing operations	(4,536,001)	1,235,428
Net cash provided by discontinued operations	—	678,577
Net cash (used in) provided by operating activities	(4,536,001)	1,914,005
<b>INVESTING ACTIVITIES</b>		
Restricted cash	(2,795)	—
Purchase of held-to-maturity securities	(51,202,000)	—
Proceeds from repayment and maturities of held-to-maturity securities	2,500,000	—
Net cash (used in) provided by continuing operations	(48,704,795)	—
Net cash used in discontinued operations	—	(142,145)
Net cash used in investing activities	(48,704,795)	(142,145)
<b>FINANCING ACTIVITIES</b>		
Proceeds from the sale of common stock	100,000	8,069
Proceeds from repayment of stock subscriptions	40,625	90,750
Purchases of common stock	(9,672,969)	—
Proceeds from issuance of convertible debt	—	2,000,000
Repayment of convertible debt	—	(50,000)
Net cash (used in) provided by continuing operations	(9,532,344)	2,048,819
Net cash provided by (used in) discontinued operations	—	—
Net cash (used in) provided by financing activities	(9,532,344)	2,048,819
Net (decrease) increase in cash and cash equivalents	(62,773,140)	3,820,679
Cash and cash equivalents at beginning of period	68,601,138	2,495,455
Cash and cash equivalents at end of period	\$ 5,827,998	\$ 6,316,134
<b>SUPPLEMENTAL CASH FLOW INFORMATION</b>		
Cash paid for interest	\$ 909	\$ 570,887
Cash paid for income taxes, net of refunds	\$ 169,903	\$ —

The Accompanying Notes are an Integral Part of these Unaudited Consolidated Financial Statements



## Notes to the Consolidated Financial Statements (unaudited)

### Note 1: Organization and Summary of Significant Accounting Policies

#### *Description of Business*

Dyadic International, Inc. ("Dyadic", "we", or the "Company") is a global biotechnology company based in Jupiter, Florida with a foreign subsidiary, Dyadic Nederland, BV, which maintains a small satellite office in Wageningen, the Netherlands. Over the past two decades, the Company has developed a method for producing commercial quantities of enzymes and other proteins required for the production of industrial enzymes; and has successfully licensed this technology to third parties such as Abengoa Bioenergy, BASF, Codexis and others. This technology is based on the *Myceliophthora thermophila* fungus, which the Company nicknamed C1. The C1 technology is a robust and versatile fungal expression system for gene discovery, development, and production of enzymes and other proteins.

On December 31, 2015, the Company sold its industrial technology business to DuPont's (NYSE: DD) industrial biosciences business for \$75 million (the "DuPont Transaction"). The DuPont Transaction included \$8 million of the purchase price to be held in escrow for 18 months to ensure Dyadic's obligations with respect to certain indemnity claims and working capital adjustments. The current escrow amount of approximately \$7.4 million in the accompanying balance sheet is net of contractual working capital adjustments already agreed to by the parties and interest earned to date. See details under caption "Escrowed Funds from Sale of Assets" below.

In connection with the DuPont Transaction, DuPont granted Dyadic co-exclusive rights to the C1 technology for use in human and animal pharmaceutical applications, with the exclusive ability to enter into sub-license agreements. DuPont retained certain rights to utilize the C1 technology for use in pharmaceutical applications, including the development and production of pharmaceutical products, for which it will make royalty payments to Dyadic upon commercialization. In certain circumstances, Dyadic may owe a royalty to either DuPont or certain licensor's of DuPont, depending upon whether Dyadic elects to utilize certain patents either owned or licensed by DuPont.

The Company is currently focusing on the biopharmaceutical industry and leveraging the patented and proprietary C1 expression system to help accelerate the development and production of biologic vaccines and drugs at flexible commercial scales for its use in the discovery, development, and manufacturing of human and animal vaccines, monoclonal antibodies, biosimilars and/or biobetters, and other therapeutic proteins.

#### *Basis of Presentation*

The accompanying unaudited interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiary. All significant intra-entity transactions and balances have been eliminated in consolidation.

The accompanying unaudited interim consolidated financial statements for Dyadic International, Inc. and its subsidiary have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") for interim financial reporting. Accordingly, certain information and footnote disclosures normally included in annual consolidated financial statements have been condensed or omitted. In the opinion of management, the accompanying unaudited interim consolidated financial statements reflect all adjustments (consisting of only normal recurring adjustments and the elimination of intra-entity accounts) considered necessary for a fair presentation of all periods presented. The results of Dyadic's operations for any interim periods are not necessarily indicative of the results of operations for any other interim period or for a full fiscal year. These unaudited interim consolidated financial statements should be read in conjunction with the consolidated financial statements and footnotes included in our Annual Report for the year ended December 31, 2015, which was posted to the OTC Markets website on March 29, 2016.

We have reclassified the revenues and expenses of our industrial technology business related to the DuPont Transaction to "income (loss) from discontinued operations" for all of the periods presented in the accompanying interim consolidated financial statements. The Company reclassified \$22,222 of 2015 income tax expense from continuing to discontinued operations for the quarter ended September 30, 2015. In addition, the Company reclassified a gain of \$23,136 and a loss of \$105,521 on foreign currency transaction for the three and nine months ended September 30, 2015, respectively, from the discontinued to continuing operations. Such adjustments were made to correct an erroneous classification.

The tables below set forth the adjusted results of operations from discontinued operations for the three and nine months ended September 30, 2015, and cash flows from discontinued operations for the nine months ended September 30, 2015:

### **INCOME FROM DISCONTINUED OPERATIONS**

	<b>Three Months Ended September 30, 2015</b>	<b>Nine Months Ended September 30, 2015</b>
<b>REVENUES:</b>		
Product Related Revenue, Net	\$ 3,272,497	\$ 9,507,207
License Fee Revenue	567	800,567
Research and Development Revenue	471,322	1,230,233
Total Revenue	<u>3,744,386</u>	<u>11,538,007</u>
<b>COSTS AND EXPENSES (INCOME):</b>		
Cost of Goods Sold	2,264,790	6,856,869
General and Administrative	82,733	(21,472)
Sales and Marketing	139,263	681,727
Research and Development	453,208	1,261,783
Foreign Currency Transaction Loss, Net	14,475	49,233
Total Expenses	<u>2,954,469</u>	<u>8,828,140</u>
<b>INCOME FROM DISCONTINUED OPERATIONS BEFORE OTHER EXPENSE</b>	<u>789,917</u>	<u>2,709,867</u>
<b>OTHER EXPENSE:</b>		
Interest Expense	(221,116)	(620,257)
<b>NET INCOME FROM DISCONTINUED OPERATIONS BEFORE INCOME TAXES</b>	<u>568,801</u>	<u>2,089,610</u>
Provision for Income Taxes	(32,200)	(32,200)
<b>NET INCOME FROM DISCONTINUED OPERATIONS</b>	<u>\$ 536,601</u>	<u>\$ 2,057,410</u>

### **CASH FLOWS FROM DISCONTINUED OPERATIONS**

	<b>Nine Months Ended September 30, 2015</b>
Cash Flows Provided By Operating Activities	\$ 678,577
Net Cash Used In Investing Activities	(142,145)
	<u>\$ 536,432</u>

#### ***Use of Estimates***

The preparation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles (“GAAP”) requires management to make estimates and judgments that affect the reported amount of assets and liabilities and related disclosure of contingent assets and liabilities at the date of our consolidated financial statements and the reported amounts of revenues and expenses during the applicable period. Actual results may differ from these estimates under different assumptions or conditions. Such differences could be material to the consolidated financial statements.

### ***Cash and Cash Equivalents***

We treat highly liquid investments with original maturities of three months or less when purchased as cash and cash equivalents, including money market funds, which are unrestricted for withdrawal or use. At times, the Company has cash and cash equivalents at financial institutions exceeding the Federal Depository Insurance Company ("FDIC") and the Securities Investor Protection Corporation ("SIPC") insured limit on domestic currency and the Netherlands FDIC counterpart for foreign currency. The Company only deals with reputable financial institutions and has not experienced any losses on these accounts.

### ***Investment Securities***

Investment securities are classified as held-to-maturity, available-for-sale, or trading at the date of purchase. Held-to-maturity securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums or discounts. Premiums and discounts are amortized over the life of the related held-to-maturity security. When a debt security is purchased at a premium, the statement of cash flows reflects an investing outflow for the face value of the debt, with the premium reflected as an operating outflow. Available-for-sale securities are recorded at fair value with associated unrealized gains or losses included in accumulated other comprehensive income (loss) in stockholders' equity. Other-than-temporary impairment charges are included in other income (expense).

In April 2016, the Company began to invest excess cash in a structured investment program managed by a reputable investment firm. Such investments consist of a basket of money market funds and investment grade corporate bonds with varying durations, in each case, less than eighteen (18) months.

Management determines the appropriate classification of its investments at the time of purchase and reevaluates the classifications at each balance sheet date. The Company's investments in debt securities have been classified and accounted for as held-to-maturity. Held-to-maturity securities are those securities that the Company has the ability and intent to hold until maturity. The Company's investments in money market funds have been classified and accounted for as available-for-sale securities, and presented as cash equivalents on the balance sheet. As of September 30, 2016, the majority of our money market funds were invested in U.S. Government money market funds.

The Company classifies its investment securities as either short-term or long-term based on each instrument's underlying contractual maturity date. Investment securities with maturities of 12 months or less are classified as short-term, and investment securities with maturities greater than 12 months are classified as long-term. The Company did not have any investment securities classified as trading as of September 30, 2016 and December 31, 2015.

### ***Accounts Receivable***

Accounts receivable are recorded at their net realizable value on the date revenue is recognized or the Company has a contractual right to receive money, either on demand or at fixed or determinable dates. The Company provides allowances for doubtful accounts for estimated losses resulting from the inability of its customers to repay their obligations. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to pay, additional allowances may be required.

### ***Prepaid Expenses and Other Assets***

Prepaid expenses and other assets as of September 30, 2016, and December 31, 2015 consisted of the following:

	<b>September 30, 2016</b>	<b>December 31, 2015</b>
	<b>(Unaudited)</b>	<b>(Audited)</b>
Prepaid income taxes and tax receivable	\$ 208,401	\$ 233,900
Prepaid expenses - general	73,290	99,208
Prepaid insurance	126,004	94,289
Prepaid value added taxes	47,068	63,353
	<b>\$ 454,763</b>	<b>\$ 490,750</b>

### ***Escrowed Funds from Sale of Assets***

As of September 30, 2016, the balance of escrowed funds from the sale of assets was approximately \$7,364,000, representing \$8,000,000 of the proceeds from the DuPont Transaction held in escrow for eighteen months and approximately \$3,000 of interest earned to date offset by the settlement of a net working capital adjustment of approximately \$639,000 which has been agreed to by the parties. The amount of working capital adjustment was paid to DuPont directly from the escrowed funds account on February 12, 2016.

### ***Accrued Expenses***

Accrued expenses as of September 30, 2016, and December 31, 2015 consisted of the following:

	<b>September 30, 2016</b>	<b>December 31, 2015</b>
	<b>(Unaudited)</b>	<b>(Audited)</b>
Accrued employee termination costs, wages and benefits	\$ 104,000	\$ 1,967,497
Accrued expenses - other	317,650	146,175
	<u>\$ 421,650</u>	<u>\$ 2,113,672</u>

### ***Revenue Recognition***

Revenue is recognized when (1) persuasive evidence of an arrangement exists; (2) services have been rendered or product has been delivered; (3) price to the customer is fixed and determinable; and (4) collection of the underlying receivable is reasonably assured.

The Company recognizes revenue from research funding under collaboration agreements when earned on a “proportional performance” basis as research hours are incurred. The Company typically performs services as specified in each respective agreement on a best efforts basis, and is reimbursed based on labor hours incurred on each contract. The Company initially defers revenue for any amounts billed and payments received in advance for services performed. The Company then recognizes revenue pursuant to the related pattern of performance, based on total labor hours incurred relative to total labor hours estimated under the contract. As of September 30, 2016 and December 31, 2015, the deferred research and development obligation were \$36,422 and \$129,018, respectively. During the nine months ended September 30, 2016 and 2015, the Company recognized research and development revenue from continuing operations in the amount of \$101,836 and \$285,721 respectively.

### ***Research and Development Costs***

Research and development (“R&D”) costs are expensed as incurred. During the three and nine months ended September 30, 2016, the Company recorded \$369,359 and \$963,673 of R&D expenses respectively. The R&D costs are related to the Company's internally funded R&D pharmaceutical programs and other governmental and commercial projects.

### ***Foreign Currency Transaction Gain or Loss***

The Company's foreign subsidiary uses the U.S. dollar as its functional currency, and it initially measures the foreign currency denominated assets and liabilities at the transaction date. Monetary assets and liabilities are then re-measured at exchange rates in effect at the end of each period, and inventories, property and nonmonetary assets and liabilities are converted at historical rates.

### ***Other Income***

On April 19, 2016, the Company received an amount of approximately \$2.1 million, in connection with the Company's settlement with one of the two remaining defendant law firms, Bilzin Sumberg Baena Price & Axelrod LLP, in its ongoing professional liability litigation. The Company recorded such amount as a gain on settlement of litigation, net of legal fees and expenses, in the second quarter of 2016.

### ***Fair Value Measurements***

The Company applies fair value accounting for certain financial instruments that are recognized or disclosed at fair value in the financial statements. The Company defines fair value as the price that would be received from selling

an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is estimated by applying the following hierarchy, which prioritizes the inputs used to measure fair value into three levels and bases the categorization within the hierarchy upon the lowest level of input that is available and significant to the fair value measurement:

- *Level 1* – Quoted prices in active markets for identical assets or liabilities.
- *Level 2* – Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- *Level 3* – Inputs that are generally unobservable and typically reflect management’s estimate of assumptions that market participants would use in pricing the asset or liability.

Assets and liabilities on the unaudited interim consolidated balance sheets are measured at carrying values, which approximate fair values due to the short term nature of these balances. Such items include cash and cash equivalents, accounts receivable, accounts payable, prepaid expenses, and accrued expenses. See Note 2 for further information on the fair value measurements of the Company's investment securities.

### ***Income Taxes***

The Company has net operating loss ("NOL") carryforwards available in 2016 that will begin to expire in 2034. As of September 30, 2016 and December 31, 2015, the Company had NOLs in the amount of approximately \$4.9 million and \$5.8 million, respectively.

In preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves management estimation of our actual current tax exposure and assessment of temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the consolidated statement of operations. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets.

For the nine months ended September 30, 2016, the Company recorded a current provision for income tax of \$184,439 for adjustments related to our 2015 tax return.

The deferred tax assets as of September 30, 2016 and December 31, 2015 were approximately \$3.3 million and \$2.0 million, respectively. Due to the Company’s history of operating losses and the uncertainty regarding our ability to generate taxable income in the future, the Company has established a 100% valuation allowance against deferred tax assets as of September 30, 2016 and December 31, 2015.

The Company is not subject to U.S. federal, state and local tax examinations by tax authorities for the years before 2013.

### ***Comprehensive Income (Loss)***

Comprehensive income (loss) includes net income (loss) and other revenue, expenses, gains and losses that are recorded as an element of shareholders' equity but are excluded from net income (loss) under U.S. GAAP. The Company does not have any items that are not included in net income (loss), and therefore, its comprehensive income (loss) is the same as net income (loss) for all periods presented.

### ***Stock-Based Compensation***

We recognize all share-based payments to employees and to non-employee directors, for service on our board of directors, as compensation expense in the consolidated financial statements based on the grant date fair values of such payments. Stock-based compensation expense recognized each period is based on the value of the portion of share-based payment awards that is ultimately expected to vest during the period. Forfeitures are estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

### ***Recent Accounting Pronouncements***

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). Under the new guidance, lessees will be required to recognize the assets and liabilities that arise from operating leases. A lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. ASU 2016-02 will be effective for the Company beginning in the first quarter of 2019 and early application is permitted. The Company is currently evaluating the impact, if any, of the adoption of this newly issued guidance to its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU 2016-09, Compensation - Stock Compensation (Topic 718) Improvements to Employee Share-Based Payment Accounting. The guidance simplifies several aspects of the accounting for employee share-based payment transactions including allowing excess tax benefits or tax deficiencies to be recognized as income tax benefits or expenses in the Statements of Income rather than in Additional Paid in Capital (APIC). Also, excess tax benefits no longer represent a financing cash inflow on the Statement of Cash Flows and instead will be included as an operating activity. Under this guidance, excess tax benefits and tax deficiencies will be excluded from the calculation of diluted earnings per share, whereas under current accounting guidance, these amounts must be estimated and included in the calculation. In addition, this simplifies the accounting for forfeitures and changes the statutory tax withholding requirements for share-based payments. ASU 2016-09 will be effective for the Company beginning in the first quarter of 2017 and early adoption is permitted. The Company is currently evaluating the impact, if any, of the adoption of this newly issued guidance to its consolidated financial statements and related disclosures.

### ***Financial Instruments***

In January 2016, the FASB issued ASU 2016-01, Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. ASU 2016-01 will be effective for the Company beginning in the first quarter of 2018. The Company is currently evaluating the impact, if any, of the adoption of this newly issued guidance to its consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which modifies the measurement of expected credit losses of certain financial instruments. ASU 2016-13 will be effective for the Company beginning in the first quarter of 2020. The Company is currently evaluating the impact, if any, of the adoption of this newly issued guidance to its consolidated financial statements.

### ***Revenue Recognition***

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), which amends the existing accounting standards for revenue recognition. ASU 2014-09 is based on principles that govern the recognition of revenue at an amount an entity expects to be entitled when products are transferred to customers. ASU 2014-09 will be effective for the Company beginning in the first quarter of 2018.

Subsequently, the FASB has issued the following standards related to ASU 2014-09: ASU 2016-08, Revenue from Contracts with Customers (Topic 606) - Principal versus Agent Considerations (Reporting Revenue Gross versus Net); ASU 2016-10, Revenue from Contracts with Customers (Topic 606) - Identifying Performance Obligations and Licensing; and ASU 2016-12, Revenue from Contracts with Customer (Topic 606) - Narrow-Scope Improvement and Practical Expedients. The Company must adopt ASU 2016-08, ASU 2016-10, and ASU 2016-12 together with ASU 2014-09 (collectively, the "new revenue standards.")

The new revenue standards may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. The Company is currently evaluating the timing of its adoption and the impact, if any, of the adoption of the new revenue standards to its consolidated financial statements and related disclosures.

## Note 2: Cash, Cash Equivalents and Investment Securities

The Company's held-to-maturity debt securities are carried at amortized costs, and its investments in money market funds are classified as cash equivalents. The following tables show the Company's cash, available-for-sale securities, and short-term and long-term investment securities by major security type as of September 30, 2016:

September 30, 2016							
	Level (1)	Fair Value	Unrealized Gains/ Losses	Adjusted Cost	Cash and Cash Equivalents	Short-Term Investment Securities	Long-Term Investment Securities
Cash		\$ 5,643,743	\$ —	\$ 5,643,743	\$ 5,643,743	\$ —	\$ —
Money Market Funds	1	184,255	—	184,255	184,255	—	—
Corporate Bonds	2	49,932,958	—	50,074,381	—	44,112,658	5,961,723
<b>Total</b>		<b>\$ 55,760,956</b>	<b>\$ —</b>	<b>\$ 55,902,379</b>	<b>\$ 5,827,998</b>	<b>\$ 44,112,658</b>	<b>\$ 5,961,723</b>

(1) See Note 1 - Significant accounting policy for the definition of the three-level fair value hierarchy.

The Company had no investment in money market funds or corporate bonds in 2015, and the cash balance of \$68,601,138 as of December 31, 2015 was classified as cash and cash equivalents.

The Company considers the declines in market value of its investment portfolio to be temporary in nature. The Company's investment policy requires investment securities to be investment grade and held to maturity with the primary objective to maintain a high degree of liquidity while maximizing yield. When evaluating an investment for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates, and whether it is more likely than not the Company will be required to sell the investment before recovery of the investment's cost basis. As of September 30, 2016, the Company does not consider any of its investments to be other-than-temporarily impaired.

## Note 3: Commitments and Contingencies

### *Leases*

#### *Jupiter, Florida Headquarters*

The Company's corporate headquarters are located in Jupiter, Florida. The Company occupies approximately 4,900 square feet with a monthly rental rate and common area maintenance charges of approximately \$8,700. The lease expires on June 30, 2017.

#### *The Netherlands Office*

The Company maintains a small satellite office in Wageningen, The Netherlands. The Company occupies approximately 900 square feet with annual rentals and common area maintenance charges of approximately \$4,700. The lease expires on January 31, 2019.

### *Employment Agreements*

The previous employment agreements of two executives of the Company contained, among other things, change of control obligations of approximately \$1.56 million that, if triggered by the employees' voluntary termination, would entitle such executives to a lump sum severance payment. During the second quarter of 2016, the Company entered into new employment agreements with these two executives. These agreements included, among other provisions, payment of the former change of control obligations over the term of the new agreements rather than in a lump sum payment, modification of base compensation, and all incentive payments in excess of base compensation will be paid solely in the form of stock options contingent upon the achievement of certain milestones either specified in the agreements and/or to be determined by the compensation committee on an annual basis. The payment of change of control obligations began in the second quarter of 2016 and will continue for the 24 and 36 month terms of their respective contracts. The new employment agreements do not contain any further change of control obligations. See

Note 5, *Share-Based Compensation* for additional information regarding the options issued for incentive compensation pursuant to these agreements.

### ***Professional Liability Lawsuit***

On March 26, 2009, the Company filed a complaint in the Circuit Court of the 15<sup>th</sup> Judicial Circuit in and for Palm Beach County, Florida against Ernst & Young LLP and Ernst & Young-Hong Kong, L.P., alleging professional negligence/malpractice, breach of fiduciary duty and constructive fraud in connection with the accounting, advisory, auditing, consulting, financial and transactional services they provided to the Company.

On April 14, 2009, the Company amended the complaint (the “Amended Complaint”) by naming as additional defendants the Company’s former outside legal counsel consisting of the law firms of Greenberg Traurig, LLP, Greenberg Traurig, P.A. (collectively, “Greenberg Traurig”), Jenkens & Gilchrist, P.C. (“Jenkins & Gilchrist”) and Bilzin Sumberg Baena Price & Axelrod LLP (“Bilzin Sumberg”) as well as attorney Robert I. Schwimmer who previously represented the Company while an attorney at Jenkins & Gilchrist and later at Greenberg Traurig. Jenkins & Gilchrist went out of business in 2007 and is in the process of winding up its business and affairs. The Company also named as defendants the law firm of Moscowitz & Moscowitz, P.A. and its attorneys Norman A. Moscowitz and Jane W. Moscowitz (collectively, the “Moscowitz Defendants”) who conducted the investigation and authored the investigative report requested by the Company’s Audit Committee following the discovery of alleged improprieties at the Company’s Asian subsidiaries. The claims against the Company’s former outside legal counsel are for breach of fiduciary duty and professional negligence. In addition to these claims, the Amended Complaint contains a claim of civil conspiracy against Ernst & Young LLP, Greenberg Traurig and Mr. Schwimmer. The claims against Ernst & Young LLP and Ernst & Young-Hong Kong, L.P. were subsequently stayed in the Circuit Court action and submitted to binding arbitration. A final hearing before the arbitration tribunal was completed on May 27, 2011. On February 29, 2012, the arbitration tribunal issued a Final Award which found no auditor negligence, denied the Company any recovery against Ernst & Young LLP and Ernst & Young Hong Kong L.P., and further provided that each party shall bear its own attorneys’ fees and costs.

On July 11, 2011, defendants Jenkins & Gilchrist, Bilzin Sumberg and the Moscowitz Defendants filed a counterclaim in the Circuit Court against the Company and a Third Party Complaint against its President and Chief Executive Officer, Mark Emalfarb, individually, for abuse of process.

The counter claim and Third Party Complaint filed by Jenkins & Gilchrist and Bilzin Sumberg also included claims for common law indemnity against the Company and Mr. Emalfarb. In addition, Jenkins & Gilchrist made a claim against the Company for breach of the implied covenant of good faith and fair dealing. On July 18, 2011, the Moscowitz Defendants filed a motion for summary judgment which the Circuit Court denied in its entirety. On September 9, 2011, Jenkins & Gilchrist and Bilzin Sumberg amended their counterclaim and Third Party Complaint which dropped their claims for abuse of process but retained their claims for common law indemnity against the Company and Mr. Emalfarb.

Bilzin Sumberg also added claims against the Company and Mr. Emalfarb for breach of its retainer agreements and for declaratory relief. Also on September 9, 2011, the Moscowitz Defendants dropped their claims for abuse of process against the Company and Mr. Emalfarb. On December 8, 2011, the Circuit Court dismissed without prejudice all counterclaims against the Company and all third party claims against Mr. Emalfarb.

On July 18, 2012, the Company filed a Second Amended Complaint which expanded and amplified the Company’s prior allegations of negligent acts and omissions by the defendants in the Circuit Court proceedings. All of the defendants have filed and served their answers and affirmative defenses.

On August 8, 2012, the Company, Jenkins & Gilchrist and Mr. Schwimmer entered into a Settlement Agreement and General Releases (the “J&G Settlement Agreement”) whereby Jenkins & Gilchrist paid the Company \$525,000 for the mutual release and discharge of (1) all causes of action between the Company and Jenkins & Gilchrist, and (2) causes of action between the Company and Mr. Schwimmer including, but not limited to, those in the professional liability lawsuit, but only those which occurred while Mr. Schwimmer served as an attorney at Jenkins & Gilchrist and not while he served as an attorney at Greenberg Traurig or any other time. Such amount was included in other income in the consolidated statement of operations for the year ended December 31, 2012. Pursuant to the J&G Settlement Agreement, the Company, Jenkins & Gilchrist and Mr. Schwimmer have filed a Stipulation of Settlement with the Court to enforce the terms of the J&G Settlement Agreement including, but not limited to, the dismissal of Counts I and II of the Second Amended Complaint against Jenkins & Gilchrist and Mr. Schwimmer with prejudice.



On January 24, 2013, each of the remaining defendants served their amended affirmative defenses to the Second Amended Complaint. On February 11, 2013, the Company served its reply to such amended affirmative defenses.

The Company and the defendants in the Circuit Court proceedings are continuing to engage in written discovery, oral depositions and motion practice.

On November 26, 2013, the Court entered a Case Management Order. Pursuant to the Order, all pretrial motions and other litigation activities were to have been concluded by the end of 2014. The Court ordered mediation was held on November 10<sup>th</sup> and 11<sup>th</sup>, 2014.

On July 31, 2015, the Company reached a settlement with one of the three remaining defendant law firms in its ongoing professional liability litigation. On August 12, 2015 the Company received full payment in the amount of \$2,170,000, which is net of fees and expenses. The settlement amount was reported in the Company's consolidated statement of operations, in other income, for the year ended December 31, 2015.

On September 29, 2015, the Court removed the professional liability litigation from the Court's eight week trial docket which commenced on October 26, 2015. Instead, the Court, in an effort to promote settlement, ordered the parties to non-binding arbitration with an initial hearing to occur before December 16, 2015. The parties were scheduled to appear before the Court on November 13, 2015 for hearings on various pre-trial motions. At that time, the Court was expected to address when the professional liability litigation will be set for trial in 2016. The parties also voluntarily agreed to again attend mediation on November 18, 2015.

The parties attended both mediation and non-binding arbitration. No resolution was reached. Pretrial motion practice is now substantially completed. On March 3, 2016, the Court issued an Order setting a six week jury trial commencing January 6, 2017.

On April 5, 2016, the Company reached a settlement with one of the two remaining defendant law firms, Bilzin Sumberg Baena Price & Axelrod LLP, in its ongoing professional liability litigation. On April 19, 2016, the Company received full payment in the amount of \$2,100,000, which is net of legal fees and expenses. The settlement amount was reported in the Company's consolidated statement of operations, in other income, for the quarter ended June 30, 2016. The trial with the remaining defendant law firm Greenberg Traurig, LLP, Greenberg Traurig, P.A. (collectively, "Greenberg Traurig") and the estate of Robert I Schwimmer remains set for January 6, 2017.

On July 8, 2016, the Court heard oral argument on Greenberg Traurig's Renewed Motion for Summary Judgment as to its judgmental immunity affirmative defense.

On July 28, 2016, the Company stipulated to the release of the estate of Robert Schwimmer as a defendant. This was a procedural decision as Greenberg Traurig remains liable for the negligent conduct of deceased Greenberg Traurig lawyer, Robert Schwimmer.

On August 17, 2016, the Court denied Greenberg Traurig's Renewed Motion for Summary Judgment as to its judgmental immunity affirmative defense.

On October 17, 2016, Greenberg Traurig filed a Motion to Continue the Trial. On October 18, 2016, Greenberg Traurig filed a motion to bifurcate the liability and damages determination by the jury into separate trials. On October 27, 2016, the Court heard oral argument on both motions. Both motions were denied.

Trial remains set to commence on January 6, 2017 with jury selection.

In addition to the matters noted above, from time to time, the Company is subject to legal proceedings, asserted claims and investigations in the ordinary course of business, including commercial claims, employment and other matters, which management considers immaterial, individually and in the aggregate. The Company makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. The requirement for these provisions are reviewed at least quarterly and adjusted to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case. Litigation is inherently unpredictable and costly. While the Company believes that it has valid defenses with respect to the legal matters pending against it, protracted litigation and/or an unfavorable resolution of one or more of such proceedings, claims or investigations against the Company could have a material adverse effect on the Company's consolidated financial position, cash flows or results of operations.

#### Note 4: Common Stock

##### *Issuances of Common Stock*

During the nine months ended September 30, 2016 and 2015, the Company issued 647,152 and 38,125 shares of common stock, respectively. The shares of common stock issued for the three and nine months ended September 30, 2016 are as follows:

	Three Months Ended September 30, 2016		Nine Months Ended September 30, 2016	
	Number of Shares Issued	Price per Share	Number of Shares Issued	Price per Share
Exercise of Stock Options	15,972	\$1.21	263,586	\$0.15 - \$1.55
Grants and Vesting of Restricted Stock	—	N/A	316,550	\$0.97 - \$1.93
Sale of Common Stock	—	N/A	64,516	\$1.55
Exercise of Warrants	—	N/A	2,500	\$0.15
TOTAL	<u>15,972</u>		<u>647,152</u>	

As of September 30, 2016, there were 1,147,273 outstanding warrants that are exercisable to purchase shares of common stock. These warrants were issued on December 31, 2015 in conjunction with the repayment or conversion of the Convertible Debt at a strike price of \$1.48, and will expire on December 31, 2016.

During the nine months ended September 30, 2016 and 2015, \$40,625 and \$90,750, respectively was repaid under the Company's 2013 Employee Loan Program (the "Loan Program"). Amounts borrowed under the Loan Program bear interest at 3% per annum and are repayable within 24 months from the date of the loan agreement. The loans are collateralized by the shares of common stock issued in connection with the exercise of the related stock options and warrants. As of September 30, 2016 and December 31, 2015, advances to employees under the Loan Program were \$0 and \$41,000, respectively, and are included in stockholders' equity in the accompanying consolidated balance sheets. As of September 30, 2016, there was no outstanding loan amount under the Loan Program, and the Company currently has no plan to grant any new loan related to the exercise of employee stock options and warrants in the future.

##### *Share Repurchase Program and Buybacks*

On January 12, 2016, the Company repurchased and retired an aggregate of 2,136,752 shares of its common stock at \$1.35 per share for an aggregate purchase price of \$2,884,615 pursuant to a Securities Purchase Agreement entered into with Abengoa Bioenergy New Technologies, LLC ("ABNT"). The \$1.35 per share price is equal to the average conversion price that Dyadic convertible debt holders received upon conversion of debt as of December 31, 2015. These shares repurchased from ABNT were treated as effective retirements, and therefore reduced reported shares issued and outstanding by the number of shares repurchased. The Company recorded the excess of the purchase price over the par value of the common stock as a reduction of additional paid-in capital.

On February 16, 2016, the Board of Directors authorized a stock repurchase program, under which the Company may repurchase up to \$15 million of its outstanding common stock (the "2016 Stock Repurchase Program"). Under the 2016 Stock Repurchase Program, the Company may repurchase shares in open-market purchases in accordance with all applicable securities laws and regulations, including Rule 10b-18 of the Securities Exchange Act of 1934, as amended. The extent to which the Company repurchases its shares, and the timing of such repurchases, will depend upon a variety of factors, including market conditions, regulatory requirements and other corporate considerations, as determined by the Company's management. The repurchase program may be extended, suspended or discontinued at any time. The Company expects to finance the program from existing cash resources. Under the 2016 Stock Repurchase Program, all repurchased shares are to be held in treasury.

The following table summarized the Company's 2016 Stock Repurchase Program activities during the periods presented:

Period	Number of Shares Purchased	Average Repurchase Price per Share	Amount	Total Number of Treasury Shares Purchased as Part of Publicly Announced Plan	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plan
January 12, 2016 - ABNT repurchased and retired shares	2,136,752	\$1.35	\$2,884,615	—	N/A
<b>2016 Stock Repurchase Program:</b>					
January through March 2016	713,655	1.56	1,114,100	713,655	\$13,885,900
April through June 2016	1,176,900	1.69	1,983,360	1,176,900	11,902,540
July 2016 through September 2016	2,457,549	\$1.50	3,690,894	2,457,549	\$8,211,646
Total open market and privately negotiated purchase	<u>6,484,856</u>		<u>\$9,672,969</u>	<u>4,348,104</u>	

## Note 5: Share-Based Compensation

### Description of Equity Plans

The Company has two stock compensation plans, the Dyadic International, Inc. 2006 Stock Option Plan, as amended (the "2006 Stock Option Plan") and the Dyadic International, Inc. 2011 Equity Incentive Award Plan (the "2011 Equity Incentive Plan") (the 2006 Stock Option Plan and the 2011 Equity Incentive Plan are hereinafter collectively referred to as the "Equity Compensation Plans"). Options granted under the Equity Compensation Plans are service-based and typically vest in equal annual installments over a four year period.

During the nine months ended September 30, 2016, the Company granted stock options to purchase an aggregate of 1,293,333 shares of the Company's common stock at a weighted average exercise price of \$1.67 per share. The weighted average grant-date fair market value of stock options granted during the nine months ended September 30, 2016 was \$1.24 per stock option based on the Black-Scholes valuation model. Assumptions used in the Black-Scholes valuation model for options granted were as follows:

Risk-Free interest rate	1.18% - 2.24%
Expected annual dividend yield	—%
Expected stock price volatility	74.01% - 77.50%
Expected life of options	5 Years

During the nine months ended September 30, 2016 and 2015, there were 796,500 and 38,125, respectively, stock options exercised. The 796,500 stock options exercised during the nine months ended September 30, 2016 were based on a cashless exercise resulting in the issuance of 263,586 shares of common stock at a weighted average exercise price of \$0.82 and the surrender of 532,914 shares at a weighted average exercise price of \$1.20.

During the nine months ended September 30, 2016 and 2015, there were 2,025,000 and 434,750, respectively, stock options that expired or were canceled. The canceled stock options for the nine months ended September 30, 2016 principally reflect stock options canceled resulting from employee and consultant separations in connection with the DuPont Transaction.

The following table summarizes the combined activity for the Company's two Equity Compensation Plans:

	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at December 31, 2014	4,102,125	\$1.68		
Granted	156,000	1.04		
Exercised	(38,125)	0.21		
Expired	(300,000)	2.28		
Canceled	(208,750)	1.38		
Outstanding at December 31, 2015	3,711,250	1.63	6.3	\$962,205
Granted	1,293,333	1.67		
Exercised	(796,500)	1.07		
Expired	(150,000)	2.12		
Canceled	(1,875,000)	1.91		
Outstanding at September 30, 2016	2,183,083	\$1.59	6.1	157,783
Exercisable at September 30, 2016	1,125,583	\$1.51	6.1	\$155,633

The foregoing table includes 650,000 stock options issued in connection with the contingent compensation incentives discussed in Note 3, *Commitments and Contingencies*, and will only vest upon the achievement of the performance milestones specified in the employment agreements. In the event that the performance milestones are not achieved, the option grants relating to any unattained milestones will be automatically canceled. Recognition of compensation costs related to these milestone-based contingent stock options has been deferred until these options vest upon the achievement of the incentive milestones contained in the employment agreements.

Share-based compensation expense is included in general and administrative expenses in the consolidated statements of operations. The following table summarizes the Company's non-cash share-based compensation expense related to continuing and discontinuing operations for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2016	2015	2016	2015
Share-based compensation expense - stock options	\$ 78,588	\$ 125,358	\$ 388,471	\$ 312,594
Share-based compensation expense - restricted stock	\$ —	\$ 7,763	\$ 150,000	\$ 53,225
Share-based compensation expense from continuing operations	\$ 78,588	\$ 133,121	\$ 538,471	\$ 365,819
Share-based compensation expense from discontinued operations	—	25,943	—	63,523
Total share-based compensation expense	\$ 78,588	\$ 159,064	\$ 538,471	\$ 429,342

## Note 6: Earnings Per Share

Basic earnings (loss) per share is computed by dividing net income or (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings (loss) per share is computed by dividing net income (loss) adjusted for convertible debt interest by the weighted average number of common shares after considering the additional dilution related to common stock options, stock warrants, restricted stock and convertible debt. The dilutive effect of potentially dilutive securities is reflected in diluted earnings per share by applying the treasury stock method.

The following table shows the calculation of basic and diluted earnings per share for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2016	2015	2016	2015
Net Income (Loss) from Continuing Operations	\$ (1,165,421)	\$ 1,373,625	\$ (1,546,554)	\$ (951,057)
Net Income (Loss) from Discontinued Operations	—	536,601	—	2,057,410
Total Net Income (Loss), As Reported	\$ (1,165,421)	\$ 1,910,226	\$ (1,546,554)	\$ 1,106,353
Weighted Average Common Shares	36,185,164	34,162,356	37,464,968	34,149,195
Adjustment for Restricted Stock	—	82,600	49,347	67,798
Adjustment for Warrants	—	2,500	—	2,500
Total Basic Weighted Average Shares	36,185,164	34,247,456	37,514,315	34,219,493
Adjustment for Dilutive Restricted Stock	—	22,850	—	22,850
Adjustment for Dilutive Stock Options	—	147,845	—	168,427
Total Dilutive Weighted Average Shares	36,185,164	34,418,151	37,514,315	34,410,770
Basic Net Income (Loss) Per Share:				
Continuing Operations	\$ (0.03)	\$ 0.04	\$ (0.04)	\$ (0.02)
Discontinued Operations	—	0.02	—	0.05
Total Basic Net Income (Loss) Per Share	\$ (0.03)	\$ 0.06	\$ (0.04)	\$ 0.03
Diluted Net Income (Loss) Per Share:				
Continuing Operations	\$ (0.03)	\$ 0.04	\$ (0.04)	\$ (0.02)
Discontinued Operations	—	0.02	—	0.05
Total Diluted Net Income (Loss) Per Share	\$ (0.03)	\$ 0.06	\$ (0.04)	\$ 0.03

Potentially dilutive securities whose effect would have been anti-dilutive are excluded from the calculation of diluted earnings (loss) per share. For the three and nine months ended September 30, 2016, a total of 3,330,359 shares of potentially dilutive securities were excluded from the computation of diluted earnings (loss) per share, including 2,183,083 shares of stock options and 1,147,276 shares of warrants outstanding as of September 30, 2016, as the effect would have been anti-dilutive.

## Note 7: Subsequent Events

For purpose of disclosure in the unaudited consolidated financial statements, the Company has evaluated subsequent events through November 10, 2016, the date the unaudited consolidated financial statements were available to be issued. Except as discussed below, management is not aware of any material events that have occurred subsequent to the balance sheet date that would require adjustment to, or disclosure in the accompanying unaudited financial statements.

### ***Share Repurchase***

Subsequent to September 30, 2016, the Company repurchased, pursuant to the terms of its 2016 Stock Repurchase Program, approximately 1,036,000 additional shares at an average price of \$1.64 per share through November 10, 2016.

### ***Reverse Stock Split***

On October 26, 2016, the Company announced that it plans to hold a special meeting of shareholders on Wednesday, December 7, 2016 at 10:00 AM, EST, at the Wyndham Grand Jupiter at Harbourside Place, 122 Soundings Ave, Jupiter, FL 33477, to seek approval for a potential reverse stock split of Dyadic's common stock. The reverse stock split proposal includes a ratio ranging between 1-for-every-2 shares to 1-for-every-4 shares, to be determined by Dyadic's Board of Directors if such proposal is approved by shareholders.

The Board of Directors of Dyadic has fixed the close of business on October 21, 2016 as the record date for the determination of stockholders entitled to notice of, and to vote at, the special meeting and any adjournments or postponements thereof. The affirmative vote of a majority of the shares of our common stock outstanding on the record date will be required to approve the reverse stock split proposal.

### **Important Information about the Reverse Stock Split Proposal**

This communication may be deemed to be solicitation material in connection with the proposal to be submitted to Dyadic's shareholders at its special meeting seeking approval to authorize a reverse stock split (the "Reverse Stock Split Proposal").

A notice of the special meeting and a proxy statement to solicit the votes of Dyadic stockholders to approve the Reverse Split Proposal (the "Proxy Statement") was posted to Dyadic's website ([www.dyadic.com](http://www.dyadic.com)) and the OTC Marketplace Portal (<http://www.otcmarkets.com/stock/DYAI/filings>) on October 26, 2016 and subsequently mailed to Dyadic stockholders. Shareholders of Dyadic are urged to read the proxy statement and all other relevant documents filed with the OTC Markets, because they may contain important information about the Reverse Stock Split Proposal and Dyadic.

Dyadic and its Board of Directors and executive officers may be deemed to be participants in the solicitation of proxies from the holders of Dyadic common stock in respect of the Reverse Stock Split Proposal. Information about the directors and executive officers of Dyadic is set forth in Dyadic's proxy statement for its 2016 annual meeting of shareholders, which was filed with the OTC Markets on March 29, 2016. Investors may obtain additional information regarding the interest of Dyadic and its directors and executive officers in the Reverse Stock Split Proposal by reading the proxy statement relating to the special meeting.

### ***Item 4. Management's Discussion and Analysis of Financial Condition and Results of Operations***

The following discussion and analysis contains forward-looking statements about our plans and expectations of what may happen in the future. Forward-looking statements are based on a number of assumptions and estimates that are inherently subject to significant risks and uncertainties, and our results could differ materially from the results anticipated by our forward-looking statements as a result of many known or unknown factors, including, but not limited to, those factors discussed under the caption "Risk Factors" in this Quarterly Report for the three and nine months ended September 30, 2016, as well as our Annual Report for the year ended December 31, 2015, which was filed with the OTC Markets on March 29, 2016. See also the "Special Cautionary Notice Regarding Forward-Looking Statements" set forth at the beginning of this report.

You should read the following discussion and analysis in conjunction with the unaudited consolidated financial statements, and the related footnotes thereto, appearing elsewhere in this report, and in conjunction with management's discussion and analysis and the audited consolidated financial statements included in our Annual Report for the year ended December 31, 2015, which was filed with the OTC Markets on March 29, 2016.

We have reclassified the revenues and expenses of our industrial technology business to "income (loss) from discontinued operations" for all of the periods presented in the accompanying consolidated financial statements.

## **OVERVIEW**

### ***Description of Business***

Dyadic International, Inc. ("Dyadic", "we", or the "Company") is a global biotechnology company based in Jupiter, Florida with a foreign subsidiary, Dyadic Nederland, BV, which maintains a small satellite office in Wageningen, the Netherlands. Over the past two decades, the Company has developed a method for producing commercial quantities of enzymes and other proteins required for the production of industrial enzymes; and has successfully licensed this technology to third parties such as Abengoa Bioenergy, BASF, Codexis and others. This technology is based on the *Myceliophthora thermophila* fungus, which the Company nicknamed C1. The C1 technology is a robust and versatile fungal expression system for gene discovery, development, and production of enzymes and other proteins.

On December 31, 2015, the Company sold its industrial technology business to DuPont's (NYSE: DD) industrial biosciences business for \$75 million (the "DuPont Transaction"). The transaction included \$8 million of the purchase price to be held in escrow for 18 months to ensure Dyadic's obligations with respect to certain indemnity claims and working capital adjustments. The current escrow amount of \$7.4 million in the accompanying balance sheet is net of contractual working capital adjustments already agreed to by the parties. Please see details under caption "Escrowed Funds from Sale of Assets" under Note 1 to the Consolidated Financial Statements.

In connection with the DuPont Transaction, DuPont granted Dyadic co-exclusive rights to the C1 technology for use in human and animal pharmaceutical applications, with the exclusive ability to enter into sub-license agreements. DuPont retained certain rights to utilize the C1 technology for use in pharmaceutical applications, including the development and production of pharmaceutical products, for which it will make royalty payments to Dyadic upon commercialization. In certain circumstances, Dyadic may owe a royalty to either DuPont or certain licensor's of DuPont, depending upon whether Dyadic elects to utilize certain patents either owned by DuPont or licensed in by DuPont.

The Company is currently focusing on the biopharmaceutical industry and leveraging the patented and proprietary C1 expression system to help accelerate the development and production of biologic vaccines and drugs at flexible commercial scales for its use in the discovery, development, and manufacturing of human and animal vaccines, monoclonal antibodies, biosimilars and/or biobetters, and other therapeutic proteins.

The Company believes that the pharmaceutical sector is an attractive opportunity to potentially apply the C1 technology platform. The Company expects to continue utilizing a portion of the proceeds from the DuPont Transaction in combination with additional potential funding that is being sought from industry and government programs to further develop and optimize the C1 technology platform to become a safe and efficient expression system. In addition, the unique attributes of C1 may create attractive research, licensing, collaboration and other opportunities, if C1 demonstrates operational efficiencies and reduced capital requirements for biologic vaccines and drug manufacturers. The Company's primary objective is to position the C1 technology as the expression platform of choice in the development and production of commercial scale biologic vaccines and drugs. In particular, as the global population ages, Dyadic's vision is for C1 to improve the speed and efficiency and reduce the costs at which biologic vaccines and drugs are brought to market. This could improve access and lower the cost of drugs for patients and the health-care system, and most importantly, save lives.

The Company is making efforts to introduce and educate the biopharmaceutical industry and governmental agencies about the potential applicability of the C1 technology platform for use in developing and manufacturing biologic vaccines and drugs. Such efforts includes attending and making presentations to the biopharmaceutical industry at various conferences, as well as other business development and marketing efforts, to create the awareness of the potential benefits of applying the industrial proven C1 technology to enable the development and large scale manufacture of low cost proteins, which has the potential to be further developed into a safe and efficient expression system that may help speed up the development, production and performance of biologic vaccines and drugs at flexible commercial scales. Additionally, we have brought on a new board member and have hired consultants with both the experience and relationships within the pharmaceutical industry and governmental agencies to help us with these efforts. Specifically, the Company is focusing on the following research and development pharmaceutical programs:

#### ***Biologic Vaccine and Drug Programs***

We continue our participation in the existing EU-funded ZAPI vaccination program. ZAPI is a research and development program sponsored by the EU which aims to develop a suitable platform for the rapid development and production of vaccines and protocols to fast-track registration of product developed to combat epidemic Zoonotic diseases that have the potential to effect the human population. Some of the benefits we anticipate coming from a

successful outcome, if the C1 antigens are used throughout the ZAPI project, will be additional performance and safety data which we would expect to help us in our efforts to leverage the C1 expression system for use in developing and manufacturing recombinant vaccines for the animal health and human pharmaceutical industries.

In September 2016, the Company entered into a multi-year research and development agreement with an additional third party Contract Research Organization ("CRO") to begin to further modify and improve the Company's C1 technology for use in developing and manufacturing biologic vaccines and drugs. Management continues to evaluate how best to leverage the preliminary, but encouraging results, knowledge and experience, along with the meaningful improvements made to the C1 expression system during our prior research collaboration with Sanofi Pasteur (which ended on October 5th, 2016), across a number of biologic vaccine and drug development programs on our own, or in collaboration with other parties. The Company's developed C1 expressed proteins that were tested in mice trials by Sanofi Pasteur S.A. ("Sanofi"), produced data indicating that C1 technology produced antigen generated an equal, or better, immune response in mice than the standard antigen selected by Sanofi. The research carried out within the Sanofi project, along with our own research efforts enabled the Company to successfully demonstrate that our C1 technology is able to produce vaccines at relatively high levels, with the potential to improve therapeutic vaccine performance. We consider the experience and knowledge obtained from these research programs invaluable.

### ***Non-glycosylated Therapeutic Programs***

The Company has started internally funded exploratory research programs at (i) the Company's former research center in Wageningen, the Netherlands (acquired by DuPont as part of the DuPont Transaction in 2015), and (ii) within the multi-year research and development agreement with a third party Contract Research Organization to evaluate the use of the current C1 technology to develop non-glycosylated therapeutic products such as Insulin and ranibizumab, a biosimilar version of Lucentis, and is exploring carrying out additional research on internally funded projects and/or funded in whole or in part with third party industry and governmental agencies on other potential biomolecules.

- The Global human insulin market is estimated to reach \$42 billion by 2019, at a compound annual growth rate of 12.5% from 2014-2019. The market is being driven by the growing prevalence of diabetes worldwide, an aging population that increases the incidence of diabetes, growing obesity due to changing lifestyles, favorable government initiatives, and the introduction of pen and inhalation devices that deliver human insulin efficiently and effectively. We believe that the production of low cost insulin by C1 represents one of the largest potential opportunities for which C1 may be applied.
- Therapeutic antibodies for the treatment of retinal diseases, such as mAb-based biosimilars and ranibizumab, a biosimilar version of Lucentis, achieved global sales of approximately \$4.5 billion per IMS Health. Since the aging population continues to grow in developed and undeveloped countries there is an increasing need to deliver more medicines and therapies to more people around the world faster, in greater volumes and at lower cost. Producing non-glycosylated biosimilars, such as ranibizumab, by using the C1 Technology we can create a differentiated approach for a gene expression system as an effective alternative in the emerging biosimilar, bio-better global-market as it becomes more competitive.

### ***Glycosylated Therapeutic Programs***

The Company's longer term objective, which will require substantially more time and money to achieve, is to leverage the C1 expression host system for the even larger therapeutic glycoprotein market. The C1 system has the potential to become a significant platform for the development and production of therapeutic glycoproteins with human-compatible or even superior glycan structures. We believe that with the rapid advances already available today, and those being made at an accelerated pace in genomics and synthetic biology, and with the accelerated pace of new advancements being made, the hyper productive and novel C1 fungal cell line is a superior option to further engineer glycosylation pathways: (i) to create improved immunogenicity in the case of vaccines, or (ii) to eliminate immunogenicity in the case of glycoproteins as therapeutic drugs. The Company has and continues to evaluate the best strategies to conduct these critical research and development tasks. We are in discussions with various leading experts and laboratories in the field of glycoengineering to identify the best path forward to glycoengineer C1 cell lines. The additional CRO that the Company engaged at the end of the third quarter of 2016 will also focus on the glycoengineering of C1 for potential use in developing and manufacturing glycosylated antibodies.

Based on our academic and commercial collaborations, we believe experts in academia and industry regard Dyadic's C1 expression system as among the foremost expression systems in the world. We continue to review and evaluate our existing and new opportunities for internal and external pharmaceutical research and development projects



and collaborations. When the Company has successfully demonstrated C1's capabilities in developing biologics, it will consider setting up its own research and development site in furtherance of our business objectives.

We are optimistic about the impact that the C1 expression system may have on the development and manufacturing of biologic vaccines and drugs and that utilizing the C1 expression system may be the critical differentiator in allowing Dyadic, our collaborators and licensees to compete in these technology-driven markets. Most importantly, we believe biologics developed without the most productive expression system, such as C1, will face heightened reimbursement challenges.

### ***Recent Developments***

See *Item 7 Other Information* for information about certain recent developments regarding the Company's Board of Directors Changes, and Reverse Stock Split.

## ***CRITICAL ACCOUNTING POLICIES, ESTIMATES AND JUDGEMENTS***

The preparation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles ("GAAP") requires management to make estimates and judgments that affect the reported amount of assets and liabilities and related disclosure of contingent assets and liabilities at the date of our consolidated financial statements and the reported amounts of revenues and expenses during the applicable period. Actual results may differ from these estimates under different assumptions or conditions. Such differences could be material to the financial statements.

We define critical accounting policies as those that are reflective of significant judgments and uncertainties and which may potentially result in materially different results under different assumptions and conditions. In applying these critical accounting policies, our management uses its judgment to determine the appropriate assumptions to be used in making certain estimates. These estimates are subject to an inherent degree of uncertainty. Our critical accounting policies include the following:

### ***Revenue Recognition***

Revenue is recognized when (1) persuasive evidence of an arrangement exists; (2) services have been rendered or product has been delivered; (3) price to the customer is fixed and determinable; and (4) collection of the underlying receivable is reasonably assured.

The Company recognizes revenue from research funding under collaboration agreements when earned on a "proportional performance" basis as research hours are incurred or as milestones are achieved. The Company typically performs services as specified in each respective agreement on a best efforts basis, and is reimbursed based on contract terms and conditions under each contract. The Company initially defers revenue for any amounts billed and payments received in advance for services performed. The Company then recognizes revenue pursuant to the related pattern of performance, based on contract terms and conditions under each contract.

### ***Stock Compensation***

We have granted stock options and restricted stock to employees, directors and consultants. For employee and director grants, the value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model. The Black-Scholes model takes into account volatility in the price of our stock, the risk-free interest rate, the estimated life of the option, the closing market price of our stock and the exercise price. We base our estimates of our stock price volatility on the historical volatility of our common and our assessment of future volatility; however, these estimates are neither predictive nor indicative of the future performance of our stock. For purposes of the calculation, we assumed that no dividends would be paid during the life of the options and warrants. The estimates utilized in the Black-Scholes calculation involve inherent uncertainties and the application of management judgment. In addition, we are required to estimate the expected forfeiture rate and only recognize expense for those equity awards expected to vest. As a result, if other assumptions had been used, our recorded stock-based compensation expense could have been materially different from that reported. In addition, because some of the options and warrants issued to employees, consultants and other third-parties vest upon the achievement of certain milestones, the total expense is uncertain.

Total compensation expense for options and restricted stock issued to consultants is determined at the "measurement date." The expense is recognized over the vesting period for the options and restricted stock. Until the

measurement date is reached, the total amount of compensation expense remains uncertain. We record stock-based compensation expense based on the fair value of the equity awards at the reporting date. These equity awards are then revalued, or the total compensation is recalculated based on the then current fair value, at each subsequent reporting date. This results in a change to the amount previously recorded in respect of the equity award grant, and additional expense or a reversal of expense may be recorded in subsequent periods based on changes in the assumptions used to calculate fair value, such as changes in market price, until the measurement date is reached and the compensation expense is finalized.

### ***Accounting for Income Taxes***

In preparing our consolidated financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. This process involves management estimation of our actual current tax exposure and assessment of temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income and, to the extent we believe that recovery is not likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the consolidated statement of operations. Significant management judgment is required in determining our provision for income taxes, our deferred tax assets and liabilities and any valuation allowance recorded against our net deferred tax assets.

### ***Recent Accounting Pronouncements***

See Note 1 to the Consolidated Financial Statements for information about recent accounting pronouncements.

### ***Results of Operations***

#### ***Three and Nine Months Ended September 30, 2016 Compared to the Same Periods in 2015***

##### ***Revenue***

Research and development revenue for the three months ended September 30, 2016 decreased 100% compared to approximately \$213,500 for the same period a year ago. The decrease in revenue was due to the Company's termination of the R&D agreement with Sanofi Pasteur S.A. in August 2016.

Research and development revenue for the nine months ended September 30, 2016 decreased 64% to approximately \$101,800 compared to \$285,700 for the same period a year ago. The decrease in revenue for the period was due to the Company's termination of the R&D agreement with Sanofi Pasteur S.A. in August 2016.

##### ***Operating Expenses***

###### ***General and Administrative Expenses***

General and administrative expenses for the three months ended September 30, 2016 decreased 6% to approximately \$939,200 compared to \$1,000,600 for the same period a year ago. The decrease primarily reflects lower employee related costs due to the organizational downsizing in connection with the DuPont Transaction of \$232,300, professional service costs of \$114,700, and bad debt expense of \$66,000, partially offset by an increase in costs related to biopharmaceutical business development of \$137,800, an increase in executive compensation costs of \$105,700, litigation costs of \$56,100 and finance department compensation costs of \$52,600.

General and administrative expenses for the nine months ended September 30, 2016 decreased 9% to approximately \$2,923,100 compared to \$3,217,800 for the same period a year ago. The decrease primarily reflects lower employee related costs due to the organizational downsizing in connection with the DuPont Transaction of \$721,000, cost reimbursement received from DuPont for services rendered in the transition services agreement of \$195,600, litigation and M&A professional service costs of \$97,400, and bad debt expense of \$66,000, partially offset by an increase in cost related to new employment agreements for executives of \$309,700, non-cash stock compensation in connection with the Special Committee of the Board and board compensation of \$239,300, as well as increase in the biopharmaceutical business development costs of \$138,300 and finance department compensation costs of \$106,900.

### ***Research and Development***

Research and development expenses from continuing operations for the three and nine months ended September 30, 2016 increased to approximately \$369,400 and \$963,700 compared to \$0 and \$0, respectively, for the same periods a year ago. The increase reflects the R&D employee costs and service agreement with DuPont to support our ongoing biopharmaceutical and internally funded projects, and other governmental and commercial projects.

### ***Foreign Currency Transaction Gain or Loss***

The Company's foreign currency transaction gain or loss, for the nine months ended September 30, 2016 was a gain of appropriately \$78,600 compared to a loss of \$105,500 for the same period a year ago. The change represents the strengthening of the US dollar in comparison to the Euro.

### ***Settlement of Litigation***

On April 19, 2016, the Company received an amount of approximately \$2.1 million, in connection with the Company's settlement with one of the two remaining defendant law firms, Bilzin Sumberg Baena Price & Axelrod LLP, in its ongoing professional liability litigation. The Company recorded such amount as a gain on settlement of litigation, net of legal fees and expenses, in the second quarter of 2016.

### ***Interest Income***

Interest income for the three and nine months ended September 30, 2016 increased to approximately \$146,900 and \$344,000 compared to \$2,600 and \$8,700, respectively for the same periods a year ago. The increase in interest income was related to the Company's investments in debt securities.

### ***Income Tax***

The Company has net operating loss ("NOL") carryforwards available in 2016 that will begin to expire in 2034. As of September 30, 2016 and December 31, 2015, the Company had NOLs in the amount of approximately \$4.9 million and \$5.8 million, respectively.

For the nine months ended September 30, 2016, the Company recorded a current provision for income tax of \$184,439 for adjustments related to our 2015 tax return.

The deferred tax assets as of September 30, 2016 and December 31, 2015 were approximately \$3.3 million and \$2.0 million, respectively. Due to the Company's history of operating losses and the uncertainty regarding our ability to generate taxable income in the future, the Company has established a 100% valuation allowance against deferred tax assets as of September 30, 2016 and December 31, 2015.

## ***LIQUIDITY AND CAPITAL RESOURCES***

Historically, the Company has financed its operations primarily with proceeds from its industrial enzyme business, upfront fees from licensing of technology, external borrowings, borrowings from its stockholders, sales of common equity securities, and the receipt of settlement proceeds from its ongoing lawsuit against the Company's former outside legal counsel.

Our primary future cash needs are expected to be concentrated on operating activities, including working capital and R&D expenses. In addition, we may use cash to repurchase additional shares of our common stock under our \$15 million share repurchase program. We believe our existing cash position and investments in debt securities will be adequate to meet our operational, business, and other liquidity requirements in the next twelve months.

On April 5, 2016, the Company reached a settlement with one of the two remaining defendant law firms, Bilzin Sumberg Baena Price & Axelrod LLP, in its ongoing professional liability litigation. On April 19, 2016, the Company received full payment in the amount of \$2,100,000, which is net of legal fees and expenses. The settlement amount was reported in the Company's consolidated statement of operations, in other income, for the quarter ended June 30, 2016. In the event the Company is able to reach a favorable settlement with the remaining defendant law firm Greenberg Traurig, LLP, Greenberg Traurig, P.A. (collectively, "Greenberg Traurig") and the estate of Robert I Schwimmer in its ongoing Professional Liability litigation, this will provide the Company with additional capital. We expect to incur

additional costs in what may be a long and protracted trial, the outcome of which is uncertain. If we do not prevail at trial, the court may determine that the Company is responsible for some or all of the defendants' costs incurred in this litigation. Additionally, even if we prevail at trial, we expect the defendants to appeal the decision. See in Note 3: Commitments and Contingencies - *Professional Liability Lawsuit*, and *Item 5. Legal Proceedings* for additional information.

At September 30, 2016, cash and cash equivalents were approximately \$5.8 million compared to \$68.6 million at December 31, 2015. Cash used in the nine months ended September 30, 2016 of approximately \$62.8 million primarily reflects stock repurchases net of stock issuances of approximately \$9.5 million, purchase of investment grade securities at face value, net of repayments and maturities of approximately \$48.7 million, and cash used in operating activities of approximately \$4.6 million which includes cash used in operations of approximately \$3.6 million, payment of DuPont Transaction related liabilities of approximately \$2.0 million, and premiums and interest paid for investment grade securities of approximately \$1.1 million, offset by cash received from the litigation settlement of approximately \$2.1 million.

Net cash used in operating activities for the nine months ended September 30, 2016 of approximately \$4,536,000 was principally attributable to a net loss of approximately \$1,546,600, investment securities premium and interest, net of amortization of approximately \$1,372,400, and changes in operating assets and liabilities of approximately \$2,155,500 primarily related to the pay out of payables related to DuPont transition services agreement and accrued employment termination costs, offset by stock based compensation expenses of approximately \$538,500.

Net cash provided by operating activities for the nine months ended September 30, 2015 of approximately \$1,914,000 was principally attributable to a net loss of approximately \$1,106,400 and changes in operating assets and liabilities of approximately \$236,700, offset by stock based compensation expenses of approximately \$365,800 and cash provided by discontinued operations of approximately \$678,600.

Net cash used in investing activities for the nine months ended September 30, 2016 of approximately \$48.7 million was primarily used for purchase of investment securities.

Net cash used in investing activities for the nine months ended September 30, 2015 of approximately \$142,100 was attributable to the cash used in discontinued operations.

Net cash used in financing activities for the nine months ended September 30, 2016 of approximately \$9.5 million was principally attributable to repurchase of common stock of \$9.7 million offset by the issuance of common stock of \$100,000 and the proceeds received from outstanding stock subscriptions of approximately \$40,600.

Net cash provided by financing activities for the nine months ended September 30, 2015 of approximately \$2,048,800 was principally attributable to the cash proceeds from the private placement of convertible debt in the amount of \$2.0 million and the repayment of stock subscriptions of approximately \$90,800, offset by the repayment of convertible debt of \$50,000.

## ***Item 5. Legal Proceedings***

### ***Professional Liability Lawsuit***

See Note 3 to the Consolidated Financial Statements for information on legal proceeding regarding the professional liability lawsuits.

The Company is also subject to legal proceedings, asserted claims and investigations in the ordinary course of business, including from time to time commercial claims, employment and other matters, which management considers immaterial, individually and in the aggregate. The Company makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. The requirement for these provisions are reviewed at least quarterly and adjusted to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case. Litigation is inherently unpredictable and costly. While the Company believes that it has valid defenses with respect to the legal matters pending against it, protracted litigation and/or an unfavorable resolution of one or more of such proceedings, claims or investigations against the Company could have a material adverse effect on the Company's consolidated financial position, cash flows or results of operations.

## ***Item 6. Defaults upon Senior Securities***

None.

## ***Item 7. Other Information***

### ***Quantitative and Qualitative Disclosures about Market Risk***

The primary objective of our investment activities is to preserve principal while maximizing our income from investments and minimizing our market risk. We currently invest in government and investment-grade corporate debt in accordance with our investment policy, which we may change from time to time. The securities in which we invest have market risk. This means that a change in prevailing interest rates, and/or credit risk, may cause the fair value of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later rises, the fair value of our investment will probably decline. As of September 30, 2016, our portfolio of financial instruments consists of cash equivalents, including money market funds. As of September 30, 2016, due to the short-term nature of these financial instruments, we believe there is no material exposure to interest rate risk, and/or credit risk, arising from our portfolio of financial instruments.

### ***Risk Factors***

***The Company relies on access to third-party contract research organizations (the "CRO's"), which may not be available to the Company on commercially reasonable terms or at all.***

The Company contracts with a number of third parties to conduct research and development projects, which include services and programs in connection with the modification and enhancement of the Company's C1 expression platform for use in the pharmaceutical applications. The licensing and service arrangements with these third parties CRO's do not guarantee the continuation or renewal of these arrangements on reasonable terms, if at all. The Company may be unable to continue to maintain its existing access to, and/or expand access if necessary to third party CRO's to conduct our research projects. Failure to maintain and expand access to certain third party CRO's could have a material adverse impact on the Company's research projects, financial condition and operating results.

Investing in our common stock involves a high degree of risk. You should carefully consider all of the matters described in this Quarterly Report for the three and nine months ended September 30, 2016 and the "risk factors" included herein and in our December 31, 2015 Annual Report filed with the OTC Markets on March 29, 2016, which is incorporated herein by reference, in evaluating our current business and future performance. We cannot assure you that any of the events discussed in the risk factors will not occur. If we are not able to successfully address any of the risks or difficulties, we could experience significant changes in our business, operations and financial performance. In such circumstances, the trading price of our common stock could decline, and in some cases, such declines could be significant and you could lose part or all of your investment. In addition to the risks, other unforeseeable risks and uncertainties or factors that we currently believe are immaterial may also adversely affect our operating results, and there may be other risks that may arise in the future. Certain statements contained in this Quarterly Report for the three and nine months ended September 30, 2016 constitute forward-looking statements. Please refer to the section entitled "Special Cautionary Notice Regarding Forward-Looking Statements" appearing on page 3 of this Quarterly Report for important limitations and guidelines regarding reliance on forward-looking statements.

### ***Off-Balance Sheet Arrangements***

We do not have any off-balance sheet arrangements.

### ***Board of Directors Changes***

On January 18, 2016, Robert D. Burke, MD resigned from the board of directors and all related board committees to which he served which included the compensation, and nominating committees of the board. Dr. Burke served on the board of directors since June 2008.

On January 19, 2016, our board of directors approved the formation of a compensated Special Committee to address the advisory needs of the Company in connection with the Company's ongoing litigation against former legal counsel and biopharmaceutical business development. The role of the Special Committee would be to serve as a resource

to management with respect to the foregoing matters, but that all decisions with respect to such matters would be subject to the Board review and approval following a presentation by the Special Committee.

On March 15, 2016, our board of directors revised our director compensation policy to return to 100% cash compensation instead of 80% cash and 20% restricted stock, effective January 1, 2016. Directors who are also employees or officers of the Company or any of its subsidiaries do not receive any separate compensation as a director. Non-employee directors receive an annual retainer for board service of \$36,000, paid in equal monthly installments. A director serving as Chairman of the Board shall also receive an additional annual retainer of \$12,000, paid in equal monthly installments. An independent director who serves as Chair of the Company's Audit Committee shall also receive an additional annual retainer of \$9,600, paid in equal monthly installments.

In June 2016, our board of directors reevaluated our director compensation plan, taking into consideration of benchmark comparisons of board compensation and our reduced internal resources after the DuPont Transaction. In anticipation of the workload demands and time commitments expected of board members in 2016 and 2017, the Company increased each board member's cash compensation from a base of \$3,000 per month to \$5,000 per month beginning July 1, 2016, and the annual stock option award was increased from 25,000 options to 50,000 options retroactively to the beginning of 2016. Accordingly, additional 25,000 stock options were granted to each board member on June 7, 2016.

On August 16, 2016, the Company announced the appointment of Arindam Bose, Ph.D., to its board of directors, effective August 15, 2016.

#### ***Reverse Stock Split Plan***

See Note 7 Subsequent Events to the Consolidated Financial Statements for details.

#### ***Item 8. Exhibits***

None

*Item 9. Certifications*

**Certification**

I, Mark A. Emalfarb, certify that:

1. I have reviewed the Information and Quarterly Report, exhibits, and all notes thereto of Dyadic International, Inc.;
2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this Quarterly Report.

Dated November 10, 2016

\_\_\_\_\_/s/ Mark A. Emalfarb

By: Mark A. Emalfarb  
Title: President and Chief Executive Officer

**Certification**

I, Thomas L. Dubinski, certify that:

1. I have reviewed the Information and Quarterly Report, exhibits, and all notes thereto of Dyadic International, Inc.;
2. Based on my knowledge, this Quarterly Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Quarterly Report; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this Quarterly Report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this Quarterly Report.

Dated November 10, 2016

\_\_\_\_\_/s/ Thomas L. Dubinski

By: Thomas L. Dubinski  
Title: Vice President and Chief Financial Officer