

**Prospectus**

**SKYLINE MEDICAL INC.**

**78,709,975 shares of common stock**

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This prospectus covers the resale by the selling stockholders of up to 78,709,975 shares of our common stock, \$.01 par value, including 15,807,692 shares issuable as “Preferred Conversion Shares”, as defined herein, 423,560 shares to be issued as dividends on shares of preferred stock, 36,047,701 shares issuable upon the conversion of convertible promissory notes, and 26,431,022 shares issuable upon the exercise of warrants.

These securities will be offered for sale from time to time by the selling stockholders identified in this prospectus in accordance with the terms described in the section of this prospectus entitled “Plan of Distribution.” The selling stockholders participating in the distribution of the shares of common stock and any broker-dealers participating in the distribution of the shares of common stock will be deemed to be “underwriters” within the meaning of the Securities Act, and any commission paid, or any discounts or concessions allowed to, any such broker-dealer may be deemed to be underwriting commissions or discounts under the Securities Act. We will not receive any of the proceeds from the sale of the common stock by the selling stockholders. However, we will receive the proceeds of any cash exercise of the warrants, and the conversion of any notes will reduce the outstanding principal and/or interest amount of certain indebtedness. Any proceeds received from the exercise of the warrants will be used for working capital and general corporate purposes.

Our securities are not listed on any national securities exchange. Our common stock is currently quoted on the OTCQB marketplace under the symbol “SKLN.QB.” The last reported per share price for our common stock was \$0.1265, as quoted by the OTCQB marketplace on September 4, 2014.

**INVESTING IN OUR COMMON STOCK INVOLVES A HIGH DEGREE OF RISK. SEE “RISK FACTORS” BEGINNING ON PAGE 3.**

**NEITHER THE SECURITIES AND EXCHANGE COMMISSION NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR DETERMINED IF THIS PROSPECTUS IS TRUTHFUL OR COMPLETE. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.**

**The date of this prospectus is September 8, 2014**

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**PROSPECTUS SUMMARY**

*This summary contains basic information about us and this offering. You should read the entire prospectus carefully, especially the risks of investing in our common stock discussed under “Risk Factors.” Some of the statements contained in this prospectus, including statements under this summary and “Risk Factors”, are forward-looking statements and may involve a number of risks and uncertainties. We note that our actual results and future events may differ significantly based upon a number of factors. You should not put undue reliance on the forward-looking statements in this document, which speak only as of the date on the cover of this prospectus.*

*References to “we,” “our,” “us,” the “Company,” or “Skyline” refer to Skyline Medical Inc., a Delaware corporation.*

**Our Business**

The Company was originally incorporated on April 23, 2002 in Minnesota as BioDrain Medical, Inc. Effective August 6, 2013, the Company changed its name to Skyline Medical Inc. Pursuant to an Agreement and Plan of Merger dated effective December 16, 2013, the Company merged with and into a Delaware corporation with the same name that was its wholly-owned subsidiary, with such Delaware Corporation as the surviving corporation of the merger.

**Financial Results; Ability to Continue as a Going Concern**

Our financial statements for the periods ended June 30, 2014 and June 30, 2013 and the years ended December 31, 2013 and 2012 are included in this prospectus. In the six months ended June 30, 2014 and 2013, we had \$388,513 and \$278,583 in revenues, respectively, and approximately \$3.4 million and \$3.3 million in net loss, respectively. In 2013 and 2012, we had \$468,125 and \$188,772 in revenues, respectively, and approximately \$9.4 million and \$7.4 million in net loss, respectively. We have approximately \$3,500,000 in debts, liabilities and cash obligations that become due in 2014. The Company has suffered recurring losses from operations and has a stockholders’ deficit. Although we have been able to fund our current working capital requirements, principally through debt and equity financing, there is no assurance that we will be able to do so in the future. These factors raise substantial doubt about our ability to continue as a going concern. As a result of the above factors, our independent registered public accounting firm has indicated in their audit opinion, contained in our financial statements included in this prospectus that they have serious doubts about our ability to continue as a going concern. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Plan of Financing; Going Concern Qualification.”

**Risks Affecting Our Business**

We are subject to a number of risks, which you should be aware of before deciding to purchase the securities in this offering. These risks are discussed in the section titled “Risk Factors.”

**General Information**

Our address is 2915 Commers Drive, Suite 900, Eagan, Minnesota 55121. Our telephone number is (651) 389-4800, and our website address is [www.skylinemedical.com](http://www.skylinemedical.com).

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**The Offering**

We are registering 78,709,975 shares of our common stock, including 15,807,692 shares issuable upon the conversion of the Preferred Shares (as defined herein) (“Preferred Conversion Shares”), 423,560 shares to be issued as dividends on Preferred Shares, 36,047,701 shares issuable upon the conversion of convertible promissory notes, and 26,431,022 shares issuable upon the exercise of warrants, in each case for sale by the selling stockholders identified in the section of this prospectus entitled “Selling Stockholders.” See “Plan of Distribution.” We will not receive any of the proceeds from the sale of the common stock by the selling stockholders. However, we will receive the proceeds of any cash exercise of the warrants, and the conversion of any notes will reduce the outstanding principal and/or interest amount of certain indebtedness. Any proceeds received from the exercise of the warrants will be used for working capital and general corporate purposes. Information regarding our common stock is included in the section of this prospectus entitled “Description of Securities.”

## RISK FACTORS

*You should carefully consider the risks described below before making an investment decision. Our business could be harmed by any of these risks. The trading price of our common stock could decline due to any of these risks, and you may lose all or part of your investment. In assessing these risks, you should also refer to the other information contained in this prospectus, including our financial statements and related notes.*

### **Risks Related to Our Business**

***We will require additional financing to sustain our operations, and if adequate financing is not available, we may be forced to go out of business. Such financing will be dilutive and feature restricted terms. Our independent public accounting firm has indicated in their audit opinion, contained in our financial statements, that they have serious doubts about our ability to remain a going concern.***

We have never generated sufficient revenues to fund our capital requirements. We have funded our operations through a variety of debt and equity instruments. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Historical Financing” below. Our future cash requirements and the adequacy of available funds depend on our ability to sell our products. See “Plan of Financing; Going Concern Qualification” below.

In February 2014, we raised \$2.0 million in gross proceeds from our private placement of convertible preferred stock and warrants. In July and August 2014, we sold convertible notes and warrants for an aggregate purchase price of over \$0.9 million. We may enter into purchase agreements for further sales of convertible notes and warrants.

We expect that we will need further equity financing to maintain our operations, including further sales of convertible notes and warrants and possibly other financing. If such financing is available, it may be highly dilutive to our existing shareholders and may otherwise include burdensome or onerous terms. Our inability to raise additional working capital at all or to raise it in a timely manner would negatively impact our ability to fund our operations, to generate revenues, and to otherwise execute our business plan, leading to the reduction or suspension of our operations and ultimately forcing us to declare bankruptcy, reorganize or to go out of business. Should this occur, the value of any investment in our securities could be adversely affected, and an investor would likely lose all or a significant portion of their investment. These factors raise substantial doubt about our ability to continue as a going concern.

Based on our current operating plan we believe that we have sufficient cash, cash equivalents and short-term investment balances to last approximately through September 30, 2014 after which additional financing will be needed to continue to satisfy our obligations. While holders of our warrants could exercise and provide cash to us during that time frame, we are not depending on that in our fundraising efforts. We commenced sales of our enhanced STREAMWAY in the first quarter of 2014. Sales of this product are expected to provide additional operating revenues and cash balances that could reduce the need for additional fundraising; however, cash collections for product sales are not immediate, which may result in a delay in positive operating cash flows over the next several quarters.

As a result of the above factors, our independent registered public accountant firm has indicated in their audit opinion, included herein, that they have serious doubts about our ability to continue as a going concern. The financial statements included herein have been prepared assuming the Company will continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

### ***Our limited operating history makes evaluation of our business difficult.***

We were formed on April 23, 2002 and to date have generated only moderate though increasing revenue year by year. Our ability to implement a successful business plan remains unproven and no assurance can be given that we will ever generate sufficient revenues to sustain our business. We believe the increase in sales in December 2012 and December 2013 may indicate that our business plan is on the right track, but we have a limited operating history which makes it difficult to evaluate our performance. You must consider our prospects in light of these risks and the expenses, technical obstacles, difficulties, market penetration rate and

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delays frequently encountered in connection with the development of new businesses. These factors include uncertainty whether we will be able to:

- Raise capital;
- Develop and implement our business plan in a timely and effective manner;
- Be successful in uncertain markets;
- Respond effectively to competitive pressures;
- Successfully address intellectual property issues of others;
- Protect and expand our intellectual property rights; and
- Continue to develop and upgrade our products.

***Our business is dependent upon proprietary intellectual property rights, which if we were unable to protect, could have a material adverse effect on our business.***

We rely on a combination of patent, trade secret and other intellectual property rights and measures to protect our intellectual property. We currently own and may in the future own or license additional patent rights or trade secrets in the U.S., Europe, Asia, Canada, and elsewhere in the world that cover certain of our products. We rely on patent laws and other intellectual property laws, nondisclosure and other contractual provisions and technical measures to protect our products and intangible assets. These intellectual property rights are important to our ongoing operations and no assurance can be given that any measure we implement will be sufficient to protect our intellectual property rights. Also, with respect to our trade secrets and proprietary know-how, we cannot be certain that the confidentiality agreements we have entered into with consultants, vendors and employees will not be breached, or that we will have adequate remedies for any breach. We may lose the protection afforded by these rights through patent expirations, legal challenges or governmental action. If we cannot protect our rights, we may lose our competitive advantage if these patents were found to be invalid in the jurisdictions in which we sell or plan to sell our products. The loss of our intellectual property rights could have a material adverse effect on our business.

***If we become subject to intellectual property actions, this could hinder our ability to deliver our products and services and our business could be negatively impacted.***

We may be subject to legal or regulatory actions alleging intellectual property infringement or similar claims against us. Companies may apply for or be awarded patents or have other intellectual property rights covering aspects of our technologies or businesses. Moreover, if it is determined that our products infringe on the intellectual property rights of third parties, we may be prevented from marketing our products. While we are currently not subject to any material intellectual property litigation, any future litigation alleging intellectual property infringement could be costly, particularly in light of our limited resources. Similarly, if we determine that third parties are infringing on our patents or other intellectual property rights, our limited resources may prevent us from litigating or otherwise taking actions to enforce our rights. Any such litigation or inability to enforce our rights could require us to change our business practices, hinder or prevent our ability to deliver our products and services, and result in a negative impact to our business. Expansion of our business via product line enhancements or new product lines to drive increased growth in current or new markets may be inhibited by the intellectual property rights of our competitors and/or suppliers. Our inability to successfully mitigate those factors may significantly reduce our market opportunity and subsequent growth.

***We face significant competition, including competition from companies with considerably greater resources than ours, and if we are unable to compete effectively with these companies, our market share may decline and our business could be harmed.***

Our industry is highly competitive with numerous competitors ranging from well-established manufacturers to innovative start-ups. A number of our competitors have significantly greater financial, technological, engineering, manufacturing, marketing and distribution resources than we do. Their greater capabilities in these areas may enable them to compete more effectively on the basis of price and production and more quickly develop new products and technologies.

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We estimate that the total market for surgical suction canisters is approximately \$100 million and has a compound annual growth rate of 5%. We estimate the total cost of using surgical canisters is a multiple of \$100 million because this amount does not include the labor to handle the canisters, disposal costs and solidifying compounds commonly used to minimize exposure to health care workers. Cardinal Health, Inc., a \$90 billion plus medical manufacturer and distributor, is a leading competitor. Another one of our competitors is Stryker Instruments, a wholly owned subsidiary of Stryker Corporation, which is a publicly traded company with revenues of approximately \$8 billion, and has a leading position in this market. Cardinal Health, Inc. has the Saf-T Pump that accommodates Medi-Vac suction canisters draining infectious fluid into the hospital sanitary sewer; the canisters must be brought to the system for draining. Both of these competitors are better capitalized than we are.

Although the Skyline STREAMWAY™ FMS is directly connected to the sanitary sewer, helping to reduce potential exposure to infectious fluids, it is possible that installation of the system will cause inconvenience and lost productivity as the operating rooms in which they are installed will need to be temporarily shut down. In addition, remodel work may be necessary in preparation for, or as a result of, an installation. In some cases, the costs to rework plumbing lines to accommodate our system may outweigh the expected savings and/or lengthen the expected return on investment time.

Companies with significantly greater resources than ours may be able to reverse engineer our products and/or circumvent our intellectual property position. Such action, if successful, would greatly reduce our competitive advantage in the marketplace.

We believe that our ability to compete successfully depends on a number of factors, including our technical innovations of unlimited suction and unlimited capacity capabilities, our innovative and advanced research and development capabilities, strength of our intellectual property rights, sales and distribution channels and advanced manufacturing capabilities. We plan to employ these and other elements as we develop our products and technologies, but there are many other factors beyond our control. We may not be able to compete successfully in the future, and increased competition may result in price reductions, reduced profit margins, loss of market share and an inability to generate cash flows that are sufficient to maintain or expand our development and marketing of new products, which could adversely impact the trading price of the shares of our common stock.

***Our products require FDA clearance and our business will be subject to intense governmental regulation and scrutiny, both in the U.S. and abroad.***

In March 2009, we filed a 510(k) submission with the FDA with respect to a product classification as a Class II non-exempt device. We cannot generate revenues from our product to be used in the surgical operating room without FDA clearance. We received written confirmation of final FDA clearance on April 1, 2009.

The potential production and marketing of some of our products, our ongoing research and development, any pre-clinical testing and clinical trial activities are subject to extensive regulation and review by FDA and other governmental authorities both in the United States and abroad. In addition to testing and approval procedures, extensive regulations also govern marketing, manufacturing, distribution, labeling, and record keeping. If we do not comply with applicable regulatory requirements, violations could result in warning letters, non-approvals, suspensions of regulatory approvals, civil penalties and criminal fines, product seizures and recalls, operating restrictions, injunctions, and criminal prosecution.

Periodically, legislative or regulatory proposals are introduced that could alter the review and approval process relating to medical products. It is possible that the FDA will issue additional regulations further restricting the sale of our present or proposed products. Any change in legislation or regulations that govern the review and approval process relating to our current and future products could make it more difficult and costly to obtain approval for new products, or to produce, market, and distribute existing products.

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***Our product has only recently entered the commercial market and, although we anticipate market acceptance, we do not have enough customer experience with it to predict future demands.***

The Skyline FMS has been launched into the fluid management market. We are currently manufacturing the Product, following GMP compliance regulations, at our own facility and anticipate the capability of producing the Skyline FMS in sufficient quantities for future near term sales. We have contracted with a manufacturing company that fits our standards and costs. We have sold and installed more than 56 FMS Systems to date and the product has been proven attractive to the target market due to its continuous suction and unlimited capacity ability, but other unknown or unforeseen market requirements may arise.

***If our product is not accepted by our potential customers, it is unlikely that we will ever become profitable.***

The medical industry has historically used a variety of technologies for fluid waste management. Compared to these conventional technologies, our technology is relatively new, and the number of companies using our technology is limited. The commercial success of our product will depend upon the widespread adoption of our technology as a preferred method by hospitals and surgical centers. In order to be successful, our product must meet the technical and cost requirements for these facilities. Market acceptance will depend on many factors, including:

- the willingness and ability of customers to adopt new technologies;
- our ability to convince prospective strategic partners and customers that our technology is an attractive alternative to conventional methods used by the medical industry;
- our ability to select and execute agreements with effective distributors and manufacturers representatives to market and sell our product; and
- our ability to assure customer use of the Skyline proprietary cleaning fluid and in-line filter.

Because of these and other factors, our product may not gain market acceptance or become the industry standard for the health care industry. The failure of such companies to purchase our products would have a material adverse effect on our business, results of operations and financial condition.

***We are dependent for our success on a few key executive officers. Our inability to retain those officers would impede our business plan and growth strategies, which would have a negative impact on our business and the value of an investment.***

Our success depends on the skills, experience and performance of key members of our management team. We heavily depend on our management team; Joshua Komberg, our President and Chief Executive Officer and Interim Chairman of the Board, David Johnson our Chief Operating Officer and Bob Myers our Chief Financial Officer. We have entered into employment agreements with all members of our senior management team and we may expand the relatively small number of executives in our company. Were we to lose one or more of these key individuals, we would be forced to expend significant time and money in the pursuit of a replacement, which could result in both a delay in the implementation of our business plan and the diversion of our limited working capital. We can give you no assurance that we can find satisfactory replacements for these key individuals at all, or on terms that are not unduly expensive or burdensome to our company. However, we have issued stock options and other equity-based compensation to attract and retain employees, and are confident that our team is committed to the products success.

***Our success is dependent on our ability to attract and retain technical personnel, sales and marketing personnel, and other skilled management.***

Our success depends to a significant degree on our ability to attract, retain and motivate highly skilled and qualified personnel. Failure to attract and retain necessary technical, sales and marketing personnel and skilled management could adversely affect our business. If we fail to attract, train and retain sufficient numbers of these highly qualified people, our prospects, business, financial condition and results of operations will be materially and adversely affected.



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### ***The relative lack of public company experience of our management team may put us at a competitive disadvantage.***

Our early management team had limited public company experience, which have impaired our ability to comply with legal and regulatory requirements such as those imposed by the Sarbanes-Oxley Act of 2002. The individuals who now constitute our senior management have had substantially more responsibility for managing publicly traded companies. Such responsibilities include complying with federal securities laws and making required disclosures on a timely basis. Our senior management team has been able to implement and affect programs and policies in an effective and timely manner that adequately responds to such increased legal, regulatory compliance and reporting requirements. However, our failure to do so could lead to the imposition of fines and penalties and result in the deterioration of our business.

### ***Costs incurred because we are a public company may affect our profitability.***

As a public company, we incur significant legal, accounting, and other expenses, and we are subject to the SEC's rules and regulations relating to public disclosure that generally involve a substantial expenditure of financial resources. In addition, the Sarbanes-Oxley Act of 2002, as well as rules subsequently implemented by the SEC, requires changes in corporate governance practices of public companies. We expect that full compliance with such rules and regulations will significantly increase our legal and financial compliance costs and make some activities more time-consuming and costly, which may negatively impact our financial results. To the extent our earnings suffer as a result of the financial impact of our SEC reporting or compliance costs, our ability to develop an active trading market for our securities could be harmed.

### **Risks Related to Our Securities**

#### ***Since our inception, a majority of our shares and other securities have been issued in violation of the preemptive rights of existing shareholders, which could result in claims against us.***

In 2013, it was brought to the attention of our management and board of directors that our company was subject to preemptive rights prior to its reincorporation in Delaware. The Minnesota Business Corporation Act (the "Act") provides such rights to shareholders of a corporation, unless the corporation's articles of incorporation "opt out" and deny them. Our company's articles of incorporation never denied preemptive rights or mentioned them in any way. Since our inception in 2002, our company has issued shares of common stock and other equity securities on numerous occasions to raise capital and for other purposes and, to our knowledge; we have never complied with the Minnesota preemptive rights statute in connection with such issuances. On December 16, 2013, the reincorporation merger became effective. From that date, stockholders no longer have preemptive rights relating to any future issuances of securities. As described in our Form 10-Q report for the quarter ended September 30, 2013 in Part II, Item 1A, "Risk Factors," in connection with previous issuances of securities, we may be subject to the claims of previous and current shareholders based on violations of their preemptive rights; the risk and magnitude of these claims are uncertain, because there is little legal authority on the application of the Minnesota preemptive rights statute and if there are any future claims, we intend to vigorously defend based in part on numerous facts and circumstances described in such Form 10-Q report and other factors. However, if current or former shareholders bring claims against the company for violations of preemptive rights, there can be no assurance that our company will not be liable for damages, the amount of which cannot be predicted. Further, in connection with any such claims, a court may grant other remedies that will have a material adverse effect on our company's financial condition or results of operations, or that will result in dilution to some existing shareholders.

#### ***There is currently a limited public trading market for our common stock and we cannot assure you that a more active public trading market for our common stock will develop or be sustained. Even if a market further develops, you may be unable to sell at or near ask prices or at all if you need to sell your shares to raise money or otherwise desire to liquidate your shares.***

There is currently a limited public trading market for our registered common stock. The numbers of institutions or persons interested in purchasing our registered common stock at or near ask prices at any given time may be relatively small or nonexistent. This situation may be attributable to a number of factors, including the fact that we are a small company that is relatively unknown to stock analysts, stock brokers,

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institutional investors and others in the investment community that generate or influence sales volume, and that even if we came to the attention of such persons, they tend to be risk averse and may be reluctant to follow a relatively unproven company such as ours or purchase or recommend the purchase of our shares until such time as we become more seasoned and viable. As a consequence, there may be periods of several days or more when trading activity in our shares is minimal or non-existent, as compared to a seasoned issuer which has a large and steady volume of trading activity that will generally support continuous sales without an adverse effect on share price. We cannot assure you that an active public trading market for our registered common stock will develop or be sustained.

***Limitations on director and officer liability and indemnification of our officers and directors by us may discourage shareholders from bringing suit against a director.***

Our certificate of incorporation and bylaws provide, with certain exceptions as permitted by governing state law, that a director or officer shall not be personally liable to us or our shareholders for breach of fiduciary duty as a director, except for acts or omissions which involve intentional misconduct, fraud or knowing violation of law, or unlawful payments of dividends. These provisions may discourage shareholders from bringing suit against a director for breach of fiduciary duty and may reduce the likelihood of derivative litigation brought by shareholders on our behalf against a director. In addition, our certificate of incorporation and bylaws may provide for mandatory indemnification of directors and officers to the fullest extent permitted by governing state law.

***We do not expect to pay dividends for the foreseeable future, and we may never pay dividends.***

We currently intend to retain any future earnings to support the development and expansion of our business and do not anticipate paying cash dividends in the foreseeable future. Our payment of any future dividends will be at the discretion of our Board of Directors after taking into account various factors, including but not limited to, our financial condition, operating results, cash needs, growth plans and the terms of any credit agreements that we may be a party to at the time. In addition, our ability to pay dividends on our common stock may be limited by state law. Accordingly, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize certain returns on their investment.

The Company completed a private offering in February 2014 issuing Series A Convertible Preferred Stock paying dividends at 6% of the Stated Value per annum on a quarterly basis (see “Subsequent Events” in Note 1 to the Consolidated Financial Statements included in this prospectus).

***Our stock may be thinly traded.***

Our common stock has been thinly traded, meaning there has been a low volume of buyers and sellers of the shares. Through this registration statement, we went public without the typical initial public offering procedures which usually include a large selling group of broker-dealers who may provide market support after going public. Thus, we will be required to undertake efforts to develop market recognition and support for our shares of common stock in the public market. The price and trading volume of our registered common stock cannot be assured. The numbers of institutions or persons interested in purchasing our registered common stock at or near ask prices at any given time may be relatively small or non-existent. This situation may be attributable to a number of factors, including the fact that we are a small company which is relatively unknown to stock analysts, stock brokers, institutional investors and others in the investment community that generate or influence sales volume, and that even if we came to the attention of such persons, they tend to be risk-averse and would be reluctant to follow an unproven company such as ours or purchase or recommend the purchase of our shares until such time as we became more seasoned and viable. As a consequence, there may be periods of several days, weeks or months when trading activity in our shares is minimal or non-existent, as compared to a seasoned issuer which has a large and steady volume of trading activity that will generally support continuous sales without an adverse effect on share price.

We cannot give you any assurance that a broader or more active public trading market for our common stock will develop or be sustained. Our ultimate intention is to apply for trading on either the Nasdaq Capital Market or the NYSE Altemext U.S. LLC (formerly American Stock Exchange) at such time that we meet the

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requirements for listing on those exchanges. We currently do not meet the objective listing criteria for listing on those exchanges and there can be no assurance as to when we will qualify for either of these exchanges or that we will ever qualify for these exchanges.

In order for our registered common stock to be eligible to trade on the Nasdaq Capital Market, we would need, among other things, a bid price of \$4.00, \$5 million in stockholders' equity, and \$15 million market value of publicly held shares. In order for our registered common stock to be eligible to trade on the NYSE MKT: Std. #4, which is a market for small and mid-sized companies, we would need, among other things, at least \$20 million market value of public float, a minimum price of \$3.00 and \$75 million in market capitalization.

Currently, our market capitalization, revenues and stockholders' equity are insufficient to qualify for these exchanges. We would also need to meet the corporate governance and independent director and audit committee standards of NASDAQ and/or the NYSE MKT Std. #4. We do satisfy such standards at this time.

### ***Our common stock is traded on the OTCQB Market, is illiquid and subject to price volatility unrelated to our operations.***

Our shares of common stock are currently traded on the OTCQB Market. Many institutional investors have investment policies which prohibit them from trading in stocks on the OTCQB Market. As a result, stocks traded on the OTCQB Market generally have limited trading volume and exhibit a wide spread between the bid/ask quotations than stock traded on national exchanges.

In addition, the stock market is subject to extreme price and volume fluctuations. The market price of our common stock could fluctuate substantially due to a variety of factors, including market perception of our ability to achieve our planned growth, our quarterly operating results, operating results of our competitors, trading volume in our common stock, changes in general conditions in the economy and the financial markets or other developments affecting our competitors or us. Certain of these factors can have a significant effect on the market price for our stock for reasons that are unrelated to our operating performance.

### ***The application of the "penny stock" rules to our common stock could limit the trading and liquidity of the common stock and adversely affect the market price of our common stock.***

As long as the trading price of our common stock is below \$5.00 per share, the open-market trading of our common stock will be subject to the "penny stock" rules, unless we otherwise qualify for an exemption from the "penny stock" definition. The "penny stock" rules impose additional sales practice requirements on certain broker-dealers who sell securities to persons other than established customers and accredited investors (generally those with net assets in excess of \$1,000,000 or annual income exceeding \$200,000 or \$300,000 together with their spouse). These regulations, if they apply, require the delivery, prior to any transaction involving a penny stock, of a disclosure schedule explaining the penny stock market and the associated risks. Under these regulations, certain brokers who recommend such securities to persons other than established customers or certain accredited investors must make a special written suitability determination regarding such a purchaser and receive such purchaser's written agreement to a transaction prior to sale. These regulations may have the effect of limiting the trading activity of our common stock, reducing the liquidity of an investment in our common stock and increasing the transaction costs for sales and purchases of our common stock as compared to other securities.

### ***Shares eligible for future sale may adversely affect the market.***

From time to time, certain of our shareholders may be eligible to sell some or all of their shares of common stock pursuant to Rule 144, promulgated under the Securities Act of 1933, as amended, (the "Securities Act") subject to certain limitations. In general, pursuant to Rule 144 as in effect as of the date of this Form S-1 Registration Statement, a shareholder (or shareholders whose shares are aggregated) who has satisfied the applicable holding period and is not deemed to have been one of our affiliates at the time of sale, or at any time during the three months preceding a sale, may sell their shares of common stock. Any substantial sale, or cumulative sales, of our common stock pursuant to Rule 144 or pursuant to any resale prospectus may have a material adverse effect on the market price of our securities.

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### ***We expect volatility in the price of our common stock and warrants, which may subject us to securities litigation.***

If established, the market for our common stock may be characterized by significant price volatility when compared to seasoned issuers, and we expect that our share price will be more volatile than a seasoned issuer for the indefinite future. In addition, there is no established trading market for the warrants being offered in this offering. Although, we intend to apply for listing of our common stock and warrants on The Nasdaq Stock Market, no assurance can be given that our application will be approved, or that, if the application is approved, the price of our common stock will be less volatile, or that the price of the warrants will not be volatile. In the past, plaintiffs have often initiated securities class action litigation against a company following periods of volatility in the market price of its securities. We may in the future be the target of similar litigation. Securities litigation could result in substantial costs and liabilities and could divert management's attention and resources.

### ***A stockholder group holds a majority of the outstanding common stock of the company and is able to effectively control our management and operations, and control by this group may create conflicts of interest.***

A group consisting of Dr. Samuel Herschkowitz, Josh Komberg (who is our Chief Executive Officer and Interim Chairman of the Board), SOK Partners, LLC and Atlantic Partners Alliance, currently owns more than 141 million shares of our outstanding common stock, representing approximately 57% of our voting power. As a result, this group controls the outcome of all matters requiring stockholder approval, including any future merger, consolidation or sale of all or substantially all of our assets. Further, this group indirectly controls our management through the power to elect and remove any members of the Board of Directors. This concentrated control could discourage others from initiating any potential merger, takeover or other change of control transaction that may otherwise be beneficial to our stockholders. As a result, the return on your investment in our common stock through the market price of our common stock or ultimate sale of our business could be adversely affected. Further, conflicts of interest may arise with respect to the interpretation, continuation, renewal or enforcement of our agreements with the members of this group and their affiliates, including the agreements described under "Certain Relationships and Related Party Transactions." The resolution of any such conflict in favor of any member of this group or any of their affiliates may materially harm our results of operations and the value of your shares of common stock.

### ***Our board of directors' ability to issue undesignated preferred stock and the existence of anti-takeover provisions may depress the value of our common stock.***

Our authorized capital includes 10 million shares of preferred stock. Of this amount, 20,550 shares have been designated as Series A Convertible Preferred Stock and the remaining authorized shares are undesignated preferred stock. Our board of directors has the power to issue any or all of the shares of undesignated preferred stock, including the authority to establish one or more series and to fix the powers, preferences, rights and limitations of such class or series, without seeking stockholder approval. Further, as a Delaware corporation, we are subject to provisions of the Delaware General Corporation Law regarding "business combinations." We may, in the future, consider adopting additional anti-takeover measures. The authority of our board to issue undesignated stock and the anti-takeover provisions of Delaware law, as well as any future anti-takeover measures adopted by us, may, in certain circumstances, delay, deter or prevent takeover attempts and other changes in control of the company not approved by our board of directors. As a result, our stockholders may lose opportunities to dispose of their shares at favorable prices generally available in takeover attempts or that may be available under a merger proposal and the market price, voting and other rights of the holders of common stock may also be affected.

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**SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS**

All statements contained in this prospectus, other than statements of historical facts, that address future activities, events, or developments, are forward-looking statements, including, but not limited to, statements containing the words “believe,” “anticipate,” “expect,” and words of similar import. These statements are based on certain assumptions and analyses made by us in light of our experience and our assessment of historical trends, current conditions and expected future developments as well as other factors we believe are appropriate under the circumstances. Whether actual results will conform to the expectations and predictions of management, however, is subject to a number of risks and uncertainties that may cause actual results to differ materially. Such risks are in the section herein entitled “Risk Factors,” and in our previous SEC filings.

Consequently, all of the forward-looking statements made in this prospectus are qualified by these cautionary statements, and there can be no assurance that the actual results anticipated by management will be realized or, even if substantially realized, that they will have the expected consequences to or effects on our business operations.

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**USE OF PROCEEDS**

We will not receive any of the proceeds from the sale of the common stock by the selling stockholders. However, we will receive the proceeds of any cash exercise of the warrants, and the conversion of any notes will reduce the outstanding principal and/or interest amount of certain indebtedness. Any proceeds received from the exercise of the warrants will be used for working capital or general corporate purposes.

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**PRICE RANGE OF COMMON STOCK**

Our common stock is not listed on any stock exchange. Our common stock has been quoted by the OTCQB under the symbol “SKLN.QB.” Prior to August 2012, it was quoted by the OTC Bulletin Board. The following table sets forth the high and low bid information for our common stock for each quarter within our last two fiscal years as reported by the OTCQB or the OTC Bulletin Board, as applicable. The bid prices reflect inter-dealer quotations, do not include retail markups, markdowns, or commissions, and do not necessarily reflect actual transactions. Prior to this offering, there was no trading market for the warrants.

	<u>High</u>	<u>Low</u>
<b>2014</b>		
Quarter ending September 30, 2014 (through September 4, 2014)	\$ 0.24	\$ 0.12
Quarter ending June 30, 2014	\$ 0.19	\$ 0.106
Quarter ended March 31, 2014	\$ 0.29	\$ 0.175
<b>2013</b>		
Quarter ended December 31, 2013	\$ 0.35	\$ 0.20
Quarter ended September 30, 2013	\$ 0.47	\$ 0.13
Quarter ended June 30, 2013	\$ 0.28	\$ 0.12
Quarter ended March 31, 2013	\$ 0.14	\$ 0.05
<b>2012</b>		
Quarter ended December 31, 2012	\$ 0.14	\$ 0.07
Quarter ended September 30, 2012	\$ 0.12	\$ 0.05
Quarter ended June 30, 2012	\$ 0.10	\$ 0.03
Quarter ended March 31, 2012	\$ 0.33	\$ 0.05

As of September 4, 2014 the closing price for shares of our common stock was \$0.1265 per share on the OTCQB.

**Holders**

As of September 4, 2014, there were approximately 165 stockholders of record of our common stock.

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**DIVIDEND POLICY**

We follow a policy of retaining earnings, if any, to finance the expansion of our business. We have not paid, and, except as set forth below, do not expect to declare or pay, cash dividends in the foreseeable future.

In February 2014 the company completed a private placement of Series A Convertible Preferred Stock on which the Company shall pay a 6% quarterly dividend on the stated value per annum commencing on the first day of each quarter. The dividends shall be payable quarterly in cash or in shares of common stock (calculated at the then applicable conversion price per share) and shall be payable on the day at the end of each dividend period (each such day being hereinafter called a “Dividend Payment Date”). No other dividends shall be paid on shares of preferred stock; and the Company shall pay no dividends (other than dividends in the form of common stock) on shares of the common stock unless it simultaneously complies with the previous sentence. Dividends shall be payable to holders of record as they appear in the stock records of the Company at the close of business on the applicable record date, which shall be the tenth (10<sup>th</sup>) day preceding the applicable Dividend Payment Date, or such other date designated by the Board of Directors or an officer of the Company duly authorized by the Board of Directors for the payment of dividends that is not more than 30 nor less than ten days prior to such Dividend Payment Date (each such date, a “Dividend Record Date”).



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### **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

You should read the following discussion and analysis of our financial condition and results of operations together with our financial statements and the related notes appearing elsewhere in this prospectus. Our discussion includes forward-looking statements based upon current expectations that involve risks and uncertainties, such as our plans, objectives, expectations, and intentions. Actual results and the timing of events could differ materially from those anticipated in these forward-looking statements as a result of a number of factors, including those set forth under the Special Note Regarding Forward-Looking Statements, Business, and Risk Factors sections in this prospectus.

#### **Recent Developments**

The paragraphs below in this section update the disclosures under "Management's Discussion and Analysis of Financial Condition and Resulting Operations" for the periods ended June 30, 2014 and 2013 and the years ended December 31, 2013 and 2012. The subsequent sections beginning with "Overview" are as originally filed in content with some minor changes in paragraph placement for easier comparison, except that we have also revised these sections to reflect the extension of the due date of certain indebtedness as described in the next paragraph.

Our cash balance was approximately \$40,000 as of June 30, 2014. Our current operating expenses are approximately \$250,000 per month.

As of June 30, 2014 the Company is not in default with respect to any debt. We expect that we will require additional funding to finance operating expenses and to enter the international marketplace. We believe that we will need to raise at least an aggregate of \$1 million from future financing in order to have sufficient financial resources to fund our operations for the next 6 months because of our cash flow deficit. We will attempt to raise these funds through equity or debt financing, alternative offerings or other means. If we are successful in securing adequate funding we plan to make significant capital or equipment investments, and we will also continue to make human resource additions over the next 12 months.

#### **Overview**

We were incorporated in Minnesota in April 2002 under the name BioDrain Medical, Inc. Effective August 6, 2013, the Company changed its name to Skyline Medical Inc. Pursuant to an Agreement and Plan of Merger dated effective December 16, 2013, the Company merged with and into a Delaware corporation with the same name that was its wholly-owned subsidiary, with such Delaware Corporation as the surviving corporation of the merger. We are a development stage company manufacturing an environmentally conscientious system for the collection and disposal of infectious fluids that result from surgical procedures and post-operative care. Since our inception in 2002, we have invested significant resources into product development. We believe that our success depends upon converting the traditional process of collecting and disposing of infectious fluids from the operating rooms of medical facilities to our wall-mounted Fluid Management System ("FMS") and use of our proprietary cleaning fluid and filter kit.

We currently have six regional sales managers to sell the STREAMWAY System. In the first quarter of 2014 we signed a contract with an independent distributor covering New York and surrounding areas.

Since inception, we have been unprofitable. We incurred net losses of approximately \$1.7 million and \$1.2 million for the three months ended June 30, 2014 and 2013, respectively. We incurred net losses of approximately \$3.4 million and \$3.3 million for the six months ended June 30, 2014 and 2013, respectively. As of June 30, 2014, we had an accumulated deficit of approximately \$32.0 million. We received approval from the FDA in April 2009 to commence sales and marketing activities of the STREAMWAY FMS system and shipped the first system in 2009. However, there was no significant revenue prior to 2011, primarily due to lack of funds to build and ship the product. We sold five original STREAMWAY units in 2011, and another twenty-nine original units to date.

In the first quarter of 2014, the Company commenced sales of an updated version of the STREAMWAY System, which provides a number of enhancements to the existing product line including a more intuitive and easier to navigate control screen, data storage capabilities, and additional inlet ports on the filters, among other improvements. This updated version utilizes improved technology, including the capability for continuous flow

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and continuous suctioning, as covered by our provisional patent application filed in 2013 and our non-provisional patent application filed in January 2014. The Company sold another eight units through April 30, 2014, and another eight units shipped and sold by May 16, 2014. The Company has trials and demonstrations set for 5 major hospital systems and teaching hospitals throughout May 2014. We have purchase orders for approximately 36 STREAMWAY Systems that will be installed in hospitals and surgical centers over the next 12 months beginning in May 2014.

We expect the revenue for STREAMWAY units to increase significantly at such time as the hospitals approve the use of the units for their applications based on trial basis units and place orders for billable units. Trial basis units are either installed in or hung on the hospital room wall. The unit is connected to the hospital plumbing and sewer systems, as well as, the hospital vacuum system. The unit remains on the customer site for 2-4 weeks, as contracted, at no cost to the customer. However, the customer does purchase the disposable kits necessary to effectively operate the units. Once the trial period has expired the unit is either returned to the Company or purchased by the customer. If purchased, at that time, the Company invoices the customer based upon a contracted price negotiated prior to the trial.

We have never generated sufficient revenues to fund our capital requirements. We have funded our operations through a variety of debt and equity instruments. See "Liquidity and Capital Resources – Historical Financing" below. Our future cash requirements and the adequacy of available funds depend on our ability to sell our products. See "Plan of Financing; Going Concern Qualification" below.

As a company still in development, our limited history of operations makes prediction of future operating results difficult. We believe that period to period comparisons of our operating results should not be relied on as predictive of our future results.

### **Results of Operations**

#### **Comparison of Six Months Ended June 30, 2014 with Six Months Ended June 30, 2013**

*Revenue.* The Company recognized \$318,000 of revenue in the three months ended June 30, 2014 compared to \$151,000 in revenue in the three months ended June 30, 2013. The Company recognized \$389,000 in revenue in the six months ended June 30, 2014 compared to \$279,000 in revenue in the six months ended June 30, 2013. The revenue in the first six months of 2014 included the sale of 20 STREAMWAY FMS systems. Three STREAMWAY Systems were sold under the Company's pay per procedure plan whereby hardware revenue is recognized on a per procedure basis. In essence, the Company adds a premium charge on top of the cleaning solution per bottle price representing an amortized amount of the STREAMWAY unit over an agreed upon period between the customer and Skyline.

*Cost of sales.* Cost of sales in the three months ended June 30, 2014 was \$98,000 and \$67,000 in the three months ended June 30, 2013. Cost of sales in the six months ended June 30, 2014 was \$129,000 and \$109,000 in the six months ended June 30, 2013. The gross profit margin was approximately 67% in the six months ended June 30, 2014 compared to 61% for the six months ended June 30, 2013. Our margins still vary as our initial production of the STREAMWAY has been released for sale. We expect our margins to increase over the remainder of the year as our manufacturing production becomes more consistent, and as increased sales allow us to achieve volume purchasing discounts on both equipment components and our cleaning solution. Over the next several quarters, we expect increases in revenues to exceed increases in costs related to increasing manufacturing and sales capabilities.

*General and Administrative expense.* General and administrative expense primarily consists of management salaries, professional fees, consulting fees, travel expense, administrative fees and general office expenses.

General and Administrative (G&A) expenses increased by \$442,000 for the three months ended June 30, 2014 compared to the 2013 period. G&A decreased by \$202,000 for the six months ended June 30, 2014 compared to the 2013 period. The increase for the three month period was primarily due to settling with Marshall Ryan thereby incurring an additional expense of \$500,000 payable over the next six months, increases in recruiting fees of \$60,000 for hiring our sales team in 2014, increases in our corporate insurance of \$15,000 for additional coverage and salary increases by \$20,000 due to hiring a controller and increasing administrative assistant salaries over 2013. Otherwise there were reductions in our investor relation fees by \$49,000 concentrating on a more specified area of the market and reducing our consulting fees by \$68,000

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that were primarily for fund raising assistance in 2013. The decrease in the six month period, above the settlement expense, was primarily due to stock based and investor stock compensation reductions of \$1,069,000 resulting from fewer private placements in 2014. Other increases were for salaries of \$107,000 as a result of hiring a controller and company-wide raises, legal fees of \$74,000, recruiting fees of \$60,000 and fund raising consulting fees of \$210,000.

*Operations expense.* Operations expense primarily consists of expenses related to product development and prototyping and testing in the company's current stage.

Operations expense increased by \$87,000 for the three months ended June 30, 2014 compared to the 2013 period. Operations increased by \$147,000 for the six months ended June 30, 2014 compared to the 2013 period. The three and six month increases are comprised of consulting of \$28,000 and \$37,000 due to hiring a quality control contractor and additional engineers, shipping and postage of \$12,000 and \$20,000 for expedited orders that were in backorder and for \$56,000 and \$116,000 in research and development costs.

*Sales and Marketing expense.* Sales and marketing expense consists of expenses required to sell products through independent reps, attendance at trades shows, product literature and other sales and marketing activities.

Sales and marketing expenses increased by \$211,000 for the three months ended June 30, 2014 compared to the 2013 period. Sales and marketing increased by \$329,000 for the six months ended June 30, 2014 compared to the 2013 period. The three and six month increases are comprised of salaries of \$137,000 and \$216,000 due to hiring four additional regional sales managers, commissions of \$12,000 for both periods as system sales began in the second quarter, a \$24,000 increase over both periods in employee benefits resulting from the increased hires, increases in travel expense of \$25,000 and \$38,000 relating to new hires, a \$15,000 increase in marketing expenses initiated in the second quarter, a \$6,000 increase in web development in the second quarter and increased trade show expenses as the Company participated in national shows resulting in a rise of \$33,000 and \$40,000, respectively. There was some offset by reduced public relations expenses of \$40,000 and \$50,000, respectively.

*Interest expense.* Interest dropped significantly in the three months and six months ended June 30, 2014 compared to the three and six months ended June 30, 2013. There was a decrease of \$112,000 in interest expense in the three-month period and \$189,000 in the six month period. The lower interest is due to the elimination of convertible notes and all but one settlement agreement less the addition of original issue discounts to SOK Partners for our bridge loan.

The (Gain)/Loss on revaluation of equity-linked financial instruments reflected a gain of \$0 in the three months ended June 30, 2014 compared to a gain of \$69,000 in the three months ended June 30, 2013. The reflected gain is \$11,000 in the six months ended June 30, 2014 compared to a gain of \$89,000 in the six months ended June 30, 2013. The increased gain in the current periods resulted from warrants moving closer to expiration; there is only one warrant remaining to the equity-linked financial instruments.

### **Comparison of Year Ended December 31, 2013 with Year Ended December 31, 2012**

*Revenue.* We recorded revenue of \$468,000 in 2013, compared to \$188,000 in 2012. Revenue in 2013 included the sale of twenty-one STREAMWAY systems and disposable supplies to operate the STREAMWAY. The revenue in 2012 included the sale of seven STREAMWAY systems and disposable supplies to operate the STREAMWAY. The Company is no longer installing the original STREAMWAY in hospitals for evaluation purposes, but will place our enhanced STREAMWAY in hospitals for evaluation in the first quarter of 2014. Additionally, the Company has purchase orders for approximately 50 enhanced STREAMWAY units that we anticipate installing over the next 12 months beginning at the end of February. The Company decision to cease production of the original STREAMWAY in June 2013 enabled us to concentrate efforts toward putting the enhanced STREAMWAY into full production that is expected to lead to stronger sales in 2014.

*Cost of sales.* Cost of sales was \$189,000 in 2013 compared to \$128,000 in 2012. The gross profit margin was 59% in 2013 and 32% in 2012. As our revenue has increased and we honed in on parts for the enhanced STREAMWAY we were better able to maximize our margins through advanced purchasing at larger volumes. The Company also developed ways to reduce cost through tooling parts and purchasing different components that improved the STREAMWAY Systems while costing less.

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*General and Administrative expense.* General and administrative (G&A) expense primarily consists of management salaries, professional fees, consulting fees, travel expense, administrative fees and general office expenses.

G&A expense increased to \$7,530,000 for 2013 from \$6,286,000 in 2012. The \$1,244,000 increase in G&A expenses for 2013, compared to 2012, is primarily due to an increase in salaries of \$306,000 as a result of additional hiring and full year compensation for the officers; an increase in legal expenses of \$429,000 incurred for private placement funding, registration filings, renaming, reincorporating and merging the Company; investor relations expenses of \$353,000 for fees to placement agents, data room costs for investors to conduct research and expenses related to a possible listing on the NASDAQ or the New York Stock Exchange, and, \$402,500 for bonuses predominantly in the form of stock options. There were offsets for reductions to accounting fees and consulting expenses.

*Operations expense.* Operations expense primarily consists of expenses related to product development and prototyping and testing in the Company's current stage.

Operations expense increased to \$1,097,000 in 2013 compared to \$761,000 in 2012. The \$336,000 increase in operations expense in 2013 is primarily due to increases of \$145,000 in salaries as a result of additional hiring and full year compensation for the COO and \$220,000 in research and development from a concentrated effort extended toward rolling out the enhanced STREAMWAY. These increases were partially offset by certain expense reductions, including a reduction of \$116,000 in consulting expense.

*Sales and marketing expense.* Sales and marketing expense consists of expenses required to sell products through independent reps, attendance at trades shows, product literature and other sales and marketing activities.

Sales and marketing expenses increased to \$579,000 in 2013 compared to \$173,000 in 2012. The \$406,000 increase is a result of a \$68,000 increase in salaries due to hiring a senior sales executive and a direct salesperson; a \$132,000 increase in public relations after contracting a firm to assist the Company in bringing essential news to the public sector; a \$68,000 increase in commissions; and, a \$20,000 increase in web development.

*Interest expense.* Interest expense increased to \$637,000 in 2013 compared to \$259,000 in 2012. The \$377,000 was a result of financing efforts through private placements that were funded through convertible notes. All of the convertible notes were converted in 2013 resulting in interest expense paid through common stock shares.

*Loss (gain) on valuation of equity-linked financial instruments.* The Company realized a gain of \$158,000 on valuation of equity-linked financial instruments in 2013 compared to a loss of \$3,100 in 2012. The gain resulted from older warrants expiring.

### **Liquidity and Capital Resources**

#### **Cash Flows for the Six Months Ended June 30, 2014 and 2013**

Net cash used in operating activities was \$1,947,000 for the six months ended June 30, 2014 compared with net cash used of \$2,123,000 for the 2013 period. The \$153,000 decrease in cash used in operating activities was due to increases in accounts payables as vendors increased terms for the past quarter, increases in accrued liabilities as payroll liabilities were increased; this was offset by a further increases in inventories as more systems were in production.

Cash flows used in investing activities was \$87,000 for the six months ended June 30, 2014 and \$58,000 dollars for the six months ended June 30, 2013. As we have grown our fixed asset acquisitions have increased as well. We have purchased furniture, computers, software and have incurred leasehold improvements.

Net cash provided by financing activities was \$1,973,000 for the six months ended June 30, 2014 compared to net cash provided of \$2,305,000 for the six months ended June 30, 2013. The provision in 2014 was primarily the result of completing a private placement of Series A Convertible Preferred Stock resulting in gross proceeds of \$2,055,000 to the Company. See Note 3 to the Financial Statements. In 2013, there were private placements comprising the amount above.

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### **Cash Flows for the Year Ended December 31, 2013 and 2012**

Net cash used in operating activities was \$3,855,000 for 2013, compared with net cash used of \$1,184,000 for 2012. The \$2,671,000 increase in cash used in operating activities was largely due to an increase consisting of contracted bonuses for 2013, short term amounts for long term liabilities resulting from settlements of old notes, an increase of \$36,000 for prepaid expenses and other assets, an increase in research and development of \$220,000 and an increase of \$68,000 in accounts receivable. There was also \$79,000 in payroll liabilities.

Cash flows used in investing activities was \$216,000 for 2013 and zero in 2012. As we have grown our fixed asset acquisitions have increased as well. We have purchased furniture, computers, software and have incurred leasehold improvements.

Net cash provided by financing activities was \$4,160,000 for 2013 compared to net cash provided of \$1,074,000 for 2012. The increase in 2013 was primarily the result of proceeds of private placements of common stock of \$1,000,000, warrant exercises of \$1,337,000 and proceeds of \$1,823,000 of convertible debt. All then outstanding convertible notes were converted in 2013.

### **Capital Resources**

We had a cash balance of \$40,000 as of June 30, 2014. Since our inception, we have incurred significant losses. As of June 30, 2014, we had an accumulated deficit of approximately \$32,050,000.

From inception to June 30, 2014, our operations have been funded through a bank loan and private convertible debt of approximately \$4,060,000 and equity investments totaling approximately \$9,104,000. See "Historical Financing" below.

In the first quarter of 2014, we raised \$2,055,000 in gross proceeds excluding offering expenses from a private placement of Series A Convertible Preferred Stock.

### ***Plan of Financing; Going Concern Qualification***

We have not achieved profitability and anticipate that we will continue to incur net losses for the foreseeable future. We expect that our operations, sales and marketing, and general and administrative expenses will increase, and as a result we will need to generate significant revenue to achieve profitability.

We are currently incurring operating expenses of approximately \$350,000 per month. Although we are attempting to curtail our expenses, there is no guarantee that we will be able to reduce these expenses significantly, and expenses for some periods may be higher as we prepare our product for broader sales, increase our sales efforts and maintain adequate inventories. Further, we have approximately \$3,500,000 in debts, liabilities and cash obligations that predominantly become due in calendar 2014.

In February 2014, we raised \$2.0 million in gross proceeds from our private placement of convertible preferred stock and warrants. In July and August 2014, we sold convertible notes and warrants for an aggregate purchase price of over \$0.9 million. We may enter into purchase agreements for further sales of convertible notes and warrants. See "Historical Financing" below.

We expect that we will need further equity financing to maintain our operations, including further sales of convertible notes and warrants and possibly other financing. If such financing is available, it may be highly dilutive to our existing shareholders and may otherwise include burdensome or onerous terms. Our inability to raise additional working capital at all or to raise it in a timely manner would negatively impact our ability to fund our operations, to generate revenues, and to otherwise execute our business plan, leading to the reduction or suspension of our operations and ultimately forcing us to declare bankruptcy, reorganize or to go out of business. Should this occur, the value of any investment in our securities could be adversely affected, and an investor would likely lose all or a significant portion of their investment. These factors raise substantial doubt about our ability to continue as a going concern.

Our current operating cash balance, subsequent to the July 2014 convertible bridge first tranche, is approximately \$75,000. The funds were predominantly used for operating expenses and purchasing. The Company is expecting \$900,000 in additional funding in second and perhaps third tranches. Based on our current operating plan we believe that we have sufficient cash, cash equivalents and short-term investment

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balances to last approximately through September 30, 2014 after which additional financing will be needed to continue to satisfy our obligations. While holders of our warrants could exercise and provide cash to us during that time frame, we are not depending on that in our fundraising efforts. We commenced sales of our enhanced STREAMWAY in the first quarter of 2014. Sales of this product are expected to provide additional operating revenues and cash balances that could reduce the need for additional fundraising; however, cash collections for product sales are not immediate, which may result in a delay in positive operating cash flow over the next several quarters.

As a result of the above factors, our independent registered public accountant firm has indicated in their audit opinion, contained herein, that they have serious doubts about our ability to continue as a going concern. The financial statements included herein have been prepared assuming the Company will continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

### **Historical Financing**

We have funded our operations through a combination of debt and equity instruments. We funded our early operations through a bank loan of \$41,400, an equity investment of \$68,000 from the Wisconsin Rural Enterprise Fund (“WREF”) and \$30,000 in early equity investment from several individuals. WREF had also previously held debt in the form of three loans of \$18,000, \$12,500 and \$25,000. In December 2006, WREF converted two of the loans totaling \$37,500 into 43,000 shares of our common stock. In August 2006, we secured a \$10,000 convertible loan from one of our vendors. In February 2007, we obtained \$4,000 in officer and director loans and in March 2007, we arranged a \$100,000 convertible note from two private investors. In July 2007, we obtained a convertible bridge loan of \$170,000. In June 2008, we paid off the remaining \$18,000 loan from WREF and raised approximately \$1.6 million through a private common stock offering completed in October 2008. The \$170,000 convertible bridge loan and the \$4,000 in officer and director loans were converted into shares of our common stock in October 2009. During 2009, we raised an additional \$725,000 in a private placement of stock units and/or convertible debt, with each stock or debt unit consisting of, or converting into, respectively, one share of our common stock, and a warrant to purchase one share of our common stock at \$.65 per share.

In 2010, we raised approximately \$229,000 in equity and \$605,000 in convertible debt.

In 2011, we raised \$1,386,000 in equity and \$525,000 in convertible debt, including the convertible debt investment by Dr. Sam Herschkowitz described under, “Certain Relationships and Related Party Transactions.”

In 2012, the Company raised \$696,000 in equity and \$529,000 in convertible debt, and \$818,000 of debt was converted into equity. This convertible debt included advances on a convertible promissory note from SOK Partners, LLC, and an investment fund affiliated with one of our directors, for approximately \$357,000. See, “Certain Relationships and Related Party Transactions.” On November 6, 2012, we entered into additional note purchase agreements with Dr. Samuel Herschkowitz, pursuant to which on the same date, we issued and sold convertible promissory notes in the total principal amount of \$156,243 to Dr. Herschkowitz and certain of his assignees. Pursuant to the note purchase agreements, we issued to these parties an aggregate 1,562,430 shares of common stock in consideration of placement of the notes. The convertible notes bear interest at a rate of 20% per annum and are secured by a security interest in the Company’s accounts receivable, patents and certain patent rights and are convertible into common stock upon certain mergers or other fundamental transactions at a conversion price based on the trading price prior to the transaction. The proceeds from this financing were used to pay off approximately \$155,000 in principal amount of secured indebtedness.

The Company also raised an additional \$300,000 from the sale of convertible notes in January 2013. Also, in January and March 2013, the Company raised an additional \$500,000 from a second private sale of equity securities. In addition, in March 2013, the Company completed a further private sale of common stock for an aggregate purchase price of \$500,000. See Note 2 to the Financial Statements included in this prospectus. In June 2013, the Company raised an additional \$1,000,000 from the sale of convertible notes. See Note 3 to the Financial Statements included in this prospectus. In the third quarter we also borrowed the remaining \$243,000 principal amount of our convertible note payable to SOK Partners, LLC. During the third

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quarter of 2013, the holders of convertible notes, including Dr. Samuel Herschkowitz and SOK Partners, LLC, converted \$1,506,000 of outstanding debt, including principal and interest, into equity. The Company converted the promissory notes totaling \$314,484 and \$680,444, respectively, including principal and interest, on September 11, 2013 for 22,463,172 and 48,603,159 shares, respectively, at \$.014 per share. Also during the third quarter of 2013, we raised approximately \$1,044,000 through the cash exercise of warrants by investors who were offered a reduction in the exercise price in connection with the exercise. In December 2013 the Company raised \$280,000 in the form of a short term non-convertible note with 10% interest based on a 365 day year from SOK Partners, LLC. In January 2014 an additional \$20,000 was raised and added to the original note to SOK Partners, LLC. Josh Kornberg the CEO, is a 50% managing partner in SOK Partners, LLC.

### ***2014 Sales of Preferred Stock and Warrants.***

On February 4, 2014, (the "Closing Date") we raised \$2,055,000 in gross proceeds from a private placement of Series A Convertible Preferred Stock, par value \$0.01 (the "Preferred Shares") pursuant to a Securities Purchase Agreement with certain investors (the "Purchasers") purchased 20,550 Preferred Shares, and warrants (the "Warrants") to acquire an aggregate of approximately 1,600,000 shares of Common Stock. The Preferred Shares are convertible into shares of Common Stock at an initial conversion price of \$0.26 per share of Common Stock. The Warrants are exercisable at an exercise price of \$0.325 per share and expire five years from the Closing Date. If the Common Stock is not listed on the Nasdaq Stock Market, the New York Stock Exchange, or the NYSE MKT within 180 days of the Closing, the Company shall issue additional Warrants to purchase additional shares of Common Stock, equal to 30% of the shares of Common Stock which the Preferred Shares each Purchaser purchased are convertible into. As of August 4, 2014, the Company issued additional warrants to purchase 4,615,385 shares to the Purchasers in connection with this provision.

The Securities Purchase Agreement requires the Company to register the resale of the shares of Common Stock underlying the Preferred Shares (the "Underlying Shares") and the Common Stock underlying the Warrants (the "Warrant Shares"). The Company is required to prepare and file a registration statement with the Securities and Exchange Commission within 132 days of the Closing Date (as extended by subsequent consent of the Purchasers), and to use commercially reasonable efforts to have the registration statement declared effective within 147 days if there is no review by the Securities and Exchange Commission, and within 192 days in the event of such review.

The Preferred Shares are convertible at the option of the holder into the number of shares of Common Stock determined by dividing the stated value of the Preferred Shares being converted by the conversion price of \$0.26, subject to adjustment for stock splits, reverse stock splits and similar recapitalization events. If the Company issues additional shares of Common Stock, other than certain stock that is excluded under the terms of the Securities Purchase Agreement, in one or more capital raising transactions with an aggregate purchase price of at least \$100,000 for a price less than the then existing conversion price for the Preferred Shares (the "New Issuance Price"), then the then existing conversion price shall be reduced to the New Issuance Price, provided, however, that under no circumstances shall the New Issuance Price be less than \$0.13 or reduced to a price level that would be in breach of the listing rules of any stock exchange or that would have material adverse effect on the Corporation's ability to list its Common Stock on a stock exchange, including but not limited to the change of accounting treatment of the Preferred Stock. The Preferred Shares contain certain limitations on conversion so that the holder will not own more than 4.99% of the number of shares of the Common Stock outstanding immediately after giving effect to the issuance of shares of Common Stock issuable upon conversion of Preferred Shares held by the applicable holder, with the percentage subject to increase in certain circumstances. The Preferred Shares are eligible to vote with the Common Stock on an as-converted basis, but only to the extent that the Preferred Shares are eligible for conversion without exceeding the Beneficial Ownership Limitation. The Preferred Shares are entitled to receive dividends on a pari passu basis with the Common Stock, when, and if declared. Upon any liquidation, dissolution or winding-up of the Company, whether voluntary or involuntary (a "Liquidation"), after the satisfaction in full of the debts of the Company and the payment of any liquidation preference owed to the holders of shares of Common Stock ranking prior to the Preferred Shares upon liquidation, the holders of the Preferred Shares

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shall receive, prior and in preference to the holders of any junior securities, an amount equal to \$2,055,000 times 1.2, plus all declared but unpaid dividends.

The Warrants are exercisable on any day on or after the date of issuance, have an exercise price of \$0.325 per share, subject to adjustment, and a term of five years from the date they are first exercisable. However, a holder will be prohibited from exercising a Warrant if, as a result of such exercise, the holder, together with its affiliates, would exceed the Beneficial Ownership Limitation as described above for the Preferred Shares. If any Warrant has not been fully exercised prior to the first anniversary of the Closing and if during such period the Company has not installed or received firm purchase orders (accepted by the Company) for at least 500 STREAMWAY® Automated Surgical Fluid Disposal Systems, then, the number of shares of Common Stock for which such Warrant may be exercised shall be increased 2.5 times.

As of July 23, 2014, in connection with the offering of convertible notes and warrants described below, the Company and the holders of at least the minimum number of Preferred Shares required to (i) waive certain covenants under the Securities Purchase Agreement for the Preferred Shares, dated February 4, 2014 (the "Preferred Stock SPA"), and (ii) consent to the automatic conversion of all outstanding Preferred Shares pursuant to Section 6(d) of the Certificate of Designation, filed January 27, 2014, setting forth the preferences, rights and limitations of the Preferred Shares (the "Certificate of Designation"), agreed to the following:

- a waiver of the Company's obligation under Section 6.12 of the Preferred Stock SPA to not enter into any contract, transaction or arrangement or issue any security or instrument that provides for forward pricing of shares of Common Stock (the "Forward Pricing Transaction Restriction") with respect to the offering of convertible notes and, following a Qualified Public Offering (as defined below), a waiver of the Forward Pricing Transaction Restriction for any subsequent offering of securities by the Company;
- a consent to the inclusion of the registration of the Additional Shares (as defined below) on a registration statement or registration statements of the Company to be filed under the Securities Act of 1933, as amended, pursuant to Section 10 of the Preferred Stock SPA (the "Registration Statement"), covering the "Registrable Securities" as defined under the Preferred Stock SPA (the "Preferred Stockholders Registrable Securities");
- a consent to further extend the Filing Deadline and the Effectiveness Deadline (each as defined in the Certificate of Designation) pursuant to Section 10.1 of the Preferred Stock SPA such that the deadlines for the filing and effectiveness of the Registration Statement shall be the same as the applicable deadlines for the Convertible Notes Offering;
- an agreement by the Preferred Stockholders to a 90-day lock-up beginning from the date of closing of an underwritten public offering of the Common Stock with gross offering proceeds of at least \$6.0 million and the concurrent listing of the Common Stock on a national securities exchange (a "Qualified Public Offering") (the "Purchaser Lock-Up"); and
- a consent to automatically convert all outstanding Preferred Shares upon a Qualified Public Offering pursuant to the Certificate of Designation as described further below.

In consideration of the waiver and consents provided by the Preferred Stockholders, the Company agreed:

- to issue additional shares of Common Stock to the Preferred Stockholders (the "Additional Shares") (A) automatically upon the closing of a Qualified Public Offering, to the extent that (i) the Qualified Public Offering closes within six (6) months of the first closing of the Convertible Notes Offering ("Qualified Public Offering Deadline") and (ii) 70% of the public offering price per share of the Common Stock in the Qualified Public Offering (the "QPO Discount Price") is less than the Conversion Price floor contained in Section 7(e)(i) of the Certificate of Designation (the "Conversion Price Floor"), or (B) if a Qualified Public Offering has not been consummated by the Qualified Public Offering Deadline, upon the Preferred Stockholders' conversion of their shares of Preferred Stock to the extent that 70% of the volume weighted average price of the Common Stock



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on the principal Trading Market (as defined in the Certificate of Designation) of the Common Stock during the ten Trading Days (as defined in the Certificate of Designation) immediately preceding the Qualified Public Offering Deadline (the “Non-QPO Discount Price”) is less than the Conversion Price Floor;

- to provide the Preferred Stockholders with the right to participate in the Affiliate Convertible Notes Offering (as defined below) pro rata up to an aggregate of \$500,000 based on their respective interests in the Preferred Shares; and
- to provide the Preferred Stockholders with the right to participate in the Affiliate Convertible Notes Offering pro rata up to an aggregate of \$500,000 based on their respective interests in the Preferred Shares; and
- to pay reasonable attorneys’ fees and expenses of the Preferred Stockholders in connection with certain transactions as described further in the waiver and consent of, and notice to, holders of Preferred Shares.

### *2014 Sales of Convertible Notes and Warrants.*

#### *Securities Purchase Agreements*

On July 23, 2014, Skyline Medical Inc. (the “**Company**”) entered into a Securities Purchase Agreement (the “**Investor Securities Purchase Agreement**”) with an institutional investor (the “**Investor**”), pursuant to which the Company agreed to issue and sell (i) a senior convertible note, in an original principal amount of \$610,978 (the “**Investor Note**”), which Investor Note shall be convertible into a certain amount of shares (the “**Investor Conversion Shares**”) of the Company’s common stock, par value \$0.01 (the “**Common Stock**”), in accordance with the terms of the Investor Note, and (ii) a warrant (the “**Investor Warrant**”) to initially acquire up to 2,036,593 additional shares of Common Stock (the “**Investor Warrant Shares**”, and collectively with the Investor Note, the Investor Warrant and the Investor Conversion Shares, the “**Investor Securities**”) for an aggregate purchase price of \$500,000 (an approximately 22.2% original issue discount) (the “**Investor Convertible Notes Offering**”).

On July 23, 2014, the Company also entered into a Securities Purchase Agreement (the “**SOK Securities Purchase Agreement**”) with SOK Partners, LLC, an affiliate of the Company (“**SOK**”), pursuant to which the Company agreed to issue and sell (i) a senior convertible note, in an original principal amount of \$122,195.60 (the “**SOK Note**”), which SOK Note shall be convertible into a certain amount of shares (the “**SOK Conversion Shares**”) of Common Stock, in accordance with the terms of the SOK Note, and (ii) a warrant (the “**SOK Warrant**”) to initially acquire up to 407,318 additional shares of Common Stock (the “**SOK Warrant Shares**”, and collectively with the SOK Note, the SOK Warrant and the SOK Conversion Shares, the “**SOK Securities**”) for an aggregate purchase price of \$100,000 (an approximately 22.2% original issue discount) (the “**SOK Convertible Notes Offering**”).

The SOK Note, the SOK Warrant, the SOK Securities Purchase Agreement and the SOK Registration Rights Agreement contain terms and conditions substantially identical to that of the Investor Note, the Investor Warrant, the Investor Securities Purchase Agreement and the Investor Registration Rights Agreement (as defined below), respectively, which are described in greater detail below.

In addition to the Investor Convertible Notes Offering and the SOK Convertible Notes Offering, the Company may enter into one or more additional Securities Purchase Agreements (collectively, the “**Affiliate Securities Purchase Agreements**”) with certain affiliates of the Company and certain persons with whom the Company has a pre-existing relationship (the “**Affiliates**”) pursuant to which the Company may issue and sell (i) one or more senior convertible notes, in an original principal amount of up to \$1,099,760.40 (the “**Affiliate Notes**”), which Affiliate Notes shall be convertible into a certain amount of shares (the “**Affiliate Conversion Shares**”) of the Company’s Common Stock in accordance with the terms of the Affiliate Notes, and (ii) one or more warrants (the “**Affiliate Warrants**”) to initially acquire up to 3,665,862 additional shares of Common Stock (the “**Affiliate Warrant Shares**”, and collectively with the Affiliate Notes, the Affiliate Warrants and the Affiliate Conversion Shares, the “**Affiliate Securities**”) for an aggregate purchase price of \$900,000 (with the same original issue discount as specified for the Investor Note and SOK Note) (the “**Affiliate Convertible Notes Offering**”).

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Except for the maturity date of the Affiliate Notes and the expiration date of the Affiliate Warrants, the Affiliate Notes, the Affiliate Warrants, the Affiliate Securities Purchase Agreements and the registration rights agreement(s) to be entered into between the Company and the Affiliates, relating to the Affiliate Conversion Shares and Affiliate Warrant Shares, will have terms and conditions identical to that of the Investor Note, the Investor Warrant, the Investor Securities Purchase Agreement and the Investor Registration Rights Agreement (as defined below), respectively, which are described in greater detail below.

The Investor Security Purchase Agreement and the SOK Security Purchase Agreement are collectively referred to herein as the “**Security Purchase Agreements**.” The Investor Note and the SOK Note are collectively referred to herein as the “**Notes**.” The Investor Warrant and the SOK Warrant are collectively referred to herein as the “**Warrants**.” The Investor Securities and the SOK Securities are collectively referred to herein as the “**Securities**.” The Investor Convertible Notes Offering, the SOK Convertible Notes Offering, and the Affiliate Convertible Notes Offering are collectively referred to herein as the “**Convertible Notes Offering**.” The Investor Conversion Shares, SOK Conversion Shares, Affiliate Conversion Shares, Investor Warrant Shares, SOK Warrant Shares, and Affiliate Shares are collectively referred to herein as the “**Additional Shares**.” There is no guarantee that the Company will consummate the Affiliate Convertible Notes Offering as described or that such Affiliate Convertible Notes Offering will occur at all as described below.

### ***Convertible Notes***

The Notes mature on July 23, 2015 (subject to extension as provided in the Notes) and, in addition to the approximately 22.2% original issue discount, accrues interest at a rate of 12.0% per annum. The Investor and SOK have no voting rights as the holders of the Notes. Upon conversion of the Notes, the holders are entitled to receive such dividends paid and distributions made to the holders of Common Stock from and after the initial issuance date of the Notes to the same extent as if the holders had effected such conversion and had held such shares of Common Stock on the record date for such dividends and distributions.

With respect to the Investor Note, \$67,500 of the outstanding original principal amount of the Investor Note (together with any accrued and unpaid interest with respect to such portion of the principal amount and accrued and unpaid late charges with respect to such portion of the principal amount and such interest) will be automatically extinguished (without any cash payment by the Company) if (i) the Company has properly filed a registration statement covering the resale by the Investor of shares of the Common Stock issued or issuable upon conversion of the Investor Note with the Securities and Exchange Commission (the “**SEC**”), and such registration statement has been declared effective by the SEC on or prior to 120<sup>th</sup> calendar day after the closing date of the Investor Convertible Notes Offering, and (ii) no event of default, or an event that with the passage of time or giving of notice would constitute an event of default, has occurred on or prior to such date.

With respect to the SOK Note, \$13,500 of the outstanding original principal amount of the SOK Note (together with any accrued and unpaid interest with respect to such portion of the principal amount and accrued and unpaid late charges with respect to such portion of the principal amount and such interest) will be automatically extinguished (without any cash payment by the Company) if (i) the Company has properly filed a registration statement covering the resale by SOK of shares of the Common Stock issued or issuable upon conversion of the SOK Note with the SEC, and such registration statement has been declared effective by the SEC on or prior to 120<sup>th</sup> calendar day after the closing date of the SOK Convertible Notes Offering, and (ii) no event of default, or an event that with the passage of time or giving of notice would constitute an event of default, has occurred on or prior to such date.

The Notes are convertible at any time after issuance, in whole or in part, at the Investor’s or SOK’s option, as the case may be, into shares of Common Stock, at a conversion price equal to the lesser of (i) the product of (x) the arithmetic average of the lowest three volume weighted average prices of the Common Stock during the ten consecutive trading days ending and including the trading day immediately preceding the applicable conversion date and (y) 72.5% (or if an event of default has occurred and is continuing, 70%), and (ii) \$0.15 (as adjusted for stock splits, stock dividends, recapitalizations or similar events).

The Notes include customary events of default provisions. The Notes provides for a default interest rate of 15% per annum. Upon the occurrence of an event of default, the Investor or SOK, as the case may be, may require the Company to pay in cash the “Event of Default Redemption Price” which is defined in the Notes

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to mean the greater of (i) the product of (A) the amount to be redeemed multiplied by (B) 125% (or 100% if an insolvency related event of default) and (ii) the product of (X) the conversion price in effect at that time multiplied by (Y) the product of (1) 125% (or 100% if an insolvency related event of default) multiplied by (2) the greatest closing sale price of the Common Stock on any trading day during the period commencing on the date immediately preceding such event of default and ending on the date the Company makes the entire payment required to be made under this provision.

With respect to the Investor Note and the SOK Note, the Company has the right at any time to redeem, in whole or in part, the outstanding amount then remaining under such Note (the “**Remaining Amount**”) at a price equal to the greater of (i) 125% of the Remaining Amount and (ii) the product of (X) the conversion price in effect at that time multiplied by (Y) the product of (1) 135% multiplied by (2) the greatest closing sale price of the Common Stock on any trading day during the period commencing on the Company option redemption notice date and ending on the date immediately prior to the date that the Company makes the entire payment required to be made under this provision. The Company is also required to initially reserve 10 million shares of Common Stock, and will take all action necessary to reserve and keep available 150% of the number of shares of Common Stock as shall from time to time be necessary to effect the conversion of such portion of the Notes then outstanding.

### **Warrants**

The Warrants are exercisable on any day on or after the date of issuance and have an exercise price of \$0.165 per share, subject to adjustment, and a term of five years from the date of issuance. With respect to the Investor Warrant, 225,000 Warrant Shares will be automatically extinguished (without any cash payment by the Company) if (i) the Company has properly filed a registration statement with the SEC that has been declared effective by the SEC on or prior to the earlier of (x) the 60<sup>th</sup> calendar day after the closing of the offering (or the 120<sup>th</sup> calendar day after the closing of the Investor Convertible Notes Offering in the event that such registration statement is subject to review by the SEC) and (y) the fifth trading day after the date the Company is notified by the SEC that such registration statement will not be reviewed or will not be subject to further review (such date, the “**Warrant Shares Initial Effective Date**”) and (ii) the prospectus contained therein is available for use by a holder for the resale by such holder of all of the shares of Common Stock issued or issuable upon exercise of the Investor Warrant or otherwise pursuant to the terms of the Investor Warrant as of the Warrant Shares Initial Effective Date.

With respect to the SOK Warrant, 45,000 Warrant Shares will be automatically extinguished (without any cash payment by the Company) if (i) the Company has properly filed a registration statement with the SEC that has been declared effective by the SEC on or prior to the earlier of (x) the 60<sup>th</sup> calendar day after the closing of the offering (or the 120<sup>th</sup> calendar day after the closing of the SOK Convertible Notes Offering in the event that such registration statement is subject to review by the SEC) and (y) the Warrant Shares Initial Effective Date and (ii) the prospectus contained therein is available for use by a holder for the resale by such holder of all of the shares of Common Stock issued or issuable upon exercise of the SOK Warrant or otherwise pursuant to the terms of the SOK Warrant as of the Warrant Shares Initial Effective Date.

The Investor and SOK, will not be entitled, by virtue of being holders of the Warrants, to vote, to consent, to receive dividends, to receive notice as shareholders with respect to any meeting of shareholders for the election of the Company’s directors or any other matter, or to exercise any rights whatsoever as our shareholders. If, however, the Company decides to declare a dividend or make distributions of its assets (the “**Distribution**”), the Investor and SOK will be entitled to such Distribution to the same extent that the Investor and SOK would have participated therein if the Investor or SOK had held the number of share of Common Stock acquirable upon complete exercise of the Warrants.

At any time commencing on the earliest to occur of (x) the public disclosure of any change of control, (y) the consummation of any change of control and (z) the Investor or SOK first becoming aware of any change of control through the date that is ninety (90) days after the public disclosure of the consummation of such change of control by the Company pursuant to a Current Report on Form 8-K filed with the SEC, the Company or the successor entity (as the case may be) may have to purchase the Warrants from the Investor and SOK in an amount equal to the Black Scholes Value (as defined in the Warrants).

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### **Critical Accounting Policies and Estimates**

The discussion and analysis of our financial condition and results of operations are based upon our audited Financial Statements, which have been prepared in accordance with U.S. Generally Accepted Accounting Principles (“GAAP”). The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of our financial statements, the reported amounts of revenues and expenses during the reporting periods presented, as well as our disclosures of contingent assets and liabilities. On an on-going basis, we evaluate our estimates and assumptions, including, but not limited to, fair value of stock-based compensation, fair value of acquired intangible assets and goodwill, useful lives of intangible assets and property and equipment, income taxes, and contingencies and litigation.

We base our estimates and assumptions on our historical experience. We also used any other pertinent information available to us at the time that these estimates and assumptions are made. We believe that these estimates and assumptions are reasonable under the circumstances and form the basis for our making judgments about the carrying values of our assets and liabilities that are not readily apparent from other sources. Actual results and outcomes could differ from our estimates.

Our significant accounting policies are described in “Note 1 – Summary of Significant Accounting Policies,” in Notes to Financial Statements of this prospectus. We believe that the following discussion addresses our critical accounting policies and reflects those areas that require more significant judgments, and use of estimates and assumptions in the preparation of our Financial Statements.

**Revenue Recognition.** We recognize revenue in accordance with the SEC’s Staff Accounting Bulletin Topic 13 Revenue Recognition and ASC 605 – Revenue Recognition.

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable and collectability is probable. Delivery is considered to have occurred upon either shipment of the product or arrival at its destination based on the shipping terms of the transaction. Our standard terms specify that shipment is FOB Skyline and we will, therefore, recognize revenue upon shipment in most cases. This revenue recognition policy applies to shipments of our STREAMWAY FMS units as well as shipments of cleaning solution and filter consumables. When these conditions are satisfied, we recognize gross product revenue, which is the price we charge generally to our customers for a particular product. Under our standard terms and conditions, there is no provision for installation or acceptance of the product to take place prior to the obligation of the customer. The customer’s right of return is limited only to our standard one-year warranty, whereby we replace or repair, at our option. We believe it would be rare that the STREAMWAY FMS unit or significant quantities of cleaning solution and filter consumables may be returned. Additionally, since we buy both the STREAMWAY FMS units and cleaning solution and filter consumables from “turnkey” suppliers, we would have the right to replacements from the suppliers if this situation should occur.

**Stock-Based Compensation.** Effective January 1, 2006, we adopted ASC 718-Compensation- Stock Compensation (“ASC 718”). Under ASC 718 stock-based employee compensation cost is recognized using the fair value based method for all new awards granted after January 1, 2006 and unvested awards outstanding at January 1, 2006. Compensation costs for unvested stock options and non-vested awards that were outstanding at January 1, 2006, are being recognized over the requisite service period based on the grant-date fair value of those options and awards, using a straight-line method. We elected the modified-prospective method in adopting ASC 718 under which prior periods are not retroactively restated.

ASC 718 requires companies to estimate the fair value of stock-based payment awards on the date of grant using an option-pricing model. We use the Black-Scholes option-pricing model which requires the input of significant assumptions including an estimate of the average period of time employees and directors will retain vested stock options before exercising them, the estimated volatility of our common stock price over the expected term, the number of options that will ultimately be forfeited before completing vesting requirements and the risk-free interest rate.

Because we do not have significant historical trading data on our common stock we relied upon trading data from a composite of 10 medical companies traded on major exchanges and 15 medical companies quoted

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by the OTC Bulletin Board to help us arrive at expectations as to volatility of our own stock when broader public trading commences. In 2013 the Company experienced significant exercises of options and warrants. The options raised \$6,500 in capital. Warrants exercised for cash produced \$1,330,000 of capital. In the case of options and warrants issued to consultants and investors we used the legal term of the option/warrant as the estimated term unless there was a compelling reason to use a shorter term. The measurement date for employee and non-employee options and warrants is the grant date of the option or warrant. The vesting period for options that contain service conditions is based upon management's best estimate as to when the applicable service condition will be achieved. Changes in the assumptions can materially affect the estimate of fair value of stock-based compensation and, consequently, the related expense recognized. The assumptions we use in calculating the fair value of stock-based payment awards represent our best estimates, which involve inherent uncertainties and the application of management's judgment. As a result, if factors change and we use different assumptions, our equity-based compensation expense could be materially different in the future. See "Note 3 – Stockholders' Deficit, Stock Options and Warrants" in Notes to Financial Statements included in this prospectus for additional information.

When an option or warrant is granted in place of cash compensation for services, we deem the value of the service rendered to be the value of the option or warrant. In most cases, however, an option or warrant is granted in addition to other forms of compensation and its separate value is difficult to determine without utilizing an option pricing model. For that reason we also use the Black-Scholes option-pricing model to value options and warrants granted to non-employees, which requires the input of significant assumptions including an estimate of the average period that investors or consultants will retain vested stock options and warrants before exercising them, the estimated volatility of our common stock price over the expected term, the number of options and warrants that will ultimately be forfeited before completing vesting requirements and the risk-free interest rate. Changes in the assumptions can materially affect the estimate of fair value of stock-based compensation and, consequently, the related expense recognized. Since we have no trading history in our common stock and no first-hand experience with how our investors and consultants have acted in similar circumstances, the assumptions we use in calculating the fair value of stock-based payment awards represent our best estimates, which involve inherent uncertainties and the application of management's judgment. As a result, if factors change and we use different assumptions, our equity-based consulting and interest expense could be materially different in the future.

Since our common stock has no significant public trading history we were required to take an alternative approach to estimating future volatility and the future results could vary significantly from our estimates. We compiled historical volatilities over a period of 2 to 7 years of 10 small-cap medical companies traded on major exchanges and 15 medical companies in the middle of the market cap size range on the OTC Bulletin Board and combined the results using a weighted average approach. In the case of standard options to employees we determined the expected life to be the midpoint between the vesting term and the legal term. In the case of options or warrants granted to non-employees, we estimated the life to be the legal term unless there was a compelling reason to make it shorter.

### **Valuation of Intangible Assets**

We review identifiable intangible assets for impairment in accordance with ASC 350 – Intangibles – Goodwill and Other, whenever events or changes in circumstances indicate the carrying amount may not be recoverable. Our intangible assets are currently solely the costs of obtaining trademarks and patents. Events or changes in circumstances that indicate the carrying amount may not be recoverable include, but are not limited to, a significant change in the medical device marketplace and a significant adverse change in the business climate in which we operate. If such events or changes in circumstances are present, the undiscounted cash flows method is used to determine whether the intangible asset is impaired. Cash flows would include the estimated terminal value of the asset and exclude any interest charges. If the carrying value of the asset exceeds the undiscounted cash flows over the estimated remaining life of the asset, the asset is considered impaired, and the impairment is measured by reducing the carrying value of the asset to its fair value using the discounted cash flows method. The discount rate utilized is based on management's best estimate of the related risks and return at the time the impairment assessment is made. The Company wrote off the entire original STREAMWAY product patent of \$140,588 in June 2013. The balance represented

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intellectual property in the form of patents for our original STREAMWAY product. The Company's enhanced STREAMWAY product has a new patent pending.

### **Recent Accounting Developments**

See Note 1 – “Summary of Significant Accounting Policies – Recent Accounting Developments” of the Financial Statements included in this prospectus.

### **Off-Balance Sheet Transactions**

We have no off-balance sheet transactions.

## BUSINESS

### Overview

We are a development stage medical device company manufacturing an environmentally conscientious system for the collection and disposal of infectious fluids that result from surgical procedures and post-operative care. We own patent rights to our products and distribute our products to medical facilities where bodily and irrigation fluids produced during surgical procedures must be contained, measured, documented, and disposed. Our products minimize the exposure potential to the healthcare workers who handle such fluids. Our goal is to create products that dramatically reduce staff exposure without significant changes to established operative procedures, historically a major stumbling block to innovation and product introduction. In addition to simplifying the handling of these fluids, we believe our technologies provide cost savings to facilities over the aggregate costs incurred today using the traditional canister method of collection, neutralization, and disposal. We sell our products through an experienced in-house sales force. The Company has hired 4 regional managers in addition to the 2 regional managers currently on staff enhancing our national coverage. We also intend to utilize independent distributors and manufacturer's representatives in the United States and Europe, initially, and eventually to other areas of the world.

The Company was originally incorporated on April 23, 2002 in Minnesota as BioDrain Medical, Inc. Effective August 6, 2013, the Company changed its name to Skyline Medical Inc. Pursuant to an Agreement and Plan of Merger dated effective December 16, 2013, the Company merged with and into a Delaware corporation with the same name that was its wholly-owned subsidiary, with such Delaware Corporation as the surviving corporation of the merger. Our address is 2915 Commers Drive, Suite 900, Eagan, Minnesota 55121. Our telephone number is 651-389-4800, and our website address is [www.skylinemedical.com](http://www.skylinemedical.com). Information on our website is not included or incorporated by reference in this prospectus.

### Industry and Market Analysis

#### *Infectious and Bio-hazardous Waste Management*

There has long been recognition of the collective potential for ill effects to healthcare workers from exposure to infectious/bio-hazardous materials. Federal and state regulatory agencies have issued mandatory guidelines for the control of such materials, and in particular, bloodborne pathogens. The medical device industry has responded to this need by developing various products and technologies to limit exposure or to alert workers to potential exposure.

The presence of infectious materials is most prevalent in the surgical suite and post-operative care units where often, large amounts of bodily fluids, including blood, bodily and irrigation fluids are continuously removed from the patient during the surgical procedure. Surgical teams and post-operative care personnel may be exposed to these potentially serious hazards during the procedure via direct contact of blood materials or more indirectly via splash and spray.

According to the Occupational Safety and Health Administration ("OSHA"), workers in many different occupations are at risk of exposure to bloodborne pathogens, including Hepatitis B and C, and HIV/AIDS. First aid team members, housekeeping personnel, nurses and other healthcare providers are examples of workers who may be at risk of exposure.

In 1991, OSHA issued the Bloodborne Pathogens Standard to protect workers from this risk. In 2001, in response to the Needlestick Safety and Prevention Act, OSHA revised the Bloodborne Pathogens Standard. The revised standard clarifies (and emphasizes) the need for employers to select safer needle devices and to involve employees in identifying and choosing these devices. The revised standard also calls for the use of "automated controls" as it pertains to the minimization of healthcare exposure to bloodborne pathogens. Additionally, employers are required to have an exposure control plan that includes universal precautions to be observed to prevent contact with blood or other potentially infectious materials, such as implementing work practice controls, requiring personal protective equipment and regulating waste and waste containment. The exposure control plan is required to be reviewed and updated annually to reflect new or modified tasks and procedures, which affect occupational exposure and to reflect changes in technology that eliminate or reduce exposure to bloodborne pathogens.

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According to the American Hospital Association's (AHA) Hospital Statistics, 2013 edition, America's hospitals performed 86 million surgeries. This number does not include the many procedures performed at surgery centers across the country.

The majority of these procedures produce potentially infectious materials that must be disposed with the lowest possible risk of cross-contamination to healthcare workers. Current standards of care allow for these fluids to be retained in canisters, located in the operating room where they can be monitored throughout the surgical procedure. Once the procedure is complete these canisters and their contents are disposed using a variety of methods all of which include manual handling and result in a heightened risk to healthcare workers for exposure to their contents. A Frost & Sullivan research report from April 24, 2006 estimates that 60,000,000 suction canisters are sold each year and the estimated market value of canisters is upwards of \$120,000,000. According to the average estimate of three manufacturers and three different solidifiers as reported in a research report by Frost & Sullivan in 2003 and in an article titled "Liquid Waste Management & Disposal" that was published in *Infection Control Today* in 2006, there is an average cost of \$2.00 per canister, \$2.00 per container of solidification powder and an average disposal cost of \$0.30/lb. of infectious waste at approximately 7.5 lbs. per canister, the estimated disposal cost to the hospitals who use solidifiers is \$6.25 per canister. This cost increases significantly for disposal of higher capacity containers.

A study by the Lewin Group, prepared for the Health Industry Group Purchasing Association in April 2007, reports that infectious fluid waste accounts for more than 75% of U.S. hospitals biohazard disposal costs. The study also includes findings from a bulletin published by the University of Minnesota's Technical Assistance Program, "A vacuum system that uses reusable canisters or empties directly into the sanitary sewer can help a facility cut its infectious waste volume, and save money on labor, disposal and canister purchase costs." The Minnesota's Technical Assistance Program bulletin also estimated that, in a typical hospital, "...\$75,000 would be saved annually in suction canister purchase, management and disposal cost if a canister-free vacuum system was installed."

We expect the hospital surgery market to continue to increase due to population growth, the aging of the population, expansion of surgical procedures to new areas, for example, use of the endoscope, which requires more fluid management, and new medical technology. According to the American Institute of Architects Consensus Construction Forecast, "Health care is expected to see even stronger growth. With recent emphasis on increasing health-care coverage, including several state mandates for universal or near-universal coverage, health-care construction has become one of the fastest growing institutional construction categories. Panel members are projecting an 8.5 percent increase in spending in 2009, followed by an additional 5 percent gain in 2010."

There are currently approximately 40,000 operating rooms and surgical centers in the U.S. (AHA, *Hospital Statistics*, 2008). The hospital market has typically been somewhat independent of the U.S. economy; therefore we believe that our targeted market is not cyclical, and the demand for our products will not be heavily dependent on the state of the economy. We benefit by having our products address both the procedure market of nearly 70 million procedures (AHA, *Beyond Health Care*; January 2009) as well as the hospital operating room market (approximately 40,000 operating rooms).

### ***Current Techniques of Collecting Infectious Fluids***

Typically, during the course of the procedure, fluids are continuously removed from the surgical site via wall suction and tubing and collected in large canisters (1,500 – 3,000 milliliters (ml) capacity or 1.5 – 3.0 liters) adjacent to the surgical table.

These canisters, made of glass or high impact plastic, have graduated markers on them allowing the surgical team to make estimates of fluid loss in the patient both intra-operatively as well as for post-operative documentation. Fluid contents are retained in the canisters until the procedure is completed or until the canister is full and needs to be removed. During the procedure the surgical team routinely monitors fluid loss using the measurement calibrations on the canister and by comparing these fluid volumes to quantities of saline fluid introduced to provide irrigation of tissue for enhanced visualization and to prevent drying of exposed tissues. After the procedure is completed the fluids contained in the canisters are measured and a



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calculation of total blood loss is determined. This is done to ensure no excess fluids of any type remain within the body cavity or that no excessive blood loss has occurred, both circumstances that may place the patient at an increased risk post-operatively.

Once total blood loss has been calculated, the healthcare personnel must dispose of the fluids. This is typically done by manually transporting the fluids from the operating room to a waste station and directly pouring the material into a sink that drains to the sanitary sewer where it is subsequently treated by the local waste management facility, a process that exposes the healthcare worker to the most risk for direct contact or splash exposure. Once emptied these canisters are placed in large, red pigmented, trash bags and disposed of as infectious waste – a process commonly referred to as “red-bagging.”

Alternatively, the canisters may be opened in the operating room and a gel-forming powder is poured into the canister, rendering the material gelatinous. These gelled canisters are then red-bagged in their entirety and removed to a bio-hazardous/infectious holding area for disposal. In larger facilities the canisters, whether pre-treated with gel or not, are often removed to large carts and transported to a separate special handling area where they are processed and prepared for disposal. Material that has been red-bagged is disposed of separately, and more expensively, from other medical and non-medical waste by companies specializing in that method of disposal.

Although all of these protection and disposal techniques are helpful, they represent a piecemeal approach to the problem and fall short of providing adequate protection for the surgical team and other workers exposed to infectious waste. A major spill of fluid from a canister, whether by direct contact as a result of leakage or breakage, splash associated with the opening of the canister lid to add gel, while pouring liquid contents into a hopper, or during the disposal process, is cause for concern of acute exposure to human blood components – one of the most serious risks any worker faces in the performance of his or her job. Once a spill occurs, the entire area must be cleaned and disinfected and the exposed worker faces a potential of infection from bloodborne pathogens. These pathogens include, but are not limited to, HIV, HPV, and other infectious agents. Given the current legal liability environment the hospital, unable to identify at-risk patients due to concerns over patient rights and confidentiality, must treat every exposure incident as a potentially infectious incident and treat the exposed employee according to a specific protocol that is both costly to the facility and stressful to the affected employee and his or her co-workers. In cases of possible exposure to communicable disease, the employee could be placed on paid administrative leave, frequently involving worker's compensation, and additional workers must be assigned to cover the affected employee's responsibilities. The facility bears the cost of both the loss of the affected worker and the replacement healthcare worker in addition to any ongoing health screening and testing of the affected worker to confirm if any disease has been contracted from the exposure incident. Employee morale issues also weigh heavily on staff and administration when a healthcare worker suffers a potentially serious exposure to bloodborne pathogens. Canisters are the most prevalent means of collecting and disposing of infectious fluids in hospitals today. Traditional, non-powered canisters and related suction and fluid disposable products are exempt and do not require FDA clearance.

We believe that our virtually hands free direct-to-drain technology will (a) significantly reduce the risk of healthcare worker exposure to these infectious fluids by replacing canisters, (b) further reduce the risk of worker exposure when compared to powered canister technology that requires transport to and from the operating room, (c) reduce the cost per procedure for handling these fluids, and (d) enhance the surgical team's ability to collect data to accurately assess the patient's status during and after procedures.

In addition to the traditional canister method of waste fluid disposal, several new powered medical devices have been developed which address some of the deficiencies described above. MD Technologies, Inc., DeRoyal (formerly Waterstone), Domo Medical Systems, Inc. (Zimmer) and Stryker Instruments have all developed systems that provide for disposal into the sanitary sewer without pouring the infectious fluids directly through a hopper disposal or using expensive gel powders and most are sold with 510(k) concurrence from the FDA. Cardinal Health, Inc. has received 510(k) concurrence to market a similar device that it has recently started advertising. Most of these competing products continue to utilize some variant on the existing canister technology, and while not directly addressing the canister, most have been successful in eliminating the need for expensive gel and its associated handling and disposal costs. Our existing competitors that

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already have products on the market have a clear competitive advantage over us in terms of brand recognition and market exposure. In addition, the aforementioned companies have extensive marketing and development budgets that could overpower an early stage company like ours. We believe that Stryker Instruments has the dominant market share position. We do not believe Cardinal Health, Inc., though having FDA concurrence, has made significant sales into the market.

### **Products**

#### ***The STREAMWAY Fluid Management System (“FMS”)***

The STREAMWAY Automated Surgical Fluid Waste Management System suctions surgical waste fluid from the patient using standard surgical tubing. The surgical waste fluid passes through our proprietary disposable filters and into the STREAMWAY System. The STREAMWAY System maintains continuous suction to the surgical field at all times. A simple, easy to use Human Interface Display screen guides the user through the set up process, ensuring that a safe vacuum level is identified and set by the user for each procedure and additionally guides them through the cleaning process.

Fluid is collected utilizing negative pressure and passes through one tank and into another during the collection process. After a predetermined amount of fluid is sensed, a valve is activated that insulates one tank from the other, the volume of fluid is identified and recorded and the tank is emptied into the facilities sewer drainage system. During this relief, measuring and draining process, negative pressure remains constant to the field. The STREAMWAY System constantly updates and displays the fluid volume removed during the procedure which allows the surgical team to immediately assess the total amount of fluid removed from the patient at any point during the procedure.

The STREAMWAY System is unique to the industry in that it allows for continuous suction to the surgical field and provides unlimited capacity to the user so no surgical procedure will ever have to be interrupted to change canisters. It is wall mounted and takes up no valuable operating room space.

The FMS will replace the manual process of collecting fluids in canisters and transporting and dumping in sinks outside of the operating room that is still being used by many hospitals and surgical centers. The manual process, involving canisters, requires that the operating room personnel open the canisters that contain waste fluid, often several liters, at the end of the surgical procedure and either add a solidifying agent or empty the canisters in the hospital drain system. Some facilities require that used canisters be cleaned by staff and reused. It is during these procedures that there is increased potential for contact with the waste fluid through splashing or spills. The FMS eliminates the use of canisters and these cleaning and disposal steps by collecting the waste fluid in the internal collection chamber and automatically disposing of the fluid with no handling by personnel. Each procedure requires the use of a disposable filter. At the end of each procedure, a proprietary cleaning fluid is attached to the FMS and an automatic cleaning cycle ensues, making the FMS ready for the next procedure. The cleaning fluid bottle is attached to the port on the FMS device. The cleaning fluid bottle and its contents are not contaminated and are used to clean the internal fluid pathway in the FMS device to which personnel have no exposure. During the cleaning cycle, the cleaning fluid is pulled from the bottle into the FMS, and then disposed in the same manner as the waste fluid from the surgical case. At the end of the cleaning cycle, the bottle is discarded. The filter and any suction tubing used during the procedure must be disposed of in the same manner as suction tubing used with the canister system. Handling of this tubing does present the potential for personnel exposure but that potential is minimal.

We believe our product provides substantial cost savings and improvements in safety in facilities that still use manual processes. In cases where healthcare organizations re-use canisters, the FMS cleaning process eliminates the need for cleaning of canisters for re-use. The FMS reduces the safety issues facing operating room nurses, the cost of the handling process, and the amount of infectious waste generated when the traditional method of disposing of canisters is used. The FMS is fully automated, does not require transport to and from the operating room and eliminates any canister that requires emptying. It is positioned to penetrate its market segment due to its virtually hands free operation, simple design, ease of use, continuous suction, continuous flow, unlimited capacity and efficiency in removal of infectious waste with minimal exposure of operating room personnel to potentially infectious material.

In contrast to competitive products, the wall-mounted FMS does not take up any operating room floor space and it does not require the use of any external canisters or handling by operating room personnel. It

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does require a dedicated system in each operating room where it is to be used. The FMS is the only known direct-to-drain system that is wall-mounted and designed to collect, measure and dispose of, surgical waste. The product from DeRoyal does not collect surgical waste fluid and is used in conjunction with traditional canisters to assist in emptying the canisters. Other systems on the market are portable, meaning that they are rolled to the bedside for the surgical case and then rolled to a cleaning area, after the surgery is complete, and use canisters, which still require processing or require a secondary device (such as a docking station) to dispose of the fluid in the sanitary sewer after it has been collected. They are essentially powered canisters. A comparison of the key features of the devices currently marketed and the FMS is presented in the table below.

**Key Feature Comparison**

<b>Feature</b>	<b>Skyline Medical Inc.</b>	<b>Stryker Instruments</b>	<b>DeRoyal</b>	<b>Dornoch Medical Systems, Inc. (Zimmer)</b>	<b>MD Technologies, Inc.</b>
Portable to Bedside vs. Fixed Installation	Fixed	Portable	Fixed	Portable	Fixed
Uses Canisters	No	Yes	Yes	Yes	No
Secondary Installed Device Required for Fluid Disposal	No	Yes	Yes	Yes	No
Numeric Fluid Volume Measurement	Yes	Yes	No	Yes	Optional
Unlimited Fluid Capacity	Yes	No	No	No	Yes
Continuous, Uninterrupted Vacuum	Yes	No	No	No	No
Installation Requirements:					
Water	No	Yes	Yes	Yes	No
Sewer	Yes	Yes	Yes	Yes	Yes
Vacuum	Yes	No	No	No	Yes

The FMS system may be installed on or in the wall during new construction or renovation or installed in a current operating room by connecting the device to the hospital’s existing sanitary sewer drain and wall suction systems. With new construction or renovation, the system will be placed in the wall and the incremental costs are minimal, limited to connectors to the hospital drain and suction systems (which systems are already required in an operating room), the construction of a frame to hold the FMS in position, and minimal labor. The fluid collection chamber is internal to the FMS unit and requires no separate installation. Based upon our consultations with several architects, we believe that there is no appreciable incremental expense in planning for the FMS system during construction.

For on-the-wall installation in a current operating room, the location of the FMS may be chosen based on proximity to the existing hospital drain and suction systems. Installation will require access to those systems through the wall and connection to the systems in a manner similar to that for within-the-wall installation. The FMS system is mounted on the wall using a mounting bracket supplied with the system and standard stud or drywall attachments.

By comparison, the majority of competing products are mobile, allowing movement from room to room. The mobility adds time and labor to the process and increases the chance of worker exposure to waste fluids but also allows the hospital to potentially purchase less than one mobile unit for each operating room. With the FMS, a unit must be installed in each room where it is intended to be used.

Once installed, the FMS has inflow ports positioned on the front of the device that effectively replace the current wall suction ports most commonly used to remove fluids during surgery. Additionally, a disposable external filter, which is provided as part of our disposable cleaning kit, allows for expansion to additional inflow suction ports by utilizing one or two dual port filters.

Although the FMS is directly connected to the sanitary sewer, helping to reduce potential exposure to infectious fluids, it is possible that installation of the system will temporarily cause inconvenience and lost productivity as the operating rooms will need to be taken off line temporarily.

One of the current techniques utilized by Stryker, Cardinal Health, and other smaller companies typically utilizes two to eight canisters positioned on the floor or on elaborate rolling containers with tubing connected

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to the hospital suction system and to the operative field. Once the waste fluids are collected, they must be transported out of the operating room and disposed of using various methods. These systems take up floor space in and around the operating room and require additional handling by hospital personnel, thereby increasing the risk of exposure to infectious waste fluids generated by the operating room procedure. Handling infectious waste in this manner is also more costly.

A summary of the features of the wall unit include:

- Minimal Human Interaction. The wall-mounted FMS provides a small internal reservoir that keeps surgical waste isolated from medical personnel and disposes the medical waste directly into the hospital sanitary sewer with minimal medical personnel interaction. This minimal interaction is facilitated by the automated electronic controls and computerized LCD touch-screen allowing for simple and safe single touch operation of the FMS.
- Fluid Measurement. The STREAMWAY System volume measurement allows for in-process, accurate measurement of blood/saline suctioned during the operative procedure, and eliminates much of the estimation of fluid loss currently practiced in the operating room. This will be particularly important in minimally invasive surgical procedures, where accounting for all fluids, including saline added for the procedure, is vital to the operation. The surgical team can view in real time the color of the extracted or evacuated fluid through the viewing window on the system.
- Cleaning Solution. A bottle of cleaning solution, proprietary to and sold by Skyline Medical, is used for the automated cleaning cycle at the conclusion of each procedure and prepares the STREAMWAY System for the next use, reducing operating room turnover time. The cleaning solution is intended to clean the internal tubing, pathways, and chamber within the system. The cleaning solution bottle is easily attached to the STREAMWAY System by inserting the bottle into the mount located on the front of the unit and inverting the bottle. The automated cleaning process takes less than five minutes and requires minimal staff intervention. The disposable cleaning fluid bottle collapses at the end of the cleaning cycle rendering it unusable; therefore it cannot be refilled with any other solution. The instructions for use clearly state that the Skyline Medical cleaning fluid, and only the Skyline Medical cleaning fluid, must be used with the STREAMWAY System following each surgical case. The warranty is voided if any other solution is used.
- Procedure Filters. One or two filters, depending on the type of procedure, will be used for every surgical procedure. The filter has been developed by Skyline Medical, is proprietary to the STREAMWAY System and is only sold through Skyline Medical. The filter is a two port, bifurcated, disposable filter that contains a tissue trap that allows staff to capture a tissue sample and send to pathology if needed. The filters are disposed of after each procedure. The cleaning fluid and filter are expected to be a substantial revenue generator for the life of the STREAMWAY System.
- Ease of Use. The FMS simply connects to the existing suction tubing from the operative field (causing no change to the current operative methods). Pressing the START button on the FMS touch screen enacts a step by step instruction with safety questions ensuring that the correct amount of suction is generated minimizing the learning curve for operation at the surgical site.
- Installation. We will arrange installation of the FMS products through a partnership or group of partnerships. Such partnerships will include, but not be limited to, local plumbers, distribution partners, manufacturer's representatives, hospital supply companies and the like. We will train our partners and standardize the procedure to ensure the seamless installation of our products. The FMS is designed for minimal interruption of operating room and surgical room utilization. Plug-and-play features of the design allow for almost immediate connection and hook up to hospital utilities for wall-mounted units allowing for quick start-up post-installation.
- Sales Channel Partners. Sales Channel Partners. We expect the FMS will be sold to end-users through a combination of independent stocking distributors, manufacturer's representatives, and direct sales personnel. We intend for all personnel involved in direct contact with the end-user will have extensive training and will be approved by Skyline. We plan to maintain exclusive agreements between Skyline and the sales channel partners outlining stocking expectations, sales objectives,

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target accounts and the like. Contractual agreements with the sales channel partners will be reviewed on an annual basis and expect that such agreements will contain provisions allowing them to be terminated at any time by Skyline based on certain specified conditions.

- Competitive Pricing. The list sales price to a hospital or surgery center is \$21,900 per system (one per operating room - installation extra) and \$24 per unit retail for the proprietary consumable kit to the U.S. hospital market.

### **Intellectual Property**

We believe that in order to maintain a competitive advantage in the marketplace, we must develop and maintain protection of the proprietary aspects of our technology. We rely on a combination of patent, trade secret and other intellectual property rights and measures to protect our intellectual property.

We spent approximately \$235,000 in 2013 and \$15,000 in 2012 on research and development. On January 25, 2014 the Company filed a non-provisional PCT Application No. PCT/US2014/013081 claiming priority from the U.S. Provisional Patent Application, number 61756763 which was filed one year earlier on January 25, 2013. The PCT makes it possible to seek patent protection for an invention simultaneously in each of 148 countries, including the United States, by filing this “international” patent application instead of filing several separate national or regional patent applications.

Our PCT patent application is for an enhanced model of the surgical fluid waste management system that has embodiments, based on our patent attorney’s recommendations, that are patentable over all prior art and will not infringe on any existing patents. This PCT Application adds features that are novel and non-obvious over all the Company’s previously filed applications. A feature claimed in the Patent is the ability to maintain continuous suction to the surgical field while simultaneously measuring, recording and evacuating fluid to the facilities sewer drainage system. This provides for continuous operation of the STREAMWAY System unit in suctioning waste fluids, which means that the unit does not have to be shut off or paused during a surgical operation, for example, to empty a fluid collection container or otherwise dispose of the collected fluid. We believe that this continuous operation and unlimited capacity feature provides us with a significant competitive advantage, particularly on large fluid generating procedures. All competing products, except for MD Technologies, have a finite fluid collection capacity necessitating that the device be emptied when capacity is reached during the surgical procedure. In the case of MD Technologies their system has an unlimited capacity but the process is not continuous because they have to interrupt the process to manually switch over to a new container and drain the original container in order to have it ready for use when the second container is full.

The Company also received a European patent in April 2007 (Patent No. EP1539580), a U.S. patent in December 2008 (U.S. Patent No. 7,469,727), a U.S. patent in February 2012 (U.S. Patent No. 8,123,731) and a Canadian patent in April 2011 (Number 2,495,747) (collectively, the “Patents”). These Patents will begin to expire on August 8, 2023.

We also rely upon trade secrets, continuing technological innovations and licensing opportunities to develop and maintain our competitive position. We seek to protect our trade secrets and proprietary know-how, in part, with confidentiality agreements with consultants, vendors and employees, although we cannot be certain that the agreements will not be breached, or that we will have adequate remedies for any breach.

### **The Disposable Kit**

The disposable kit is an integral, critical component of the FMS and our total value proposition to the customer. It consists of a proprietary, pre-measured amount of cleaning solution in a plastic bottle that attaches to the FMS. The disposal cleaning kit also includes an in-line filter with single or multiple suction ports. The proprietary cleaning solution placed in the specially designed holder is attached and recommended to be used following each surgical procedure. Due to the nature of the fluids and particles removed during surgical procedures, the FMS is recommended to be cleaned following each use. Utilizing the available vacuum of the wall system, the proprietary cleaning fluid is drawn into the FMS to provide a highly effective cleaning process that breaks up bio-film at the cellular level. Proper cleaning is required for steady, dependable and repeated FMS performance and for maintenance of the warranty of the FMS.

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The Skyline disposables are a critical component of our business model. The disposables have the “razor blade business model” characteristic with an ongoing stream of revenue for every FMS unit installed, and revenues from the sale of the kits are expected to be significantly higher over time than the revenues from the sales of the unit. Our disposable, dual use filter is designed specifically for use only on our FMS. The filter is used only once per procedure followed by immediate disposal. Our operation instructions and warranty require that a Skyline filter is used for every procedure. There are no known off the shelf filters that will fit our FMS. We have developed a more effective and cost efficient filter, with intent to patent. We have exclusive distribution rights to the disposable fluid and facilitate the use of only our fluid for cleaning following procedures by incorporating a special adapter to connect the fluid to the connector on the FMS system. We will also tie the fluid usage, which we will keep track of with the FMS software, to the product warranty. While it could be possible for other manufacturers to provide fluids for utilization in this process, it would require that they manufacture an adapter compatible with our connector on the FMS, obtain a container that fits in the specially designed container holder on the FMS and perform testing to demonstrate that any other fluid would not damage the FMS. We believe that these barriers and the warranty control will allow us to achieve substantial revenue from our cleaning fluid. The instructions for use that accompanies the product will clearly state how the fluid is to be hooked up to the FMS machine. Further, a diagram on the FMS will also assist the user in attaching the fluid bottle to the machine. This will be a very simple task, and we do not anticipate that any training of operating room staff will be necessary.

All installations of our FMS product will be completed by either a hospital appointed service technician or a service and maintenance organization that is familiar with completing such installations in health care settings. We have had conversations with multiple providers and expect to reach agreements to perform this function in the first quarter of 2014. The general availability of these types of service and maintenance personnel in the health care sector should not hinder us from forming a beneficial relationship in this area.

### **Corporate Strategy**

We intend to succeed by deploying a strategy of focused expansion within our core product and market segments, while utilizing a progressive approach to manufacturing and marketing to ensure maximum flexibility and profitability.

Our strategy is to:

- *Develop a complete line of wall-mounted fluid evacuation systems for use in hospital operating rooms, radiological rooms and free standing surgery centers as well as clinics and physicians' offices.* Initially, we have developed the FMS to work in hospital operating rooms and surgical centers. This device was developed for use with the wall vacuum suction currently installed in hospitals. Opportunities for future products include an FMS developed for post-operation and recovery rooms with multiple inlet ports and multiple volume measurements that may incorporate an on-board vacuum supply.
- *Provide products that greatly reduce worker and patient exposure to harmful materials present in infectious fluids and that contribute to an adverse working environment.* As one of the only stand-alone surgical fluid disposal systems directly connected to the sanitary sewer, the FMS could advance the manner in which such material is collected, measured and disposed of in operating rooms, post-operating recovery, emergency rooms and intensive care settings by eliminating the need to transport a device to the patient bedside and remove it for emptying and cleaning at the end of the procedure. The cost of such exposures, measured in terms of human suffering, disease management costs, lost productivity, liability or litigation, will be, when properly leveraged, the strongest motivating factor for facilities looking at investing in the FMS line of products.
- *Utilize existing medical products independent distributors and manufacturer's representatives to achieve the desired market penetration.* Contacts have been established with several existing medical products distributors and manufacturer's representatives and interest has been generated regarding the sales of the FMS and cleaning kits.

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- *Continue to utilize operating room consultants, builders and architects as referrals to hospitals and day surgery centers.* To date, the STREAMWAY System has achieved market acceptance through the installation of more than thirty (30) FMS systems. The product has received numerous references from users and was also recognized by LifeScience Alley as a top ten finalist in their new technology showcase. Additionally, Skyline has become a member of Practice Greenhealth; highlighting the positive environmental impact of the STREAMWAY System.

Other strategy may also include:

- *Employing a lean operating structure, while utilizing the latest trends and technologies in manufacturing and marketing, to achieve both market share growth and projected profitability.*
- *Providing a leasing program and/or “pay per use” program as alternatives to purchasing.*
- *Providing service contracts to establish an additional revenue stream.*
- *Utilizing the manufacturing experience of our management team to develop sources of supply and manufacturing to reduce costs while still obtaining excellent quality. While cost is not a major consideration in the roll-out of leading edge products, we believe that being a low-cost provider will be important long term.*
- *Offering an innovative warranty program that is contingent on the exclusive use of our disposable kit to enhance the success of our after-market disposable products.*

## **Technology and Competition**

### ***Fluid Management for Surgical Procedures***

The management of surgical waste fluids produced during and after surgery is a complex mix of materials and labor that consists of primary collection of fluid from the patient, transportation of the waste fluid within the hospital to a disposal or processing site and disposal of that waste either via incineration or in segregated landfills.

Once the procedure has ended, the canisters currently being used in many cases, and their contents must be removed from the operating room and disposed. There are several methods used for disposal, all of which present certain risks to the operating room team, the crews who clean the rooms following the procedure and the other personnel involved in their final disposal. These methods include:

- *Direct Disposal Through the Sanitary Sewer.* In virtually all municipalities, the disposal of liquid blood may be done directly to the sanitary sewer where it is treated by the local waste management facility. This practice is approved and recommended by the EPA. In most cases these municipalities specifically request that disposed bio-materials not be treated with any known anti-bacterial agents such as glutaldehyde, as these agents not only neutralize potentially infectious agents but also work to defeat the bacterial agents employed by the waste treatment facilities themselves. Disposal through this method is fraught with potential exposure to the service workers, putting them at risk for direct contact with these potentially infectious agents through spillage of the contents or via splash when the liquid is poured into a hopper — a specially designated sink for the disposal of infectious fluids. Once the infectious fluids are disposed of into the hopper, the empty canister is sent to central processing for re-sterilization (glass and certain plastics) or for disposal in the bio-hazardous/infectious waste generated by the hospital (red-bagged).
- *Conversion to Gel for Red-Bag Disposal.* In many hospital systems the handling of this liquid waste has become a liability issue due to worker exposure incidents and in some cases has even been a point of contention during nurse contract negotiations. Industry has responded to concerns of nurses over splash and spillage contamination by developing a powder that, when added to the fluid in the canisters, produces a viscous, gel-like substance that can be handled more safely. After the case is completed and final blood loss is calculated, a port on the top of each canister is opened and the powder is poured into it. It takes several minutes for the gel to form, after which the canisters are placed on a service cart and removed to the red-bag disposal area for disposal with the other infectious waste.

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There are four major drawbacks to this system:

- It does not ensure protection for healthcare workers, as there remains the potential for splash when the top of the canister is opened.
- Based on industry pricing data, the total cost per canister increases by approximately \$2.00.
- Disposal costs to the hospital increase dramatically as shipping, handling and landfill costs are based upon weight rather than volume in most municipalities. The weight of an empty 2,500 ml canister is about 1 pound. A canister and its gelled contents weigh about 7.5 pounds, and the typical cost to dispose of medical waste is approximately \$.30 per pound.
- The canister filled with gelled fluid must be disposed; it cannot be cleaned and re-sterilized for future use.

Despite the increased cost of using gel and the marginal improvement in health care worker protection it provides, several hospitals have adopted gel as their standard procedure.

### ***Drainage Systems***

Several new medical devices have been developed which address some of the deficiencies described above. MD Technologies, Inc., DeRoyal (formerly Waterstone), Cardinal Health, Inc., Domoch Medical Systems, Inc. (now Zimmer) and Stryker Instruments have all developed systems that provide disposal into the sanitary sewer without pouring the infectious fluids directly through a hopper disposal or using expensive gel powders. All of these newer products are currently sold with 510(k) exempt concurrence from the FDA. Most of these competing products incorporate an internal collection canister with finite capacity, and while not directly eliminating the need to transport a device to and from the surgical room, we believe most have been successful in eliminating the need for expensive gel and its associated handling and disposal costs.

Existing competitors, that already have products on the market, have a competitive advantage in terms of brand recognition and market exposure. In addition, the aforementioned companies have extensive marketing and development budgets that could overpower an early stage company like ours.

We believe that Stryker Instruments has the dominant market share position. Cardinal Health, Inc., though having FDA concurrence has only recently started advertising its product. We also believe competing products are used in select procedures and often in some, but not all, surgical procedures.

### ***Current Competition, Technology, and Costs***

#### ***Single Use Canisters***

In the U.S., glass reusable containers are infrequently used as their high initial cost, frequent breakage and costs of reprocessing are typically more costly than single use high impact plastic canisters, even when disposal is factored in. Each single use glass canister costs roughly \$8.00 each while the high impact plastic canisters cost \$2.00 – \$3.00 each and it is estimated that a range of two to eight canisters are used in each procedure, depending on the operation.

Our FMS would replace the use of canisters and render them unnecessary, as storage and disposal would be performed automatically by the FMS. It should be noted that these canisters are manufactured by companies with substantially more resources than our Company. Cardinal Health, a very significant competitor, manufactures both single use canisters as well as a more automated fluid handling system that will compete with us. Accordingly, faced with this significant competition, we may have difficulty penetrating this market. Our true competitive advantage, however, is our unlimited capacity, eliminating the need for any high volume cases to be interrupted for canister changeover.

#### ***Solidifying Gel Powder***

The market potential for solidifying gel was estimated by industry publications at over \$100 million in 2002. This market is not yet fully realized, but many hospitals, responding to increased concerns over inadvertent worker exposure to liquid waste, are converting to this technology. There have been many reports (Allina and Fairview to name two Minneapolis-based health systems) of nursing contracts containing language that requires the facilities to use gels after every procedure. We are aware that at a large healthcare facility in



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Minneapolis, Minnesota, routine usage of gel increased annual operating room expenditures by \$63,000, based on 14,000 procedures done in 2006. It is clear that solidifying gels, while not providing complete freedom from exposure to workers does present a level of safety and peace of mind to the healthcare workers who handle gel-treated canisters. While several gel manufacturers proclaim that sterility of the contents is achieved with the use of their product, protocols continue to recommend that the red-bag procedure is followed when using these products. One significant drawback of the solidifying gels is that they increase the weight of the materials being sent to the landfill by a factor of five to seven times, resulting in a significant cost increase to the hospitals that elect to use the products.

The FMS eliminates the need for solidifying gel, providing savings in both gel powder usage and associated landfill costs.

### *Sterilization and Landfill Disposal*

Current disposal methods include the removal of the contaminated canisters (with or without the solidifying gel) to designated biohazardous/infectious waste sites. Previously many hospitals used incineration as the primary means of disposal, but environmental concerns at the international, domestic and local level have resulted in a systematic decrease in incineration worldwide as a viable method for disposing of blood, organs or materials saturated with bodily fluids. When landfill disposal is used, canisters are included in the general red-bag disposal and, when gel is used, comprise a significant weight factor. Where hopper disposal is still in use, most of the contents of the red-bag consist only of outer packaging of supplies used in surgery and small amounts of absorbent materials impregnated with blood and other waste fluid. These, incidentally, are retained and measured at the end of the procedure to provide a more accurate assessment of fluid loss or retention. Once at the landfill site, the red-bagged material is often steam-sterilized with the remaining waste being ground up and interred into a specially segregated waste dumpsite.

In a related note, many countries are struggling with landfills within their own borders, and a thriving and growing biohazardous/infectious waste disposal business is emerging. The inevitable disputes connected with such a highly charged and potentially politically sensitive topic have developed, particularly in Europe and the former Soviet Republics, over the disposition and disposal of these infectious wastes. Such disputes have also arisen in the U.S. as states lacking landfill capacity (New Jersey, for example) seek to offload their medical waste on less populous states or those which lack stringent enforcement.

### *Handling Costs*

Once the surgical team has finished the procedures, and a blood loss estimate is calculated, the liquid waste (with or without solidifying gels) is removed from the operating room and either disposed of down the sanitary sewer or transported to an infectious waste area of the hospital for later removal.

The FMS would significantly reduce the labor costs associated with the disposal of fluid or handling of contaminated canisters, as the liquid waste is automatically emptied into the sanitary sewer after measurements are obtained. We will utilize the same suction tubing currently being used in the operating room, so no additional cost is incurred with our process. While each hospital handles fluid disposal differently, we believe that the cost of our cleaning fluid after each procedure will be less than the current procedural cost that could include the cost of canisters, labor to transport the canisters, solidifying powder, gloves, gowns, mops, goggles, shipping, and transportation, as well as any costs associated with spills that may occur due to manual handling.

A hidden but very real and considerable handling cost is the cost of an infectious fluid exposure. A July 2007 research article published in *Infection Control Hospital Epidemiology* concluded that "Management of occupational exposures to blood and bodily fluids is costly; the best way to avoid these costs is by prevention of exposures." According to the article, hospital management cost associated with occupational blood exposure can, conservatively, be more than \$4,500 per exposure. Because of privacy laws, it is difficult to obtain estimates of exposure events at individual facilities; however, in each exposure the worker must be treated as a worse case event. This puts the healthcare worker through a tremendous amount of personal trauma, and the health care facility through considerable expense and exposure to liability and litigation.

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### *Nursing Labor*

Nursing personnel spend significant time in the operating room readying canisters for use, calculating blood loss and removing or supervising the removal of the contaminated canisters after each procedure. Various estimates have been made, but an internal study at a large healthcare facility in Minneapolis, Minnesota, revealed that the average nursing team spends twenty minutes pre-operatively and intra-operatively setting up, monitoring fluid levels and changing canisters as needed and twenty minutes post-operatively readying blood loss estimates or disposing of canisters. Estimates for the other new technologies reviewed have noted few cost savings to nursing labor.

The FMS would save nursing time as compared to the manual process of collecting and disposing of surgical waste. Set-up is as easy as attaching the suction tube to the inflow port of the FMS. Post-operative clean-up requires approximately five minutes, the time required to dispose of the suction tubing and disposable filter to the red-bag, calculate the patient's blood loss, attach the bottle of cleaning solution to the inlet port of the unit, initiate the cleaning cycle, and dispose of the emptied cleaning solution. The steps that our product avoids, which are typically involved with the manual disposal process include, canister setup, interpretation of an analog read out for calculating fluid, canister management during the case (i.e. swapping out full canisters), and then temporarily storing, transferring, dumping, and properly disposing of the canisters.

### *Competitive Products*

Disposable canister system technology for fluid management within the operating room has gone virtually unchanged for decades. As concern for the risk of exposure of healthcare workers to bloodborne pathogens, and the costs associated with canister systems has increased, market attention has increasingly turned toward fluid management. The first quarter of 2001 saw the introduction of three new product entries within the infectious material control field. Stryker Instruments introduced the "Neptune™" system, offering a combination of bio-aerosol and fluid management in a portable two-piece system; Waterstone Medical (now DeRoyal) introduced the "Aqua Box™" stationary system for fluid disposal; Cardinal Health introduced the Orwell Fluid Collection and Disposal System; and Domoch Medical Systems, Inc. (Zimmer) introduced the "Red Away™" stationary system for fluid collection and disposal. All companies, regardless of size, have their own accessory kits.

We differentiate from these competitors since we are completely direct-to-drain and have the most automatic, hands-free process of any of the systems currently on the market. Each of our competitors, with the exception of MD Technologies, Inc., has some significant manual handling involved in the process. For instance, some competing products require transport of the mobile unit to a docking port and then emptying of the fluid, while others require that the canister be manually transported to a more efficient dumping station. Regardless, most of our competitors require more human interaction with the fluid than Skyline. Please refer to the chart included in the section headed as Products for a comparison of the key features of the devices currently marketed and the FMS.

Although the mobility associated with most of the competing products adds time and labor to the process and increases the chance of worker exposure to waste fluids, it also allows the hospital to purchase only as many mobile units needed for simultaneous procedures in multiple operating rooms. With the FMS, a unit must be purchased and installed in each room where it is intended to be used.

### **Marketing and Sales Distribution**

We sell the FMS and procedure disposables through various methods that may include a direct sales force, independent distributors and manufacturer's representatives covering the vast majority of major U.S. and outside U.S. markets. Currently we have six regional managers selling, and demoing the FMS for prospective customers and distributors, as well as, supporting our current customer base for disposable resupply. We are close to signing contracts with various hospital purchasing groups and have signed on an independent distributor. Our targeted customer base includes nursing administration, operating room managers, CFOs, CEOs, risk management, and infection control. Other professionals with an interest in the product include physicians, nurses, biomedical engineering, anesthesiologists, imaging, anesthesiologists, human resources, legal, administration and housekeeping.

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The major focus of our marketing efforts will be to introduce the FMS as a standalone device capable of effectively removing infectious waste and disposing of it automatically while providing accurate measurement of fluids removed, and also limiting exposure of the surgical team and healthcare support staff.

Governmental and professional organizations have become increasingly aggressive in attempting to minimize the risk of exposure by medical personnel to bloodborne pathogens. We believe that the FMS provides a convenient and cost effective way to collect and dispose of this highly contaminated material.

Our distributors may have installation and service capability, or we will contract those functions with an independent service/maintenance company. We have been in contact with both distributors and service companies regarding these installation requirements. We will establish extensive training and standards for the service and installation of the FMS to ensure consistency and dependability in the field. Users of the system will require a minimal amount of training to operate the FMS. The instructions for use and the installation guide will be included with every system along with a quick start guide, a troubleshooting manual and an on-board PLC controlling an intuitive touch screen with step by step instruction and safety features.

We have structured our pricing and relationships with distributors and/or service companies to ensure that these entities receive at least a typical industry level compensation for their activities. We believe our current cost and price estimates are conservative and allow for reasonable profit margins for all entities in the FMS and the cleaning fluid and filter supply chain.

### ***Promotion***

The dangers of exposure to infectious fluid waste are well recognized in the medical community. It is our promotional strategy to effectively educate medical staff regarding the risks of contamination using current waste collection procedures and the advantages of the FMS in protecting medical personnel from inadvertent exposure. We intend to leverage this medical awareness and concern with education of regulatory agencies at the local, state and federal levels about the advantages of the FMS.

We supplement our sales efforts with a promotional mix that will include a number of printed materials, video support and a website. We believe our greatest challenge lies in reaching and educating the 1.6 million medical personnel who are exposed daily to fluid waste in the operating room or in other healthcare settings (OSHA, CPL 2-2.44C). These efforts will require utilizing single page selling pieces, video educational pieces for technical education, use of scientific journal articles and a webpage featuring product information, educational materials, and training sites.

We support our sales organization by attending major scientific meetings where large numbers of potential users are in attendance. The theme of our trade show booths will focus on education, the awareness of the hazards of infectious waste fluids and the Company's innovative solution to the problem. We will focus our efforts initially on the Association of Operating Room Nurses ("AORN") meeting, where the largest concentration of potential buyers and influencers are in attendance and the Radiological Society of North America Scientific Assembly and Annual Meeting. We feature information on protection of the healthcare worker on our website as well as links to other relevant sites. We have invested in limited journal advertising for targeted audiences that have been fully identified. The initial thrust focuses on features of the product and ways of contacting the Company via the webpage or directly through postage paid cards or direct contact. Additionally, we will create a press release distribution to clinician-oriented periodicals for inclusion in their new product development columns. These periodicals will provide the reader with an overview of the FMS and will direct readers to pursue more information by direct contact with us by accessing our webpage.

### ***Pricing***

We believe prices for the FMS and its disposable procedure kit reflect a substantial cost savings to hospitals compared to their long-term procedure costs. Our pricing strategy ensures that the customer realizes actual cost savings when using the FMS versus replacing traditional canisters, considering the actual costs of the canisters and associated costs such as biohazard processing labor and added costs of biohazard waste disposal. Suction tubing that is currently used in the operating room will continue to be used with our system and should not be considered in the return on investment equation. Our cleaning solution's bottle is completely recyclable, and the anticipated selling price of the fluid is built into our cost analysis. In contrast, an operation using traditional disposal methods will often produce multiple canisters destined for biohazard

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processing. Biohazard disposal costs are estimated by *Outpatient Surgery Magazine* to be 5 times more per pound to dispose of than regular waste (*Outpatient Surgery Magazine*, April 2007). Once the canister has touched blood, it is considered “red bag” biohazard waste, whereas the cleaning fluid bottle used in our system can be recycled or disposed with the rest of the facility’s plastics.

The FMS lists for \$21,900 per system (one per operating room — installation extra) and \$24 per unit retail for the proprietary disposables: one filter and one bottle of cleaning solution to the U.S. hospital market. By comparison, the disposal system of Stryker Instruments, one of our competitors, retails for approximately \$25,000 plus an \$8,000 docking station and requires a disposable component with an approximate cost of \$25 per procedure and a proprietary cleaning fluid (cost unknown per procedure). Per procedure cost of the traditional disposal process includes approximate costs of \$2 – \$3.00 per liter canister, plus solidifier at \$2 per liter canister, plus the biohazard premium disposal cost approximated at \$1.80 per liter canister. In addition, the labor, gloves, gowns, goggles, and other related material handling costs are also disposal expenses.

Installation will be done by distributors, independent contractors, or in-house engineering at an estimated price of \$300 – \$1,000, depending on the operating room. Installation of the FMS requires access only to the hospital’s sanitary sewer, vacuum suction, and electricity. To help facilities maintain their utilization rates, we will recommend installation during off peak hours. In smaller facilities, an outside contractor may be called in, while larger institutions have their own installation and maintenance workforce. Installation time should not seriously impact the use of the operating room. Each FMS will have an industry standard warranty period that can be extended through documented use of our disposables: one filter and one bottle of cleaning solution per procedure.

### **Engineering and Manufacturing**

We are currently manufacturing the FMS in our own facility. We have the capability to manufacture, test, house, ship and receive from our warehouse. We contracted a manufacturing company, Wair Products in Bloomington, Minnesota that meets our standards and requirements that can produce six times the amount of FMS systems produced in-house at our facility on a monthly basis as sales increase.

The disposables, including a bottle of proprietary cleaning solution and an in-line filter is sourced through Diversified Manufacturing Corporation (cleaning solution) situated in Newport, Minnesota and MPP Corporation (filters), located in Osceola, Wisconsin that has tooled to manufacture our own newly designed disposable filter. Both these companies have the potential for long term vendor agreements with the Company. We are pursuing Intellectual Property protection for these disposable products as well.

### **Government Regulation**

To date, no regulatory agency has established exclusive jurisdiction over the area of biohazardous and infectious waste in healthcare facilities. Several prominent organizations maintain oversight function concerning various aspects of pertinent technologies and methods of protection.

These agencies include:

- OSHA (Occupational Safety and Health Administration)
- EPA (Environmental Protection Agency)
- DOT (Department of Transportation)
- JCAHO (Joint Commission of Accreditation of Hospitals)
- NFPA (National Fire Protection Association)
- AIA (American Institute of Architects)
- AORN (Association of Operating Room Nurses)

### ***Application for Electrical Safety Testing and Certification***

We sought and achieved testing and certification to the IEC 60606-1 and IEC 60606-1-2, two internationally recognized standards.

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The 6060101 & 60601-2 2<sup>nd</sup> edition certification for our STREAMWAY System is valid and enables us to continue to market and sell our product domestically.

A new standard; IEC 60601-1 3<sup>rd</sup> Edition Medical Device Safety Testing was adopted by the International Organization of Standards in 2005 and had a compliance date of June 2012 for OUS and Dec 31, 2013 for the U.S. This standard, which is now recognized by the US FDA, includes a provision of risk management which the 2<sup>nd</sup> edition did not require. The purpose of these rules is to ensure that equipment manufacturers have safety, performance, and risk management control measures in place.

The EU & Canada required 60601-1 3<sup>rd</sup> Edition compliance for all product sold or currently on the market after June 2013. Any product that had previously been certified to the 60601-1 2<sup>nd</sup> generation standard was no longer allowed for use as the old standard was no longer recognized. This did not affect Skyline Medical as the company did not sell internationally.

The U.S. FDA compliance date to meet the new standard was Dec 31, 2013. The major difference between the U.S. and the EU & Canadian market transition to the new standard is that the U.S. allows the 60601-1 2<sup>nd</sup> edition testing to be grandfathered in, allowing previously certified product to remain on the market. Any new product that will be tested after December 31, 2013 should be certified to the new 60601-1 3<sup>rd</sup> generation standard.

### ***FDA Clearance under Section 510(k)***

The FDA Center for Devices and Radiological Health requires 510(k) submitters to provide information that compares its new device to a marketed device of a similar type, in order to determine whether the device is substantially equivalent (“SE”).

This means that a manufacturer can submit a 510(k) comparing a new device to a device that has been found to be SE and the FDA can use this as evidence to determine whether the new device is SE to an already legally marketed device (or a “predicate device”). The ultimate burden of demonstrating the substantial equivalence of a new device to a predicate device remains with the 510(k) submitter, and in those occasions when the Center for Devices and Radiological Health is unfamiliar with certain aspects of the predicate device, the submitter will be required to provide information that substantiates a claim of substantial equivalence.

As a matter of practice, the Center for Devices and Radiological Health generally considers a device to be SE to a predicate device if, in comparison to the predicate device, (i) the new device has the same intended use, (ii) the new device has the same technological characteristics (i.e., same materials design, energy source), (iii) the new device has new technological characteristics that could not affect safety or effectiveness, or (iv) the new device has new technological characteristics that could affect safety or effectiveness, but there are accepted scientific methods for evaluating whether safety or effectiveness has been adversely affected and there is data to demonstrate that the new technological features have not diminished safety or effectiveness. Pre-market notification submissions are designed to facilitate these determinations.

The FDA requires, pursuant to a final regulation for Establishment Registration and Device Listing for Manufacturers of Devices, that a 510(k) premarket notification be submitted at least ninety days before marketing a device that: (1) is being introduced into distribution for the first time by that person or entity, or (2) is in distribution but is being significantly modified in design or use. A 510(k) submission must contain, among other things: (i) proposed labeling sufficient to describe the device’s intended use; (ii) a description of how the device is similar to or different from other devices of comparable type, or information about what consequences a proposed device modification may have on the device's safety and effectiveness; and (iii) any other information necessary to determine whether the device is substantially equivalent. The FMS is a Class II device, which is less stringently reviewed as that of a Class III device. Our COO has numerous years’ significant experience in the FDA clearance process and has a team of regulatory consultants with significant experience in the FDA clearance process.

We filed the 510(k) submission for clearance of the FMS device on March 14, 2009 and received written confirmation on April 1, 2009 that our 510(k) has been cleared by the FDA.

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Following this 510(k) clearance by the FDA, we continue to be subject to the normal ongoing audits and reviews by the FDA and other governing agencies. These audits and reviews are standard and typical in the medical device industry, and we do not anticipate being affected by any extraordinary guidelines or regulations.

### **Employees**

We have 16 employees, thirteen of whom are full-time, and three who are part-time.

### **Property**

Our corporate offices are located at 2915 Commers Drive, Suite 900, Eagan, Minnesota 55121. On January 28, 2013, the Company signed an amendment to the month to month lease originally signed on April 30, 2012. The lease as amended has a five-year term effective February 1, 2013 ending January 31, 2018. We lease 5,773 square feet at this location, of which 2,945 square feet is used for office space and 2,828 is used for manufacturing. Our lease is effective through January 31, 2018. We expect that this space will be adequate for our current office and manufacturing needs.

### **Legal Proceedings**

On July 17, 2014, the Company and a stockholder entered into a settlement agreement and release (the "Settlement Agreement") with Marshall Ryan ("Ryan") and a company related to Ryan (together, the "Plaintiffs"). The settlement relates to a lawsuit by the Plaintiffs initiated in March 2014. Ryan is an engineer who previously worked with the Company on design of certain of the Company's products. The lawsuit alleged among other things, breach of a 2008 consulting agreement, a 2006 manufacturing agreement and a 2006 supply agreement among the Plaintiffs and the Company, various claims of fraud and negligent misrepresentation, and breach of the duty of good faith and fair dealing.

Under the Settlement Agreement, the parties have agreed that the lawsuit will be dismissed. The Company has agreed to pay Ryan an aggregate of \$500,000 in various cash installments through April 25, 2015, which amount includes \$200,000 in installments that are payable during the remainder of 2014. The Settlement Agreement, among other things, extinguishes any prior claims of Plaintiffs for royalties or other alleged rights to payments under their prior agreements with the Company. Payment of the outstanding balance under the Settlement Agreement will be accelerated if the Company raises \$2 million or more of gross dollars in a single funding round or raises aggregate funding of \$4 million of gross dollars on or before April 10, 2015. If the Company defaults on the required cash payments and fails to cure as provided in the Settlement Agreement, then Ryan will have the option to either sue Skyline to enforce the Settlement Agreement or rescind the Settlement Agreement, including returning all payments previously made thereunder.

The Settlement Agreement also contains mutual releases covering claims other than a breach of the Settlement Agreement. In the Settlement Agreement, Ryan fully, unconditionally and irrevocably affirms and ratifies the Company's rights to Ryan's prior patent assignments, and disclaims any right, title or interest in the Company's Streamway product including any claims to royalties both past and future. In addition, the parties confirmed that the patents related to the Streamway product belong exclusively to Skyline and remain in full force and effect.

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**MANAGEMENT**

Our directors and executive officers, their ages, their respective offices and positions, and their respective dates of election or appointment are as follows:

<u>Name</u>	<u>Age</u>	<u>Position</u>	<u>Date of Election or Appointment</u>
Josh Kornberg	40	President, Chief Executive Officer, and Interim Chairman of the Board	July 1, 2012
Ricardo Koenigsberger	47	Director	June 25, 2012
Thomas J. McGoldrick	72	Director	2005
Andrew P. Reding	44	Director	2006
David O. Johnson	61	Chief Operating Officer	July 1, 2012
Bob Myers	59	Chief Financial Officer	July 1, 2012
Dr. Arnon Dreyfuss	60	Director	August 1, 2013
Frank Mancuso Jr.	54	Director	August 1, 2013

**Business Experience Descriptions**

Set forth below is a summary of our executive officers' and directors' business experience for the past 5 years. Other than as described below, the experience and background of each of the directors, as summarized below, were significant factors in their previously being nominated as directors of the Company.

**Josh Kornberg, President, Chief Executive Officer and Interim Chairman of the Board.** Effective July 22, 2012, Josh Kornberg was appointed as the Chief Executive Officer and President of the Company. Mr. Kornberg was appointed Interim Chairman of the Board on August 21, 2013. Mr. Kornberg was elected Interim President and Chief Executive Officer by the Board on April 23, 2012. Mr. Kornberg was elected to the Board on March 9, 2012. Mr. Kornberg is President and founding partner of Atlantic Partners Alliance (APA), a private equity fund based in New York. APA and its affiliates are controlling stockholders of the Company. Prior to founding APA, Mr. Kornberg served as Chief Investment Officer of The Lightstone Group, a national private equity firm and Director of the Lightstone Value Plus REIT, a public company focused on commercial real estate. Mr. Kornberg worked in the capital markets group at Morgan Stanley, and also served as Vice President at The RREEF Funds, one of the leading global pension fund advisors. In December 2013 Mr. Kornberg was appointed to the Board of Directors of Prospect Park Capital Corporation a business development company currently trading on the Canadian TSX exchange.

**Ricardo Koenigsberger.** Effective June 25, 2012, Ricardo Koenigsberger, was elected to the Board of Directors of Skyline Medical Inc. (the "Company"). Mr. Koenigsberger is currently co-CEO of CV Holdings, Inc. a publically held REIT. In addition he is a managing partner of ROCA Management, a private investment fund focused on the REIT industry. Previously, Mr. Koenigsberger was a partner of Apollo Real Estate, a large private equity firm, where he was responsible for new investments and investment management. At Apollo, he oversaw the investment of over \$1+ billion in equity. Mr. Koenigsberger graduated summa cum laude from the Wharton School of the University of Pennsylvania.

**Thomas J. McGoldrick.** Mr. McGoldrick has served as a director of the Company since 2005. Prior to that, he served as Chief Executive Officer of Monteris Medical Inc. from November 2002 to November 2005. He has been in the medical device industry for over 30 years and was co-founder and Chief Executive Officer of Fastitch Surgical in 2000. Fastitch is a start-up medical device company with unique technology in surgical wound closure. Prior to Fastitch, Mr. McGoldrick was President and Chief Executive Officer of Minntech from 1997 to 2000. Minntech was a \$75 million per year publicly traded (Nasdaq-MNTX) medical device company offering services for the dialysis, filtration, and separation markets. Prior to employment at Minntech from 1970 to 1997, he held senior marketing, business development and international positions at Medtronic, Cardiac Pacemakers, Inc. and Johnson & Johnson. Mr. McGoldrick is on the board of directors of two other start-up medical device companies.

**Andrew P. Reding.** Mr. Reding is an executive with extensive experience in sales and marketing of capital equipment for the acute care markets. He has served as a director of the Company since 2006 and he is currently the President and Chief Executive Officer of TRUMPF Medical Systems, Inc., a position he has

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held since April 2007. Prior to that, he was Director of Sales at Smith & Nephew Endoscopy and prior to that, he served as Vice President of Sales and Director of Marketing with Berchtold Corporation from 1994 to 2006. His experience is in the marketing and sales of architecturally significant products for the operating room, emergency department and the intensive care unit. Mr. Reding has successfully developed high quality indirect and direct sales channels, implemented programs to interface with facility planners and architects and developed GPO and IDN portfolios. Mr. Reding holds a bachelor's degree from Marquette University and an MBA from The University of South Carolina.

**David O. Johnson, Chief Operating Officer.** Mr. Johnson has been Chief Operating Officer since July 2012. He was previously the Acting Chief Operating Officer since December 2011 and had been a consultant to medical device companies since October 2010. Mr. Johnson has over 30 years' experience in executive, operations and management positions in rapid growth medical device organizations, directing growth domestically and internationally with products ranging from consumer based disposable commodity items to Class III implantable devices. His experience includes executive management, training, product development, business development, regulatory and quality assurance, operations, supplier development and technology acquisitions. From August 2007 to September 2010 Mr. Johnson was President and CEO of Spring Forest Qigong, an alternative healthcare organization. Prior to August 2007 he had been a co-founder and Vice President of Operations at Epitek, Inc. since January 2005, and prior to that time he was a co-founder and President of Timm Medical Technologies. He also held positions including Vice President — Operations/Technology at UroHealth/Imagyn, Vice-President Operations at Dacomed Corporation and various technical, operations and training positions at American Medical Systems and Pfizer Corporation. He also holds a number of patents in the medical device field and the exercise fitness industry.

**Bob Myers, Chief Financial Officer.** Effective July 1, 2012 Bob Myers was appointed as the Chief Financial Officer of the Company. Mr. Myers was the Acting Chief Financial Officer and Corporate Secretary for the Company since December 2011. He has over 30 years' experience in multiple industries focusing on medical device, service and manufacturing and for the past ten years has been a financial contractor represented by various contracting firms in the Minneapolis area. He has spent much of his career as a Chief Financial Officer and/or Controller. Mr. Myers was a contract CFO at Disetronic Medical, contract Corporate Controller for Diametric Medical Devices and contract CFO for Cannon Equipment. Previously he held executive positions with American Express, Capitol Distributors, and International Creative Management and was a public accountant with the international firm of Laventhol & Horwath. Mr. Myers has an MBA in Finance from Adelphi University and a BBA in Public Accounting from Hofstra University.

**Dr. Arnon Dreyfuss.** Dr. Dreyfuss, age 60, has decades of experience in healthcare and entrepreneurship. As an oncologist, he spent his career at Harvard Medical School's Beth Israel Hospital and the Dana Farber Cancer Institute caring for patients while conducting and leading clinical trials. His scientific work appeared in major medical journals as well as in books and medical conferences. From 1987 to 1998, Dr. Dreyfuss also served as the founder, publisher, editor and Chief Executive Officer of Dreyfuss Hunt, Inc. (formerly The Health Source Corporation), a health and financial information provider and an "Inc. 500" company. He also co-founded epodia.com, a teaching material network, now owned and operated by the University of Pennsylvania. During the past decade, Dr. Dreyfuss has been consulting, advising and investing in start-up companies, particularly in the healthcare space. Dr. Dreyfuss obtained his undergraduate degree from the Sackler School of Medicine at Tel Aviv University and his Doctorate in Medicine from Hadassah Medical School at the Hebrew University in Jerusalem. He completed his residency training in Internal Medicine in 1984 at Tufts-New England Medical Center in Boston, which included a three-month rotation at the Clinical Research Institute in Nairobi, Kenya. In 1987 he completed a three-year combined Hematology and Oncology Fellowship at Harvard Medical School. In 1986, Dr. Dreyfuss received a Postdoctoral Fellowship Award from the American Cancer Society. He has been a member of the American Medical Association since 1987 and the American Society of Clinical Oncology since 1989.

**Frank Mancuso, Jr.** Mr. Mancuso, age 54, is a veteran of the film production industry with more than 30 years of industry experience. He is currently the President of Boss Media, LLC, which he co-founded in 2010. Prior to joining Boss Media, Mr. Mancuso was the President of 360 Pictures, LLC and FGM Entertainment Inc. Mr. Mancuso also has an extensive background in healthcare and has served on the boards of multiple public companies. Mr. Mancuso has been a director of Prospect Park Capital Corp.



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(TSX VENTURE: PPK.P), a company whose strategy is to invest in early to mid-stage healthcare companies. Previously, he was a director at Delcath Systems, Inc. (NASDAQ: DCTH), a healthcare device company dedicated to the infusion of high dose chemotherapy to targeted areas of the body for the treatment of cancer. Mr. Mancuso obtained a Bachelor of Arts degree in business and graduated with honors from Upsala College in 1980.

### **Family Relationships**

There are no family relationships among our directors and executive officers.

### **Audit Committee of the Board; Audit Committee Financial Expert**

The Audit Committee was established by the Board in accordance with Section 3(a)(58)(A) of the Exchange Act to oversee our corporate accounting and financial reporting processes and audits of our financial statements.

The functions of the Audit Committee include, among other things:

- serving as an independent and objective party to monitor our financial reporting process and internal control system;
- coordinating, reviewing and appraising the audit efforts of our independent auditors and management and, to the extent we have an internal auditing or similar department or persons performing the functions of such department (“internal auditing department” or “internal auditors”), the internal auditing department; and
- communicating directly with the independent auditors, financial and senior management, the internal auditing department, and the Board of Directors regarding the matters related to the committee’s responsibilities and duties.

Both our independent registered public accounting firm and management periodically meet privately with the Audit Committee.

Our Audit Committee currently consists of Mr. Koenigsberger as the chairperson, Mr. McGoldrick and Mr. Reding. The Board of Directors has appointed Ricardo Koenigsberger to the audit committee. Mr. Koenigsberger has a strong and vast financial history specializing in investment banking and management. Mr. Koenigsberger graduated from the Wharton School of Business of the University of Pennsylvania summa cum laude; he qualifies as a financial expert and meets independence within the meaning of NASDAQ’s listing standards. Each Audit Committee member is a non-employee director of our Board. The Board of Directors reviews the NASDAQ listing standards definition of independence for Audit Committee members on an annual basis and has determined that all current members of our Audit Committee are independent (as independence is currently defined in Rule 5605(a)(2) of the Nasdaq listing standards). The Audit Committee met four times in fiscal 2013.

### **Director Independence**

Although we are not required to comply with the NASDAQ Stock Market listing standards, we use these listing standards as our guide toward determining independence of our directors and other areas of corporate governance. Under NASDAQ listing standards, a majority of the members of a listed company’s board of directors must qualify as “independent,” as affirmatively determined by the board of directors. The Board of Directors consults with our counsel to ensure that the Board of Directors’ determinations are consistent with relevant securities and other laws and regulations regarding the definition of “independent,” including those set forth in pertinent listing standards of the NASDAQ, as in effect from time to time.

Consistent with these considerations, after review of all relevant transactions or relationships between each director, or any of his or her family members, and the Company, its senior management, and its independent registered public accounting firm, the Board of Directors has affirmatively determined that the following directors and nominees are independent directors within the meaning of the NASDAQ listing standards: Messrs. McGoldrick, Reding, Koenigsberger, Mancuso and Dr. Dreyfuss. In making this determination, the Board of Directors found that none of these directors and nominees had a material or other

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disqualifying relationship with the Company. Mr. Kornberg, our President and Chief Executive Officer, is not independent by virtue of his managing partnership position with SOK Partners. Mr. Koenigsberger is a shareholder of SOK Partners, LLC.

### **Compensation Committee Interlocks and Insider Participation**

The Compensation Committee of the Board of Directors currently consists of two directors, Dr. Dreyfuss, as the chairperson, and Mr. Mancuso. All members of the Compensation Committee were appointed by the Board of Directors, and consist entirely of directors who are “outside directors” for purposes of Section 162(m) of the Internal Revenue Code of 1986, as amended (the “Code”), “non-employee directors” for purposes of Rule 16b-3 under the Exchange Act and “independent” as independence is currently defined in Rule 4200(a) (15) of the NASDAQ listing standards. In fiscal 2013, the Compensation Committee met two times. The functions of the Compensation Committee include, among other things:

- approving the annual compensation packages, including base salaries, incentive compensation, deferred compensation and stock-based compensation, for our executive officers;
- administering our stock incentive plans, and subject to board approval in the case of executive officers, approving grants of stock, stock options and other equity awards under such plans;
- approving the terms of employment agreements for our executive officers;
- developing, recommending, reviewing and administering compensation plans for members of the Board of Directors;
- reviewing and discussing the compensation discussion and analysis with management; and
- preparing any compensation committee report required to be included in the annual proxy statement.

All Compensation Committee approvals regarding compensation to be paid or awarded to our executive officers are rendered with the full power of the Board, though not necessarily reviewed by the full Board.

Our Chief Executive Officer may not be present during any Board or Compensation Committee voting or deliberations with respect to his compensation. Our Chief Executive Officer may, however, be present during any other voting or deliberations regarding compensation of our other executive officers, but may not vote on such items of business.

As indicated above, the Compensation Committee consists of Dr. Dreyfuss and Mr. Mancuso. No member of the Compensation Committee has ever been an executive officer or employee of ours. None of our officers currently serves, or has served during the last completed year, on the compensation committee or the board of directors of any other entity that has one or more officers serving as a member of the Board of Directors or the Compensation Committee.

### **Governance/Nominating Committee**

The Governance/Nominating Committee of the Board of Directors currently consists of Mr. McGoldrick, as the chairperson, and Mr. Koenigsberger, each of whom is an “independent director,” as such term is defined by The NASDAQ Market Listing Rule 5605(a)(2), and free from any relationship that, in the opinion of the Board, would interfere with the exercise of his or her independent judgment as a member of the Committee.

The members of the Committee shall be elected annually by the Board. Committee members may be removed for any reason or no reason at the discretion of the Board, and the Board may fill any Committee vacancy that is created by such removal or otherwise. The Committee’s chairperson shall be designated by the full Board or, if it does not do so, the Committee members shall elect a chairperson upon the affirmative vote of a majority of the directors serving on the Committee.

The Committee may form and delegate authority to subcommittees as it may deem appropriate in its sole discretion.

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### **Structure and Meetings**

The chairperson of the Committee presides at each meeting and, in consultation with the other members of the Committee, sets the frequency and length of each meeting and the agenda of items to be addressed at each meeting. The chairperson of the Committee ensures that the agenda for each meeting is circulated to each Committee member in advance of the meeting. The Committee reports its actions and recommendations to the Board.

### **Goals and Responsibilities**

In furtherance of its purposes, the Committee:

- Evaluates the composition, organization and governance of the Board, determines future requirements and make recommendations to the Board for approval;
- Determines desired Board and committee skills and attributes and criteria for selecting new directors;
- Reviews candidates for Board membership consistent with the Committee's criteria for selecting new directors and annually recommend a slate of nominees to the Board for consideration at the Company's annual shareholders' meeting;
- Reviews candidates for Board membership, if any, recommended by the Company's shareholders;
- Conducts the appropriate and necessary inquiries into the backgrounds and qualifications of possible director candidates;
- Evaluates and considers matters relating to the qualifications and retirement of directors;
- Develops a plan for, and consults with the Board regarding, management succession; and
- Advises the Board generally on corporate governance matters.

In addition, the Committee, if and when deemed appropriate by the Board or the Committee, develop and recommend to the Board a set of corporate governance principles applicable to the Company, and review and reassess the adequacy of such guidelines annually and recommend to the Board any changes deemed appropriate. The Committee also advises the Board on (a) committee member qualifications, (b) appointments, removals and rotation of committee members, (c) committee structure and operations (including authority to delegate to subcommittees), and (d) committee reporting to the Board. Finally, the Committee performs any other activities consistent with this Charter, the Company's certificate of incorporation, bylaws and governing law as the Committee or the Board deems appropriate.

The Committee will review and reassess at least annually the adequacy of the Charter and recommend any proposed changes to the Board for approval.

### **Committee Resources**

The Committee has the authority to obtain advice and seek assistance from internal or external legal, accounting or other advisors. The Committee has the sole authority to retain and terminate any search firm to be used to identify director candidates, including sole authority to approve such search firm's fees and other retention terms.

### **Diversity**

The Board of Directors does not currently have a policy regarding attaining diversity on the Board.

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**EXECUTIVE COMPENSATION**

The following table provides information regarding the compensation earned during the fiscal years ended December 31, 2013 and December 31, 2012 by each of the named executive officers:

**Summary Compensation Table for Fiscal 2013 and 2012**

<u>Name and Principal Position</u>	<u>Year</u>	<u>Salary<sup>(5)</sup></u>	<u>Bonus</u>	<u>Stock Awards</u>	<u>Option Awards<sup>(1)</sup></u>	<u>All Other Compensation<sup>(6)</sup></u>	<u>Total Compensation</u>
Joshua Kornberg,	2013	\$ 238,691	\$ 50,000	\$ —	\$ 689,169	\$ 36,000	\$ 1,013,860
CEO, President <sup>(2)</sup>	2012	\$ 45,000	\$ —	\$ 45,000	\$ 345,044	\$ 112,162	\$ 547,206
David O. Johnson,	2013	\$ 161,466	\$ 50,000	\$ —	\$ 68,252	\$ 10,350	\$ 290,068
COO <sup>(3)</sup>	2012	\$ 35,625	\$ —	\$ —	\$ 57,507	\$ 65,725	\$ 158,857
Bob Myers,	2013	\$ 140,561	\$ 62,500	\$ —	\$ 56,877	\$ 1,133	\$ 261,071
CFO <sup>(4)</sup>	2012	\$ 30,933	\$ —	\$ —	\$ 57,507	\$ 15,000	\$ 103,440

- (1) Represents the actual compensation cost recognized during 2013 and 2012 as determined pursuant to FASB ASC 718 — Stock Compensation utilizing the assumptions discussed in Note 3, “Stock Options and Warrants,” in the notes to the Financial Statements included in this prospectus.
- (2) Mr. Kornberg became a consultant on March 13, 2012, interim CEO on April 4, 2012 and CEO on July 1, 2012. Mr. Kornberg’s bonus earned in 2013 was 75% of his base salary, \$187,500, and will be paid in 2014. Mr. Kornberg was also awarded 225% of his base salary in the form of options to purchase 2,445,652 shares of common stock at \$.23. Mr. Kornberg received a salary increase of \$25,000 in March 2014. In 2013 he also received options to purchase 34,242 shares of common stock as fees for serving on the Board of Directors. Mr. Kornberg received options to purchase 14,400,000 shares at \$.075 in 2013 as part of his 2012 bonus. Mr. Kornberg’s 2012 cash bonus was for \$360,000 payable in 2013; he was paid \$50,000 in 2013 and the Company has the remainder recorded as an accrued liability. Mr. Kornberg received options to purchase 6,000,000 shares at \$.08 following his appointment in 2012.
- (3) Mr. Johnson was a contract employee from December 2011 to June 30, 2012 and became COO on July 1, 2012. Mr. Johnson’s bonus awarded by the Board in 2013 was fifty percent in cash (\$72,000) payable in 2014 and fifty percent in the form of options to purchase 304,348 shares of common stock at \$.23 per share. The bonus awarded by the Board in 2012 was fifty percent in cash (\$75,000) payable in 2013 and fifty percent in the form of options to purchase 948,368 shares of common stock at \$.079. Mr. Johnson was paid \$50,000 in 2013 and the Company has the remainder recorded as an accrued liability. Following his 2012 appointment Mr. Johnson was granted options to purchase 1,000,000 shares of common stock at \$.08 per share.
- (4) Mr. Myers was a contract employee from December 2011 to June 30, 2012 and became CFO on July 1, 2012. Mr. Myers’s bonus awarded by the Board in 2013 was fifty percent in cash (\$60,000) payable in 2014 and fifty percent in the form of options to purchase 260,870 shares of common stock at \$.23 per share. The bonus awarded by the Board in 2012 was fifty percent in cash (\$62,500) payable in 2013 and fifty percent in the form of options to purchase 791,140 shares of common stock at \$.079. Mr. Myers was paid \$62,500 in 2013. Mr. Myers received a salary increase of \$15,000 in March 2014. Following his 2012 appointment Mr. Myers was granted options to purchase 1,000,000 shares of common stock at \$.08 per share.
- (5) Salaries shown, where applicable are net of the 401(k) retirement plan put in place during 2013.
- (6) All Other Compensation in 2013 consists of consulting income for Messrs. Johnson and Myers remaining due from 2012 and paid in 2013. Mr. Kornberg’s All Other Compensation consists of health insurance reimbursement for 2013.

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**Outstanding Equity Awards at Fiscal Year-end for Fiscal 2013**

The following table sets forth certain information regarding outstanding equity awards held by the named executive officers as of December 31, 2013:

	Grant Date	Option Awards			
		Number of Securities Underlying Options Exercisable	Number of Securities Underlying Options Unexercisable	Option Exercise Price	Option Expiration Date
Joshua Komberg <sup>(1)</sup>	8/13/2012	6,000,000		\$ 0.08	8/13/2022
	3/14/2013	14,400,000		\$ 0.075	3/14/2023
	9/30/13	15,723		\$ 0.318	9/30/2018
	12/31/2013	18,519		\$ 0.27	12/31/2018
	3/6/2014	2,445,652		\$ 0.23	3/6/2024
David O. Johnson	8/13/2012	1,000,000		\$ 0.08	8/13/2022
	3/18/2013	949,368		\$ 0.079	3/18/2023
	3/6/2014	303,348		\$ 0.23	3/6/2024
Bob Myers	8/13/2012	1,000,000		\$ 0.08	8/13/2022
	3/18/2013	791,140		\$ 0.079	3/18/2023
	3/6/2014	260,870		\$ 0.23	3/6/2024

(1) Does not reflect an award of 5,000,000 shares of restricted stock which the Compensation Committee has approved. Such shares would vest upon certain changes in control of the Company.

**Executive Compensation Components for Fiscal 2013**

*Base Salary.* Base salary is an important element of our executive compensation program as it provides executives with a fixed, regular, non-contingent earnings stream to support annual living and other expenses. As a component of total compensation, we generally set base salaries at levels believed to attract and retain an experienced management team that will successfully grow our business and create shareholder value. We also utilize base salaries to reward individual performance and contributions to our overall business objectives, but seek to do so in a manner that does not detract from the executives' incentive to realize additional compensation through our stock options and restricted stock awards.

The Compensation Committee reviews the Chief Executive Officer's salary at least annually. The Compensation Committee may recommend adjustments to the Chief Executive Officer's base salary based upon the Compensation Committee's review of his current base salary, incentive cash compensation and equity-based compensation, as well as his performance and comparative market data. The Compensation Committee also reviews other executives' salaries throughout the year, with input from the Chief Executive Officer. The Compensation Committee may recommend adjustments to other executives' base salary based upon the Chief Executive Officer's recommendation and the reviewed executives' responsibilities, experience and performance, as well as comparative market data.

In utilizing comparative data, the Compensation Committee seeks to recommend salaries for each executive at a level that is appropriate after giving consideration to experience for the relevant position and the executive's performance. The Compensation Committee reviews performance for both our Company (based upon achievement of strategic initiatives) and each individual executive. Based upon these factors, the Compensation Committee may recommend adjustments to base salaries to better align individual compensation with comparative market compensation, to provide merit-based increases based upon individual or company achievement, or to account for changes in roles and responsibilities.

*Stock Options and Other Equity Grants.* Consistent with our compensation philosophies related to performance-based compensation, long-term shareholder value creation and alignment of executive interests with those of shareholders, we make periodic grants of long-term compensation in the form of stock options or restricted stock to our executive officers, directors and others in the organization.

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Stock options provide executive officers with the opportunity to purchase common stock at a price fixed on the grant date regardless of future market price. A stock option becomes valuable only if the common stock price increases above the option exercise price and the holder of the option remains employed during the period required for the option shares to vest. This provides an incentive for an option holder to remain employed by us. In addition, stock options link a significant portion of an employee's compensation to shareholders' interests by providing an incentive to achieve corporate goals and increase shareholder value. Under the 2012 Plan, we may also make grants of restricted stock awards, restricted stock units, performance share awards, performance unit awards and stock appreciation rights to officers and other employees. We adopted the 2012 Plan to give us flexibility in the types of awards that we could grant to our executive officers and other employees.

*Limited Perquisites; Other Benefits.* We provide our employees with a full complement of employee benefits, including health and dental insurance, long term disability insurance, life insurance, a 401(k) plan, FSA flex plan and Section 125 plan. Mr. Kornberg receives \$3,000 monthly as a health insurance reimbursement in lieu of accepting the Company medical plan benefits.

### **Employment Contracts**

#### *Employment Agreement with Chief Executive Officer*

*Base Salary.* Our employment agreement, dated March 14, 2013, with Joshua Kornberg, President, Chief Executive Officer and Interim Chairman of the Board, provided that his initial annual base salary would be \$250,000 and that his base salary for subsequent years is to be determined by the Board. Effective in March 2014 Mr. Kornberg's annualized base salary was increased to \$275,000. We offered this amount as part of a package of compensation to ensure that we retain Mr. Kornberg in his current capacity with our Company. The compensation package for Mr. Kornberg was designed to provide annual cash compensation, combined with the equity compensation described below, sufficient to induce him to remain with the Company and continue to incentivize him to create revenue growth and shareholder value. Based upon the recommendation of the Compensation Committee, the Board approved an increase to Mr. Kornberg's base salary rate from \$180,000 to \$250,000 for calendar 2014.

*Compensation and Related Matters.* Notwithstanding the terms of the Existing Employment Agreement, in connection with the Mr. Kornberg's employment with the Company from April 24, 2012 to December 31, 2012, the Executive shall receive, or has received, the following incentive compensation payments in lieu of the payments described in Section 2(b) of the Existing Employment Agreement:

2012 Annual Bonus. Mr. Kornberg shall receive a cash bonus equal to Three Hundred Sixty Thousand Dollars (\$360,000), which is equal to two hundred percent (200%) of the Executive's annual Base Salary in 2012, payable in a lump sum no later than the Company's first regularly scheduled payroll date after the Effective Date. In March 2014 Mr. Kornberg was awarded a \$187,500 cash bonus equal to 75% of his base salary, and 225% of his base salary in the form of options to purchase 2,445,652 shares of common stock at \$.23.

Incentive Compensation. In connection with his employment during the Term, Mr. Kornberg shall be eligible to receive cash and/or equity incentive compensation as determined by the Board and/or the Compensation Committee from time to time, including, without limitation, the incentive compensation described below:

Annual Bonus. Mr. Kornberg shall be eligible to receive with respect to each calendar year ending during the Term of the Executive's employment with the Company a bonus payment subject to the terms of this Section (the "Annual Bonus"). The amount of the Annual Bonus shall be determined based on the attainment of reasonable Company and/or individual performance metrics established and revised annually by the Compensation Committee and/or Board in consultation with Mr. Kornberg, which shall be set at or about the beginning of the given year to which the metrics relate. Mr. Kornberg's target Annual Bonus shall be one hundred fifty percent (150%) of his Base Salary (the "Target Annual Bonus"); provided, however, that the actual amount of the Annual Bonus for each calendar year shall be determined by the Compensation Committee and/or the Board based on relative level of achievement of the applicable metrics and which may be in an amount greater or less than the Target Annual Bonus but shall not be less than fifty percent (50%) of the Target Annual Bonus (the "Minimum Bonus"). The Annual Bonus shall be payable in a single lump sum

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in cash between January 1 and March 15 of the year following the calendar year to which such Annual Bonus relates. Except as otherwise provided in this Agreement, to earn and be entitled to payment of an Annual Bonus in respect of a given calendar year, Mr. Kornberg must be employed by the Company on the last day (*i.e.*, December 31<sup>st</sup>) of the calendar year to which the bonus relates. Notwithstanding the foregoing, Mr. Kornberg (or his estate, if applicable) shall receive a pro-rata portion of the Target Annual Bonus (calculated as if all applicable performance metrics had been attained at one hundred percent (100%) and based on the portion of the calendar year during which the Executive was employed) (the “Pro-Rata Bonus”) for the calendar year during which the Executive’s employment terminates due to: (i) termination by the Company without Cause (as defined below); (ii) termination by the Executive for Good Reason (as defined below); or (iii) termination due to the Executive’s death or Disability (as defined below).

2012 Stock Option Award Grant. On March 14, 2013, the Company granted to Mr. Kornberg Fourteen Million Four Hundred Thousand (14,400,000) stock options, which is equal to (A) Three Hundred Sixty Thousand Dollars (\$360,000) (*i.e.*, two hundred percent (200%) of the Executive’s annual Base Salary in 2012); divided by (B) the price of a share of common stock of the Company on the day preceding the date of grant; multiplied by (C) three (3) (the “2012 Stock Option Award Grant”). The 2012 Stock Option Award Grant will be fully vested on the date of grant. If the shares covered by the 2012 Stock Option Award Grant exceed, as of the date of grant, the number of shares of common stock which may be issued under the Skyline Medical Inc. 2012 Stock Incentive Plan (the “Plan”) as last approved by the shareholders of the Company, then the 2012 Stock Option Award Grant shall be void with respect to such excess shares, unless shareholder approval of an amendment sufficiently increasing the number of shares of common stock issuable under the Plan is obtained in accordance with the provisions of the Plan on or before June 30, 2013.

2012 Restricted Stock Award Grant. On March 14, 2013, the Company granted to Mr. Kornberg Five Million (5,000,000) shares of common stock, subject to the restrictions contained in the applicable award agreement (the “2012 Restricted Stock Award Grant”). The 2012 Restricted Stock Award Grant will fully vest on a Change in Control (as defined below), as provided in the applicable award agreement. If the shares covered by the 2012 Restricted Stock Award Grant exceed, as of the date of grant, the number of shares of common stock which may be issued under the Plan as last approved by the shareholders of the Company, then the 2012 Restricted stock Award Grant shall be void with respect to such excess shares, unless shareholder approval of an amendment sufficiently increasing the number of shares of common stock issuable under the Plan is obtained in accordance with the provisions of the Plan on or before June 30, 2013.

Equity Incentive Grants. Mr. Kornberg shall receive annual equity incentive grants (*e.g.*, stock options, restricted stock or other stock-based awards) with respect to each calendar year ending during the Term of Mr. Kornberg’s employment with the Company, which shall be granted on December 31<sup>st</sup> of the calendar year to which such grant pertains (each an “Annual Grant”). Each Annual Grant shall be granted in accordance with the terms and conditions of the applicable equity incentive plan or plans then in effect and will be evidenced by an award agreement issued under the applicable plan. The target aggregate grant date fair value of each such Annual Grant shall be two hundred percent (200%) of Mr. Kornberg’s Base Salary (the “Target Grant”); provided, however, that the actual amount of any such award shall be determined in the reasonable discretion of the Compensation Committee and/or the Board and may be greater than the Target Grant but shall not be less than the Target Grant. Each Annual Grant shall be fully vested on the date of grant; provided, however, that any equity incentive grant Mr. Kornberg receives that is not an Annual Grant will be subject to the vesting provisions contained in the applicable award agreement.

### Compensation Upon Termination.

Termination Generally. If Mr. Kornberg’s employment with the Company is terminated for any reason, the Company shall pay or provide to Mr. Kornberg (or to his authorized representative or estate) (i) any Base Salary earned through the Date of Termination (paid on or before the time required by law but in no event more than thirty (30) days after the Date of Termination); (ii) if the Date of Termination occurs following the end of a given calendar year, but prior to payment of the Annual Bonus with respect to such year, the Annual Bonus payable for such prior calendar year (paid in accordance with Section 2(c)(i)); (iii) if applicable under Section 2(c)(i), the Pro-Rata Bonus for the year during which the Date of Termination occurs (paid at the time the Company pays bonuses with respect to such year); (iv) unpaid expense reimbursements (subject to, and in accordance with, Sections 2(d), 2(f) and 2(i) of this Agreement) and, if applicable under Section 2(h), unused

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vacation that accrued through the Date of Termination (paid on or before the time required by law but in no event more than thirty (30) days after the Date of Termination); and (v) any vested benefits the Executive may have under any Executive Benefit Plan or other employee benefit plan of the Company through the Date of Termination, which vested benefits shall be paid and/or provided in accordance with the terms of such benefit plans (collectively, the “Accrued Benefits”).

Termination by the Company Without Cause or by the Executive with Good Reason. During the Term, if Mr. Kornberg’s employment is terminated by the Company without Cause as provided in Section 3(d) or Mr. Kornberg terminates his employment for Good Reason as provided in Section 3(e), then the Company shall pay Mr. Kornberg his Accrued Benefits (as provided in Section 4(a) above). In addition, subject to Mr. Kornberg signing a full and final release of all releasable claims in favor of the Company and related persons and entities in a reasonable form and manner reasonably satisfactory to the Company (the “Release”) and the expiration of the applicable revocation period for the Release:

- a. the Company shall pay Mr. Kornberg an amount equal to two (2) times the sum of (x) the Executive's Base Salary; and (y) the Executive's Target Annual Bonus (*i.e.*, one hundred percent (100%) of the Target Annual Bonus amount as if employed for the full year and all applicable performance metrics had been fully achieved) (the “Severance Amount”). The Severance Amount shall be paid in a cash lump sum payment within sixty (60) days after the Date of Termination; provided, however, that if the sixty (60) day period begins in one calendar year and ends in a second calendar year, the lump sum payment of the Severance Amount shall be paid in the second calendar year (but prior to the end of the sixty (60) day period). Each payment pursuant to this Agreement is intended to constitute a separate payment for purposes of Treasury Regulations Section 1.409A-2(b)(2);
- b. effective upon the Date of Termination, all stock options and other stock-based awards (including, without limitation, all such awards/grants under Sections 2(b)(ii) and 2(c)(ii)) held by Mr. Kornberg and all yet unvested portions thereof shall immediately and fully accelerate and vest and become exercisable or nonforfeitable as of the Date of Termination (to the extent that the Release is not effective as of the Date of Termination, the Company shall take all necessary corporate action to ensure that no such stock-based awards terminate or are forfeited by Mr. Kornberg from the Date of Termination until the date such accelerated vesting and/or exercisability becomes effective);
- c. if the Annual Grant had not been made with respect to the year in which the Date of Termination occurs, the Company shall grant to Mr. Kornberg on the Date of Termination such number of shares of common stock with an aggregate fair market value on the Date of Termination equal to two hundred percent (200%) of Mr. Kornberg's Base Salary (which grant shall be fully vested on the Date of Termination); and
- d. the Company shall provide Mr. Kornberg (and, as applicable, his spouse and eligible dependents) with continued medical (health, dental, and vision), life insurance (as provided in Section 2(g) above) and disability benefits, at the Company's expense, to the same extent in which the Executive participated prior to the Date of Termination for a period of eighteen (18) months following the Date of Termination; provided, however, if the Company cannot provide, for any reason, Mr. Kornberg or his dependents with the opportunity to participate in the benefits to be provided pursuant to this paragraph (at the Company's expense), the Company shall pay to Mr. Kornberg a single sum cash payment, payable within sixty (60) days following the date the Company cannot provide such benefits, in an amount equal to the fair market value of the benefits to be provided pursuant to this paragraph plus an amount necessary to “gross-up” Mr. Kornberg with respect to any Federal, state or local taxation due on such single sum cash payment. If Mr. Kornberg (and his spouse and dependents, as applicable) was/were covered by Mr. Kornberg's own health insurance premiums for which Mr. Kornberg was being reimbursed pursuant to Section 2(t) above, then the Company shall pay to Mr. Kornberg a single sum cash payment, payable within sixty (60) days following the Date of Termination, equal to the total amount of the monthly premiums for such insurance coverage for a period of eighteen (18) months.



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Change in Control Payment. The provisions of this set forth certain terms of an agreement reached between Mr. Kornberg and the Company regarding Mr. Kornberg's rights and obligations upon the occurrence of a Change in Control of the Company. These provisions are intended to assure and encourage in advance Mr. Kornberg's continued attention and dedication to his assigned duties and his objectivity during the pendency and/or after the occurrence of any such event. These provisions shall apply in lieu of, and expressly supersede, the provisions of Section 4 regarding severance pay and benefits upon a termination of employment by the Company without Cause as provided in Section 3(d), if such termination of employment occurs in connection with or within eighteen (18) months after the occurrence of the first event constituting a Change in Control. These provisions shall terminate and be of no further force or effect beginning eighteen (18) months after the occurrence of a Change in Control if Mr. Kornberg remains employed with the Company through and at such time.

Change in Control. In the event of a Change in Control (as defined below):

- a. notwithstanding anything to the contrary in any applicable option agreement or stock-based award agreement, all stock options and other stock-based awards held by Mr. Kornberg (including, without limitation, all such awards/grants under Sections 2(b)(ii) and 2(c)(ii)) and all yet unvested portions thereof shall immediately and fully accelerate and vest and become fully exercisable or nonforfeitable as of immediately prior to the closing or occurrence (as applicable) of the event constituting the Change in Control; and
- b. if, in connection with or within eighteen (18) months after a Change in Control, Mr. Kornberg's employment is terminated by the Company without Cause as provided in Section 3(d) or Mr. Kornberg terminates his employment for any reason, then the Company shall pay Mr. Kornberg his Accrued Benefits (as provided in Section 4(a) above). In addition, subject to the signing of the Release by the Executive and the expiration of the applicable revocation period for the Release:
  - (A) the Company shall pay Mr. Kornberg a lump sum in cash in an amount equal to three (3) times the sum of (A) Mr. Kornberg's current Base Salary (or the Executive's Base Salary in effect immediately prior to the Change in Control, if higher); and (B) Mr. Kornberg's Target Annual Bonus (or Mr. Kornberg's Target Annual Bonus in effect immediately prior to the Change in Control, if higher). Such payment shall be paid within sixty (60) days after the Date of Termination; provided, however, that if the sixty (60) day period begins in one calendar year and ends in a second calendar year, such payment shall be paid in the second calendar year (but prior to the end of the sixty (60) day period);
  - (B) to the extent not covered by and accelerated pursuant to Section 5(a)(i) above, effective upon the Date of Termination all stock options and other stock-based awards (including, without limitation, all such awards/grants under Sections 2(b)(ii) and 2(c)(ii)) held by Mr. Kornberg and all yet unvested portions thereof shall immediately and fully accelerate and vest and become exercisable or nonforfeitable as of the Date of Termination (to the extent that the Release is not effective as of the Date of Termination, the Company shall take all necessary corporate action to ensure that no such stock-based awards terminate or are forfeited by Mr. Kornberg from the Date of Termination until the date such accelerated vesting and/or exercisability becomes effective);
  - (C) if the Annual Grant had not been made with respect to the year in which the Date of Termination occurs, the Company shall grant to Mr. Kornberg on the Date of Termination such number of shares of common stock with an aggregate fair market value on the Date of Termination equal to two hundred percent (200%) of Mr. Kornberg's Base Salary (which grant shall be fully vested on the Date of Termination); and
  - (D) the Company shall provide Mr. Kornberg (and, as applicable, his spouse and eligible dependents) with continued medical (health, dental, and vision), life insurance (as provided in Section 2(g) above) and disability benefits, at the Company's expense, to the same extent in which Mr. Kornberg participated prior to the Date of Termination for a period of eighteen (18) months following the Date of Termination; provided, however, if the Company cannot provide,

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for any reason, Mr. Kornberg or his dependents with the opportunity to participate in the benefits to be provided pursuant to this paragraph (at the Company's expense), the Company shall pay to Mr. Kornberg a single sum cash payment, payable within sixty (60) days following the date the Company cannot provide such benefits, in an amount equal to the fair market value of the benefits to be provided pursuant to this paragraph plus an amount necessary to "gross-up" Mr. Kornberg with respect to any Federal, state or local taxation due on such single sum cash payment. If Mr. Kornberg (and his spouse and dependents, as applicable) was/were covered by Mr. Kornberg's own health insurance premiums for which Mr. Kornberg was being reimbursed pursuant to Section 2(f) above, then the Company shall pay to Mr. Kornberg a single sum cash payment, payable within sixty (60) days following the Date of Termination, equal to the total amount of the monthly premiums for such insurance coverage for a period of eighteen (18) months.

### (E) Gross-Up Payment.

- (i) Anything in this Agreement to the contrary notwithstanding, in the event it shall be determined that the amount of any compensation, payment or distribution by the Company to or for the benefit of Mr. Kornberg, whether paid or payable or distributed or distributable pursuant to the terms of this Agreement or otherwise, calculated in a manner consistent with Section 280G of the Internal Revenue Code of 1986, as amended (the "Code") and the applicable regulations thereunder (the "Severance Payments"), would be subject to the excise tax imposed by Section 4999 of the Code, or any interest or penalties are incurred by Mr. Kornberg with respect to such excise tax (such excise tax, together with any such interest and penalties, are hereinafter collectively referred to as the "Excise Tax"), then Mr. Kornberg shall be entitled to receive an additional payment or payments (collectively, the "Gross-Up Payment") such that the net amount retained by Mr. Kornberg, after deduction of any Excise Tax on the Severance Payments, any Federal, state, and local income tax, employment tax and Excise Tax upon the payment provided by this Section, and any interest and/or penalties assessed with respect to such Excise Tax, shall be equal to the Severance Payments.
- (ii) Subject to the provisions of Section 5(b)(iii) below, all determinations required to be made under this Section 5(b)(ii), including whether a Gross-Up Payment is required and the amount of such Gross-Up Payment, shall be made by a nationally recognized accounting firm selected by the Company (the "Accounting Firm"), which shall provide detailed supporting calculations both to the Company and Mr. Kornberg within fifteen (15) business days of the Date of Termination, if applicable, or at such earlier time as is reasonably requested by the Company or Mr. Kornberg. For purposes of determining the amount of the Gross-Up Payment, Mr. Kornberg shall be deemed to pay federal income taxes at the highest marginal rate of federal income taxation applicable to individuals for the calendar year in which the Gross-Up Payment is to be made, and state and local income taxes at the highest marginal rates of individual taxation in the state and locality of Mr. Kornberg's residence on the Date of Termination, net of the maximum reduction in federal income taxes which could be obtained from deduction of such state and local taxes. The Gross-Up Payment, if any, as determined pursuant to this Section 5(b)(ii), shall be paid to the relevant tax authorities as withholding taxes on behalf of Mr. Kornberg at such time or times when each Excise Tax payment is due. Any determination by the Accounting Firm shall be binding upon the Company and Mr. Kornberg. As a result of the uncertainty in the application of Section 4999 of the Code at the time of the initial determination by the Accounting Firm hereunder, it is possible that Gross-Up Payments which will not have been made by the Company should have been made (an "Underpayment"). In the event that the Company exhausts its remedies pursuant to Section 5(b)(iii) below and Mr. Kornberg thereafter is required to make a payment of any Excise Tax, the Accounting Firm shall determine the amount of the Underpayment that has occurred, consistent with the calculations required to be made hereunder, and any such Underpayment, and any interest

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and penalties imposed on the Underpayment and required to be paid by Mr. Kornberg in connection with the proceedings described in Section 5(b)(iii) below, shall be promptly paid by the Company to the relevant tax authorities as withholding taxes on behalf of Mr. Kornberg.

- (iii) Mr. Kornberg shall notify the Company in writing of any claim by the Internal Revenue Service that, if successful, would require the payment by the Company of the Gross-up Payment. Such notification shall be given as soon as practicable but no later than ten (10) business days after Mr. Kornberg knows of such claim and shall apprise the Company of the nature of such claim and the date on which such claim is requested to be paid. Mr. Kornberg shall not pay such claim prior to the expiration of the thirty (30) day period following the date on which he gives such notice to the Company (or such shorter period ending on the date that any payment of taxes with respect to such claim is due). If the Company notifies Mr. Kornberg in writing prior to the expiration of such period that it desires to contest such claim, provided that the Company has set aside adequate reserves to cover the Underpayment and any interest and penalties thereon that may accrue, the Executive shall:
- (A) give the Company any information reasonably requested by the Company relating to such claim;
  - (B) take such action in connection with contesting such claim as the Company shall reasonably request in writing from time to time, including, without limitation, accepting legal representation with respect to such claim by an attorney selected by the Company;
  - (C) cooperate with the Company in good faith in order to effectively contest such claim; and
  - (D) permit the Company to participate in any proceedings relating to such claim; provided, however, that the Company shall bear and pay directly all costs and expenses (including additional interest and penalties) incurred in connection with such contest and shall indemnify and hold Mr. Kornberg harmless, on an after-tax basis, for any Excise Tax or income tax, including interest and penalties with respect thereto, imposed as a result of such representation and payment of costs and expenses.
- (iv) If, after a Gross-Up Payment by the Company on behalf of Mr. Kornberg pursuant to this Section 5(b), Mr. Kornberg becomes entitled to receive any refund with respect to such claim, Mr. Kornberg shall (subject to the Company's complying with the requirements of Section 5(b)(iii)) promptly pay to the Company the amount of such refund (together with any interest paid or credited thereon after taxes applicable thereto).

Definitions. For purposes of this Section 5, the following terms shall have the following meanings:

"Change in Control" shall mean any of the following:

- (i) there is consummated a merger, consolidation, statutory exchange or reorganization, unless securities representing more than fifty percent (50%) of the total combined voting power of the outstanding voting securities of the successor corporation are immediately thereafter beneficially owned directly or indirectly and in substantially the same proportion, by the persons who beneficially owned the Company's outstanding voting securities immediately prior to such transaction;
- (ii) any transaction or series of related transactions pursuant to which any person or any group of persons comprising a "group" within the meaning of Rule 13d-5(b)(1) under the Securities Exchange Act of 1934, as amended (other than the Company or a person that, prior to such transaction or series of related transactions, directly or indirectly, is controlled by or is under common control with the Company) becomes directly or indirectly the beneficial owner (within the meaning of Rule 13d-3 of the Securities Exchange Act of 1934, as amended) of securities possessing (or convertible into or exercisable for securities possessing) thirty percent (30%) or more of the total

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combined voting power of the securities (determined by the power to vote with respect to the elections of Board members) outstanding immediately after the consummation of such transaction or series of related transactions, whether such transaction involves a direct issuance from the Company or the acquisition of outstanding securities held by one or more of the Company's shareholders;

- (iii) there is consummated a sale, lease, exclusive license, or other disposition of all or substantially all of the consolidated assets of the Company and its subsidiaries, other than a sale, lease, license, or other disposition of all or substantially all of the consolidated assets of the Company and its subsidiaries to an entity, more than fifty percent (50%) of the combined voting power of the voting securities of which are owned by shareholders of the Company in substantially the same proportions as their ownership of the Company immediately prior to such sale, lease, license, or other disposition; or
- (iv) individuals who, on the Effective Date, are members of the Board (the "Incumbent Board") cease for any reason to constitute at least a majority of the members of the Board; provided, however, that if the appointment or election (or nomination for election) of any new director was approved or recommended by a majority vote of the members of the Incumbent Board then still in office, such new director shall, for purposes of sentence, be considered as a member of the Incumbent Board.

Notwithstanding the foregoing, a "Change in Control" shall not be deemed to have occurred for purposes of the foregoing clause (ii) solely as the result of (A) the acquisition of additional securities by Dr. Samuel Herschkowitz, Joshua Kornberg or their affiliates; or (B) a repurchase or other acquisition of securities by the Company which, by reducing the number of shares of voting securities outstanding, increases the proportionate number of voting securities beneficially owned by any person to thirty percent (30%) or more of the combined voting power of all of the then outstanding voting securities; provided, however, that if any person referred to in this clause (B) shall thereafter become the beneficial owner of any additional shares of voting securities (other than pursuant to a stock split, stock dividend, or similar transaction or as a result of an acquisition of securities directly from the Company) and immediately thereafter beneficially owns thirty percent (30%) or more of the combined voting power of all of the then outstanding voting securities, then a "Change in Control" shall be deemed to have occurred for purposes of the foregoing clause (ii).

### *Employment Agreements with Chief Operating Officer and Chief Financial Officer.*

On August 13, 2012, the Company entered into employment agreements with David O. Johnson, who has served as Chief Operating Officer since July 1, 2012, and Bob Myers, who has served as Chief Financial Officer since July 1, 2012 (Messrs. Johnson and Myers are referred to as the "executives"). Under the agreements the employment of each of these individuals with the Company is at will.

The annualized base salaries of Messrs. Johnson and Myers were \$150,000 and \$125,000, respectively for their first year employed. Effective July 1, 2013 the annualized base salaries of Messrs. Johnson and Myers were \$180,000 and \$150,000, respectively. Effective in March 2014 Mr. Myers annualized base salary was increased to \$165,000. Such base salaries may be adjusted by the Company but may not be reduced except in connection with a reduction imposed on substantially all employees as part of a general reduction. The executives will also each be eligible to receive an annual incentive bonus for each calendar year at the end of which he remains employed by the Company, subject to the attainment of certain objectives. The executives have a minimum bonus guarantee of twenty percent (20%) of their annualized salary. Messrs. Johnson and Myers each had received ten year stock options to purchase 1 million shares of common stock at \$.08 per share with each option vested immediately with respect to 700,000 shares and with the remaining 300,000 shares to vest 18 months after the date of grant. The executives received bonuses for 2012 equal to one hundred percent (100%) of their annualized salary; fifty percent (50%) in cash and fifty percent (50%) in options to purchase 949,368 and 791,140 shares of common stock, respectively, at \$.079 per share, with each option vesting immediately. Also, in 2013 the 300,000 unvested shares for Messrs. Johnson and Myers were accelerated to immediate vesting.

If the Company terminates the executive's employment without cause or if the executive terminates his employment for "good reason," he shall be entitled to receive from Company severance pay in an amount equal to (a) before the first anniversary of the date of the agreement, three months of base salary, or (b) on or

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after the first anniversary of the date of the agreement, twelve months of base salary, in either case less applicable taxes and withholdings. In that event, he will receive a bonus payment on a pro-rata basis through the date of termination and any accrued, unused vacation pay. The severance pay, bonus payment, and other consideration are conditioned upon executive's execution of a full and final release of liability. "Cause" is defined to mean the executive engages in willful misconduct or fails to follow the reasonable and lawful instructions of the Board, if such conduct is not cured within 30 days after notice; the executive embezzles or misappropriates assets of Company or any of its subsidiaries; the executive's violation of his obligations in the agreement, if such conduct is not cured within 30 days after notice; breach of any agreement between the executive and the Company or to which Company and the executive are parties, or a breach of his fiduciary responsibility to the Company; commission by of fraud or other willful conduct that adversely affects the business or reputation of Company; or, Company has a reasonable belief the executive engaged in some form of harassment or other improper conduct prohibited by Company policy or the law. "Good reason" is defined as (i) a material diminution in Employee's position, duties, base salary, and responsibilities; or (ii) Company's notice to Employee that his or her position will be relocated to an office which is greater than 100 miles from Employee's prior office location. In all cases of Good Reason, Employee must have given notice to Company that an alleged Good Reason event has occurred and the circumstances must remain uncorrected by Company after the expiration of (30) days after receipt by Company of such notice.

During each executive's employment with the Company and for twelve months thereafter, regardless of the reason for the termination, he will not engage in a competing business, as defined in the agreement and will not solicit any person to leave employment with the Company or solicit clients or prospective clients of the Company with whom he worked, solicited, marketed, or obtained confidential information about during his employment with the Company, regarding services or products that are competitive with any of the Company's services or products.

### **Potential Payments Upon Termination or Change of Control**

Most of our stock option agreements provide for an acceleration of vesting in the event of a change in control as defined in the 2012 Stock Incentive Plan. Also, see "Employment Contracts" below.

Most of our stock option agreements provide for an acceleration of vesting in the event of a change in control as defined in the agreements and in the 2012 Stock Incentive Plan. Additionally, the restricted stock agreements that were awarded to management and directors in 2013 also provide for an acceleration of vesting in the event there is a change in control as defined in the 2012 Plan. Also, see "Employment Contracts" above.

### **Adoption of 2012 Stock Incentive Plan**

*2012 Stock Incentive Plan.* On August 13, 2012, board adopted the 2012 Stock Incentive Plan (the "Plan") and the Plan became effective. The shareholders approved the Plan on September 20, 2013. The Plan replaced the 2008 Equity Incentive Plan (the "2008 Plan"). A summary of the Plan is as follows:

*General.* The purpose of the Plan is to increase shareholder value and to advance the interests of the Company by furnishing a variety of economic incentives designed to attract, retain and motivate employees, certain key consultants and directors of the Company. The Plan is administered by the compensation committee, or if no committee is designated, the board. The compensation committee may grant incentives to employees (including officers) of the Company or its subsidiaries, members of the board, and consultants or other independent contractors who provide services to the Company or its subsidiaries, in the following forms: (a) non-statutory stock options and incentive stock options; (b) stock appreciation rights ("SARs"); (c) stock awards; (d) restricted stock; (e) restricted stock units ("RSUs"); and (f) performance awards.

*Shares Subject to Plan.* Subject to adjustment, the number of shares of common stock which may be issued under the Plan shall not exceed 20,000,000 shares. In addition, as of the effective date of the Plan, any shares available in the reserve of the 2008 Plan (3,850,720 shares) shall be added to the Plan share reserve and be available for issuance under the Plan. If an incentive granted under the Plan or under the 2008 Plan expires or is terminated or canceled unexercised as to any shares of common stock or forfeited or reacquired by the Company pursuant to rights reserved upon issuance thereof, such forfeited and reacquired shares may again be issued under the Plan pursuant to another incentive. The Company expects that, at a special

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shareholders meeting on April 15, 2013, the shareholders will approve an amendment to the plan to increase the number of shares issuable under the Plan by 30,000,000 shares, to a total of 50,000,000 shares, plus the previous reserve under the 2008 Plan.

### *Description of Incentives.*

**Stock Options.** The compensation committee may grant non-qualified and incentive stock options to eligible employees to purchase shares of common stock from the Company. The Plan confers on the compensation committee discretion, with respect to any such stock option, to determine the term of each option, the time or times during its term when the option becomes exercisable and the number and purchase price of the shares subject to the option. However, the option price per share may not be less than the fair market value of the common stock on the grant date, and the term of each option shall not exceed ten years and one day from the grant date. With respect to stock options which are intended to qualify as “incentive stock options” (as defined in Code Section 422), the aggregate fair market value of the shares with respect to which incentive stock options are exercisable for the first time cannot exceed \$100,000. All incentive stock options must be granted within ten years from the earlier of the date of the Plan’s adoption by the board or approval by the Company’s shareholders.

**Stock Appreciation Rights.** A stock appreciation right or “SAR” is a right to receive, without payment to the Company, a number of shares, cash or any combination thereof, the amount of which is equal to the aggregate amount of the appreciation in the shares of common stock as to which the SAR is exercised. The compensation committee has the discretion to determine the number of shares as to which a SAR will relate as well as the duration and exercisability of a SAR. The exercise price may not be less than the fair market value of the common stock on the grant date.

**Limitation on Certain Grants.** During any one fiscal year, no person shall receive Incentives under the Plan that could result in that person receiving, earning or acquiring, subject to adjustment: (a) stock options and SARs for, in the aggregate, more than 10,000,000 shares of common stock; or (b) performance awards, in the aggregate, for more than 10,000,000 shares of common stock or, if payable in cash, with a maximum amount payable exceeding \$2,000,000. The Company expects that, at a special shareholders meeting on April 15, 2013, the shareholders will approve an amendment to the plan to increase the limits on stock options and SARs and on performance awards to 20,000,000 shares each.

**Stock Awards.** Stock awards consist of the transfer by the Company to an eligible participant of shares of common stock, with or without other payment, as additional compensation for services to the Company. The number of shares transferred pursuant to any stock award is determined by the compensation committee.

**Restricted Stock.** Restricted stock consists of the sale or transfer by the Company to an eligible participant of one or more shares of common stock that are subject to restrictions on their sale or other transfer by the employee which restrictions will lapse after a period of time as determined by the compensation committee. If restricted stock is sold to a participant, the sale price will be determined by the compensation committee, and the price may vary from time to time and among participants and may be less than the fair market value of the shares at the date of sale. Subject to these restrictions and the other requirements of the Plan, a participant receiving restricted stock shall have all of the rights of a shareholder as to those shares.

**RSUs.** Restricted stock units represent the right to receive one share of common stock at a future date that has been granted subject to terms and conditions, including a risk of forfeiture, established by the compensation committee. Dividend equivalents may be granted with respect to any amount of RSU’s and either paid at the dividend payment date in cash or in shares of unrestricted stock having a fair market value equal to the amount of such dividends, or deferred with respect to such RSU’s and the amount or value thereof automatically deemed reinvested in additional RSU’s until the time for delivery of shares pursuant to the terms of the restricted stock unit award. RSU’s may be satisfied by delivery of shares of stock, cash equal to the fair market value of the specified number of shares covered by the RSU’s, or a combination thereof, as determined by the compensation committee at the date of grant or thereafter.

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Performance Awards. A performance award is a right to either a number of shares of common stock, their cash equivalent, or a combination thereof, based on satisfaction of performance goals for a particular period. At or about the same time that performance goals are established for a specific period, the compensation committee shall in its absolute discretion establish the percentage of the performance awards granted for such performance period which shall be earned by the participant for various levels of performance measured in relation to achievement of performance goals for such performance period.

Performance goals applicable to a performance award will be established by the compensation committee not more than 90 days after the beginning of the relevant performance period. The performance goals for performance awards that are intended to qualify as “performance based” compensation within the meaning of Section 162(m) of the Code must be based on one or more of the business criteria specified in the Plan, including earnings per share, operating income or profit, net income, gross or net sales, or other specified criteria. The compensation committee may modify the performance goals if it determines that circumstances have changed and modification is required to reflect the original intent of the performance goals; provided, however, that no such change or modification may be made to the extent it increases the amount of compensation payable to any participant who is a “covered employee” within the meaning of Code Section 162(m).

The compensation committee will determine the terms and conditions applicable to any performance award, which may include restrictions on the delivery of common stock payable in connection with the performance award, the requirement that the stock be delivered in the form of restricted stock, or other restrictions that could result in the future forfeiture of all or part of any stock earned. The compensation committee will, as soon as practicable after the close of a performance period, determine the extent to which the performance goals for such performance period have been achieved; and the percentage of the performance awards earned as a result. Performance awards will not be earned for any participant who is not employed by the Company or a subsidiary continuously during the entire performance period for which such performance award was granted, except in certain events such as death, disability or retirement.

Transferability of Incentives. Incentives granted under the Plan may not be transferred, pledged or assigned by the holder thereof except, in the event of the holder’s death, by will or the laws of descent and distribution or pursuant to a qualified domestic relations order. However, non-qualified stock options may be transferred by the holder thereof to certain family members or related entities.

Duration, Termination and Amendment of the Incentive Plan and Incentives. The Plan will remain in effect until all Incentives granted under the Plan have been satisfied or terminated and all restrictions on shares issued under the Plan have lapsed. No Incentives may be granted under the Plan after August 13, 2022, the tenth anniversary of the approval of the Plan by the Board of Directors. The Board of Directors may amend or discontinue the Plan at any time. However, no such amendment or discontinuance may adversely change or impair a previously granted incentive without the consent of the recipient thereof. Certain Plan amendments require shareholder approval, including amendments which would increase the maximum number of shares of common stock which may be issued to all participants under the Plan, change the class of persons eligible to receive Incentives under the Plan, or materially increase the benefits accruing to participants under the Plan. Generally, the terms of an existing incentive may be amended by agreement between the compensation committee and the participant. However, in the case of a stock option or SAR, no such amendment shall (a) without shareholder approval, lower the exercise price of a previously granted stock option or SAR when the exercise price per share exceeds the fair market value of the underlying shares in exchange for another incentive or cash or take any other action with respect to a stock option that may be treated as a re-pricing under the federal securities laws or generally accepted accounting principles, or (b) extend the term of the incentive, with certain exceptions.

Change in Control: Effect of Sale, Merger, Exchange or Liquidation. Upon the occurrence of an event satisfying the definition of “change in control” with respect to a particular incentive, unless otherwise provided in the agreement for the incentive, such incentive shall become vested and all restrictions shall lapse. The compensation committee may, in its discretion, include such further provisions and limitations in any agreement for an incentive as it may deem desirable. The definition of “change in control” is similar to that in Mr. Komberg’s employment agreement. Unless otherwise provided in the agreement for an incentive, in the

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event of an acquisition of the Company through the sale of substantially all of the Company's assets or through a merger, exchange, reorganization or liquidation of the Company or a similar event, the compensation committee has broad discretion to take any and all action it deems equitable under the circumstances, including but not limited to terminating the Plan and all incentives and issuing to the holders of outstanding vested options and SARs the stock, securities or assets they would have received if the incentives had been exercised immediately before the transaction, or other specified actions.

Amendment to Agreement. The Compensation Committee amended Mr. Kornberg's Employment Agreement. In this amendment the Committee has approved for Mr. Kornberg, among other things, an increase in his base salary to \$250,000 per year and a further grant of 5,000,000 shares of restricted stock relating to fiscal 2012 performance that would vest only upon certain events relating to a change in control of the Company.

### **Director Compensation**

The directors of Skyline Medical Inc. are not paid cash compensation for their service on the Board except for Lawrence Gadbaw, the former Chairman of the Board, who was paid \$2,000 per month for his service as Chairman of the Board.

Mr. Gadbaw and Dr. Peter Morawetz were awarded 20,000 shares of common stock, par value \$0.01 by the Board upon resigning from the Board in 2013. Additionally, both Mr. Gadbaw and Dr. Morawetz were awarded 30,000 shares of common stock, par value \$0.01 by the Board pursuant to prior agreements recognizing the attainment of a fund-raising threshold.

Effective in 2013 the Board instituted a quarterly and an annual stock options award program for all the directors under which they will be awarded options to purchase 5,000 shares of common stock, par value \$0.01 per quarter at an exercise price determined by the close on the last day of the quarter. Additionally, the directors that serve on a committee will receive options to purchase 10,000 shares of common stock, par value \$0.01 annually, per committee served, at an exercise price determined by the close on the last day of the year.

### **Director Compensation Table for Fiscal 2013**

The following table summarizes the compensation paid to each non-employee director in the fiscal year ended December 31, 2013.

<u>Name</u>	<u>Fees Paid or Earned in Cash</u>	<u>Stock Awards</u>	<u>Option Awards</u>	<u>Total</u>
<b>Lawrence W. Gadbaw<sup>(1)</sup></b>	<b>\$ 26,000</b>	<b>15,900</b>		<b>\$ 41,900</b>
<b>Peter Morawetz<sup>(2)</sup></b>	<b>\$ —</b>	<b>15,900</b>		<b>\$ 15,900</b>
<b>Thomas McGoldrick<sup>(3)</sup></b>	<b>\$ —</b>	<b>21,459</b>		<b>\$ 21,459</b>
<b>Ricardo Koenigsberger<sup>(4)</sup></b>	<b>\$ —</b>	<b>21,459</b>		<b>\$ 21,459</b>
<b>Andrew Reding<sup>(5)</sup></b>	<b>\$ —</b>	<b>14,295</b>		<b>\$ 14,295</b>
<b>Dr. Arnon Dreyfuss<sup>(6)</sup></b>	<b>\$ —</b>	<b>14,295</b>		<b>\$ 14,295</b>
<b>Frank Mancuso Jr.<sup>(7)</sup></b>	<b>\$ —</b>	<b>14,295</b>		<b>\$ 14,295</b>

(1) Mr. Gadbaw received \$2,000 per month as compensation for serving as Chairman of the Board. At the end of fiscal 2012 he was owed \$10,000 in compensation that was paid in 2013. Mr. Gadbaw also received \$16,000 in total in 2013 for 8 monthly fees paid until he resigned from the Board in August 2013. Mr. Gadbaw was awarded 50,000 shares of common stock, par value \$0.01 when he resigned.

(2) Dr. Morawetz was awarded 50,000 shares of common stock, par value \$0.01 when he resigned in August 2013.

(3) Mr. McGoldrick was awarded options to purchase 108,316 shares of common stock both for serving on the Board and for participating on the Audit and Corporate Governance Committees.

(4) Mr. Koenigsberger was awarded options to purchase 108,316 shares of common stock both for serving on the Board and for participating on the Audit and Corporate Governance Committees.

(5) Mr. Reding was awarded options to purchase 71,279 shares of common stock both for serving on the Board and for participating on the Audit Committee.



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- (6) Dr. Dreyfuss was awarded options to purchase 71,279 shares of common stock both for serving on the Board and for participating on the Compensation Committee.
- (7) Mr. Mancuso was awarded options to purchase 71,279 shares of common stock both for serving on the Board and for participating on the Compensation Committee.

**Equity Compensation Plan Information**

The following table presents the equity compensation plan information as of December 31, 2013:

	Number of securities to be issued upon exercise of outstanding restricted stock, warrants and options (a)	Weighted-average exercise price of outstanding options, warrants (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders <sup>(1)</sup>	33,939,398	\$ 0.085	66,060,602
Equity Compensation plans not approved by security holders	—	\$ —	—

(1) Consists of outstanding options under the 2008 Equity Incentive Plan and the 2012 Stock Incentive Plan. The remaining share authorization under the 2008 Equity Incentive Plan was been rolled over to the current 2012 Stock Incentive Plan.

## CERTAIN RELATIONSHIPS AND RELATED PARTY TRANSACTIONS

The Audit Committee has the responsibility to review and approve all transactions to which a related party and the Company may be a party prior to their implementation, to assess whether such transactions meet applicable legal requirements. Rick Koenigsberger, a director, is a holder of membership units of SOK Partners.

### *Agreements with Former Directors*

The Company entered into agreements, in 2008, with our Chairman of the Board, Lawrence Gadbow, and in 2009 with a board member, Peter Morawetz, to pay Mr. Gadbow \$25,000 and Mr. Morawetz \$30,000 upon the Company raising \$3 million in new equity. Mr. Gadbow received 277,778 shares at \$.09 per share in June 2012 as compensation in lieu of the \$25,000 cash for raising \$3 million in new equity. Mr. Gadbow was paid the balance due under his separation agreement from 2008. This amount was \$46,000 upon signing the agreement in 2008 payable at \$2,000 per month; the payments to Mr. Gadbow are complete. Mr. Gadbow was due \$10,000 in accounts payable as of December 31, 2012 pertaining to his monthly fee as Chairman of the Board of Directors. Mr. Gadbow also received a warrant for 30,000 shares at \$.15 per share in June 30, 2012 as compensation for service as Chairman. Mr. Gadbow and Mr. Morawetz have both resigned from the Board in the third quarter of 2013. Both Mr. Gadbow and Mr. Morawetz received 50,000 shares of common stock each at \$.325 per share; 20,000 of these shares were for compensation from serving as Board members and the remaining 30,000 shares were issued to satisfy previous contractual agreements.

### *Convertible Note Issuances to Dr. Samuel Herschkowitz and SOK Partners, LLC*

On September 11, 2013, both the Herschkowitz Note and the SOK Note (each as defined below) were converted in full by the holders thereof at \$0.014 per share. The principal and interest balance of the Herschkowitz Note of \$314,484 was converted into 22,463,172 shares of common stock. The principal and interest balance of the SOK Note of \$680,444 was converted into 48,603,721 shares of common stock. The collateral that secured these notes was released back to the Company.

On March 28, 2012, the Company, entered into a Convertible Note Purchase Agreement, dated as of March 28, 2012 (the "SOK Purchase Agreement") with SOK Partners, LLC ("SOK Partners"), an investment partnership. Josh Kornberg, who is the Company's Chief Executive Officer and Chairman of the Board, and Dr. Samuel Herschkowitz are affiliates of the manager of SOK Partners and Ricardo Koenigsberger, a director, is a holder of membership units of SOK Partners. Pursuant to the SOK Purchase Agreement, the Company issued a 20.0% convertible note due August 2012 in the principal amount of up to \$600,000 (the "SOK Note"). Principal and accrued interest on the SOK Note was initially due and payable on August 28, 2012. The Company's obligations under the SOK Note were secured by the grant of a security interest in substantially all tangible and intangible assets of the Company. The SOK Purchase Agreement and the SOK Note included customary events of default that include, among other things, non-payment defaults, covenant defaults, inaccuracy of representations and warranties, cross-defaults to other indebtedness and bankruptcy and insolvency defaults. The occurrence of an event of default would have resulted in the acceleration of the Company's obligations under the SOK Note, and interest rate of twenty-four (24%) percent per annum accrues if the SOK Note had not been paid when due.

On March 28, 2012, the Company received an advance of \$84,657 under the SOK Note, including a cash advance of \$60,000 net of a prepayment of interest on the first \$300,000 in advances under the SOK Note. The holder of the SOK Note was entitled to convert such note into shares of common stock of the Company at an initial conversion price per share of \$0.065 per share, subject to adjustment in the event of (1) certain issuances of common stock or convertible securities at a price lower than the conversion price of the SOK Note, and (2) recapitalizations, stock splits, reorganizations and similar events. In addition, the Company is required to issue two installments of an equity bonus to SOK Partners in the form of common stock valued at the rate of \$0.065 per share. In March 2012, the Company issued the first equity bonus to SOK Partners, consisting of 4,615,385 shares of common stock, with a second installment due within five business days after SOK Partners has made aggregate advances under the note of at least \$300,000. In May 2012, the Company issued the second installment consisting of 4,615,385 shares of common stock subsequent to SOK Partners surpassing the aggregate advances of \$300,000. Until the maturity date of the SOK Note, if the Company obtained financing from any other source without the consent of SOK Partners, then the Company was

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required to issue additional bonus equity in an amount equal to \$600,000 less the aggregate advances on the SOK Note made prior to the breach. The principal balance of the SOK Note was \$357,282 as of December 31, 2012.

As long as any amount payable under the SOK Note remained outstanding, SOK Partners or its designee were entitled to appoint a new member to the Company's Board of Directors, to be appointed upon request. As a result, Mr. Koenigsberger was appointed to the Board by SOK Partners on June 25, 2012.

On March 28, 2012, the Company signed an Amended and Restated Note Purchase Agreement, dated as of December 20, 2011, with Dr. Herschkowitz (as amended, the "Herschkwitz Purchase Agreement"). Pursuant to the Herschkowitz Purchase Agreement, the Company issued a 20.0% convertible note due June 20, 2012 in the principal amount of \$240,000 for previous advances under the note (the "Herschkwitz Note"). The Company's obligations under the Herschkowitz Note was secured by the grant of a security interest in substantially all tangible and intangible assets of the Company. The Company has previously issued to Dr. Herschkowitz an equity bonus consisting of 1,546,667 shares of common stock. An additional 7,500,000 shares were transferred to Dr. Herschkowitz effective in April 2012, upon the occurrence of an event of default on the Herschkowitz Note. On August 13, 2012, the Company entered into a settlement and forbearance agreement described below, relating to the defaults under the Herschkowitz Note and other matters.

As long as any amount payable under the Herschkowitz Note remained outstanding, Dr. Herschkowitz or his designee was entitled to appoint a special advisor to the Company's Board of Directors, to be appointed as a member of the Board upon request. Pursuant to this authority, Josh Komberg was appointed to the Board on March 9, 2012. In addition, pursuant to this authority, Ricardo Koenigsberger was appointed to the Board on June 25, 2012.

Pursuant to a letter dated April 20, 2012, Dr. Herschkowitz advised the Company of the occurrence of numerous events of default under the terms of the Herschkowitz Note and the Herschkowitz Note Purchase Agreement. As a result of such events of default, Dr. Herschkowitz asserted significant rights as a secured creditor of the Company, including his rights as a secured creditor with a security interest in substantially all assets of the Company. Without a settlement relating to the defaults and other matters, Dr. Herschkowitz could have taken action to levy upon the Company's assets, including patents and other intellectual property.

In addition, the Company and Atlantic Partners Alliance LLC ("APA") were parties to a letter agreement dated March 14, 2012, providing APA and its affiliates (including Dr. Herschkowitz and SOK) with rights to avoid dilution relating to additional issuances of equity securities by the Company through July 14, 2012, evidencing the parties' intent that APA would be provided with significant protection against dilution. This protection was in recognition of APA's investments in the Company involving a high degree of risk and the Company's contemplated need for restructuring its indebtedness, which were anticipated to result, and have resulted, in significant dilution. The parties acknowledged that Dr. Herschkowitz and SOK would not have made their historical cash investments in the Company to the same degree had the dilution protection not been provided, and the investments by these parties have enabled the Company to avoid insolvency. Since the respective dates of the Herschkowitz Note Purchase Agreement and the SOK Note Purchase Agreement, the Company has issued in excess of 16,000,000 shares of common stock to parties other than APA and its affiliates, resulting in significant dilution.

Effective August 15, 2012, the Company entered into a letter agreement with Dr. Herschkowitz, APA and SOK (the "Forbearance Agreement"). Under the Forbearance Agreement, among other things, (i) Dr. Herschkowitz agreed to forbear from asserting his rights as a secured creditor to substantially all of the Company's assets, resulting from the Company's defaults; (ii) the Company issued an aggregate 26.5 million shares of common stock to Dr. Herschkowitz and SOK and adjusted the conversion price of the Herschkowitz Note and the SOK Note, respectively, to \$0.014 per share from \$0.065 per share, to satisfy the Company's obligations to adjust for dilution under the March 14, 2012 letter agreement; (iii) Dr. Herschkowitz and SOK agreed to extend the maturity of the Herschkowitz Note and the SOK Note, respectively, to December 31, 2012; (iv) the Company agreed to pay certain compensation to Dr. Herschkowitz upon the achievement of financial milestones; and (v) Dr. Herschkowitz clarified and waived certain of his rights, including the right to interest at a penalty rate upon default.

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In the Forbearance Agreement, Dr. Herschkowitz agreed to forbear from exercising any of his rights arising under the Herschkowitz Note or the Herschkowitz Note Purchase Agreement with respect to the existing defaults against the Company, subject to the limitations set forth in the letter agreement and without releasing or waiving any future breach of the letter agreement. He further agreed to forbear from exercising any rights with respect to events of default, security interests in the collateral and other similar remedies against the Company or his interests under the Herschkowitz Note or the Herschkowitz Note Purchase Agreement until the occurrence of an event of default under the Herschkowitz Note: (a) that does not constitute an existing default and (b) occurs and accrues after the effective date of the letter agreement.

Dr. Herschkowitz and the Company acknowledged that 7.5 million shares of the Company's common stock, constituting the "penalty shares" under the Herschkowitz Note Purchase Agreement, were delivered to Dr. Herschkowitz in April 2012 as provided in the Herschkowitz Note Purchase Agreement upon an event of default. Notwithstanding a provision that would have increased the rate of interest from 20% to 24% upon an event of default, Dr. Herschkowitz agreed that the Company would not pay the increased rate of interest but would accrue interest at 20% until a subsequent event of default.

Under the Forbearance Agreement, the Herschkowitz Note and the SOK Note were amended as follows: (i) the due dates of the notes were extended to December 31, 2012, from the previous due dates of June 20, 2012 and August 28, 2012, respectively; (ii) Dr. Herschkowitz will release his security agreement after payment of all currently outstanding promissory notes to parties other than SOK; and (iii) the Herschkowitz Note was amended to add certain events of default relating to judgments against the Company or other creditors taking action with respect to the collateral. In consideration of the extension additional milestone fees were revised as described below. Pursuant to a Forbearance and Settlement Agreement with these parties dated August 15, 2012, as subsequently amended, the due date of these notes were extended to August 31, 2013.

APA and its affiliates agreed to terminate the letter agreement regarding dilution dated March 14, 2012. In consideration of the various provisions of the letter agreement and in recognition of the understanding of the parties regarding dilution and the agreements of APA and its affiliates to forbear and to extend the due dates of the notes, the Company (i) issued 13,250,000 shares to Dr. Herschkowitz, (ii) issued 13,250,000 shares to SOK, and (iii) the conversion price of the Herschkowitz Note and the SOK Note, respectively was changed to \$0.014 per share from \$0.065 per share.

In the event that the Company consummated the following series of transactions on or prior to June 30, 2013: (i) a merger or similar transaction with a public shell company, (ii) raising between \$2 million and \$4 million through an offering of the securities of the public shell company concurrent with or subsequent to the shell merger and (iii) listing the Company's shares on NASDAQ pursuant to an underwritten offering of the Company's securities resulting in gross proceeds of between \$5 million and \$30 million, then the Company would have been required to deliver to Dr. Herschkowitz the following compensation: (A) \$75,000 upon consummating the shell merger, (B) \$150,000 upon consummating the qualifying financing round and (C) 3% of the gross proceeds of the NASDAQ underwriting, which payment shall under no circumstances be less than \$200,000 or greater than \$1,000,000. The Company was also required to reimburse Dr. Herschkowitz at his actual out-of-pocket cost for reasonable expenses incurred in connection with the shell transactions, with a maximum limit of \$10,000 for such expenses.

In connection with the extension of the due date for the Herschkowitz Note and the SOK Note on March 6, 2013, the milestone fees were revised. The following fees were payable to Dr. Herschkowitz in the event that the Company consummates the following series of transactions on or prior to December 31, 2013: (i) financing raising not less than \$1 million, compensation of \$75,000; (ii) a going private transaction, compensation of \$200,000 and (iii) 3% of the gross proceeds of the NASDAQ underwriting, which payment shall under no circumstances be less than \$200,000 or greater than \$3,000,000. In May 2013 Dr. Herschkowitz received \$75,000 after the Company surpassed raising \$1 million. On January 6, 2014 a side-letter to the forbearance agreement was signed between Dr. Herschkowitz and the Company. Skyline agreed that the private offering for its Series A Convertible Preferred Stock, plus any future offering of any class of its preferred stock, shall be considered a NASDAQ underwriting for purposes of Section 8(e) of the Forbearance Agreement. As such Dr. Herschkowitz received \$200,000 or 3% of the gross proceeds of any

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such offering per the terms of Section 8(e) of the Forbearance Agreement. In addition, any listing of the Company's shares on the New York Stock Exchange shall qualify as a NASDAQ underwriting under the Forbearance Agreement. For the avoidance of doubt, the payment in the aggregate for all offerings qualifying as a NASDAQ underwriting shall under no circumstances be less than \$200,000 or greater than \$1,000,000. Section 8(e) of the Forbearance Agreement will apply to any transactions consummated by Skyline on or before June 30, 2014.

As a result of the transactions under the Forbearance Agreement and other investments, Dr. Herschkowitz, SOK and their affiliates currently own shares of common stock and securities representing beneficial ownership of approximately 57% of the Company's outstanding common stock, giving such parties significant control over election of the Board of Directors and other matters.

On November 6, 2012, the Company issued and sold convertible promissory notes in the total principal amount of \$156,243 to Dr. Herschkowitz and certain of his assignees. The Company issued to these parties an aggregate 1,562,430 shares of common stock in consideration of placement of the notes. These notes bear interest at a rate of 20% per annum and are secured by a security interest in the Company's accounts receivable, patents and certain patent rights and are convertible into common stock upon certain mergers or other fundamental transactions at a conversion price based on the trading price prior to the transaction. The proceeds from this transaction were used to pay off approximately \$155,000 in principal amount of secured indebtedness. Such notes were converted in April 2013 into 1,041,622 shares of common stock at \$.10 per share.

In December 2013 the Company received an additional \$300,000 in debt financing from SOK Partners under a non-convertible grid note due February 28, 2014, with 10% interest based on a 365 day year. Dr. Herschkowitz received 10% of the gross proceeds in advance, and the Company received \$250,000 in three tranches in December 2013. In January 2014, the Company received an additional \$20,000 from SOK Partners completing the grid note maximum. Should the company default on the note the interest rate will increase to 20% interest based on a 365 day year. In February 2014, the Company wired \$305,589.04 to SOK Partners in complete payment of the grid note, including interest.

Finally, SOK invested in the July 2014 offering of convertible notes and warrants. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Historical Financing" and "Selling Stockholders."

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**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth as of August 21, 2014 certain information regarding beneficial ownership of our common stock by:

- Each person known to us to beneficially own 5% or more of our common stock;
- Each executive officer who in this proxy statement are collectively referred to as the “Named Executive Officers;”
- Each of our directors; and
- All of our executive officers (as that term is defined under the rules and regulations of the SEC) and directors as a group.

We have determined beneficial ownership in accordance with Rule 13d-3 under the Exchange Act. Beneficial ownership generally means having sole or shared voting or investment power with respect to securities. Unless otherwise indicated in the footnotes to the table, each shareholder named in the table has sole voting and investment power with respect to the shares of common stock set forth opposite the shareholder’s name. We have based our calculation of the percentage of beneficial ownership on 223,834,099 shares of the Company’s common stock outstanding on August 21, 2014. Unless otherwise noted below, the address for each person or entity listed in the table is c/o Skyline Medical Inc., 2915 Commers Drive, Suite 900, Eagan, Minnesota 55121.

<b>Name of Beneficial Owner</b>	<b>Amount and Nature of Beneficial Ownership</b>	<b>Percent of Class</b>
Josh Kornberg <sup>(5)(6)</sup>	94,349,436	38.21%
David Johnson <sup>(2)</sup>	2,267,016	1.00%
Bob Myers <sup>(3)</sup>	2,057,010	0.91%
Ricardo Koenigsberger <sup>(4)</sup>	235,343	0.11%
Thomas J. McGoldrick <sup>(4)</sup>	353,849	0.16%
Andrew Reding <sup>(7)</sup>	263,479	0.12%
Dr. Arnon Dreyfuss <sup>(7)</sup>	2,073,545	0.93%
Frank Mancuso <sup>(7)</sup>	414,973	0.19%
<b>All directors and executive officers as a group (8 persons)</b>	<b>102,014,651</b>	<b>45.58%</b>
Sam Herschkowitz <sup>(5)(6)</sup>	117,762,938	52.61%
SOK Partners	70,916,995	31.63%
APA, SOK, Sam Herschkowitz, Josh Kornberg	141,195,379	57.19%
Carl Schwartz <sup>(8)</sup>	12,335,143	5.41%

(1) Under Rule 13d-3, a beneficial owner of a security includes any person who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise has or shares: (i) voting power, which includes the power to vote, or to direct the voting of shares; and (ii) investment power, which includes the power to dispose or direct the disposition of shares. Certain shares may be deemed to be beneficially owned by more than one person (if, for example, persons share the power to vote or the power to dispose of the shares). In addition, shares are deemed to be beneficially owned by a person if the person has the right to acquire the shares (for example, upon exercise of an option) within 60 days of the date as of which the information is provided. In computing the percentage ownership of any person, the amount of shares outstanding is deemed to include the amount of shares beneficially owned by such person (and only such person) by reason of these acquisition rights. As a result, the percentage of outstanding shares of any person as shown in this table does not necessarily reflect the person’s actual ownership or voting power with respect to the number of shares of common stock actually outstanding.

(2) Includes (i) option to purchase 1,000,000 shares of common stock at a price of \$.08 per share (ii) option to purchase 949,368 shares of common stock at a price of \$.079 per share and (iii) option to purchase 303,348 shares of common stock at a price of \$.23 per share that may be exercised within 60 days of August 21, 2014.

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- (3) Includes (i) option to purchase 1,000,000 shares of common stock at a price of \$.08 per share (ii) option to purchase 791,140 shares of common stock at a price of \$.079 per share and (iii) option to purchase 260,870 shares of common stock at a price of \$.23 per share that may be exercised within 60 days of August 21, 2014.
- (4) Includes (i) option to purchase 15,723 shares of common stock at a price of \$.318 per share (ii) option to purchase 92,593 shares of common stock at a price of \$.27, and (iii) option to purchase 100,000 shares of common stock at a price of \$.15 per share that may be exercised within 60 days of August 21, 2014.
- (5) Includes (i) options to purchase 22,906,921 shares common stock that may be exercised within the next 60 days, (ii) 70,916,995 shares owned directly by SOK Partners, (iii) two warrants to purchase 19,231 shares of common stock at a price of \$.325 per share, respectively, and (iv) 96,154 shares of common stock issuable upon conversion of 250 shares of Series A Convertible Preferred Stock, par value, \$.01, stated value \$100.00. Mr. Kornberg and Dr. Samuel Herschkowitz are the managing partners of SOK Partners.
- (6) Includes 70,916,995 shares owned directly by SOK Partners. Joshua Kornberg and Dr. Samuel Herschkowitz are the managing partners of SOK Partners.
- (7) Includes (i) option to purchase 15,723 shares of common stock at a price of \$.318 per share (ii) option to purchase 55,556 shares of common stock at a price of \$.27, and (iii) option to purchase 66,667 shares of common stock at a price of \$.15 that may be exercised within 60 days of August 21, 2014.
- (8) Includes 7,973,239 shares of common stock. Includes an option to purchase 133,333 shares of common stock at \$.15; and a warrant to purchase 4,228,571 shares of common stock at \$.15.

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### DESCRIPTION OF SECURITIES

The following information describes our capital stock and provisions of our certificate of incorporation and our bylaws. This description is only a summary. You should also refer to our certificate of incorporation and bylaws, each as amended, that have been incorporated by reference or filed with the SEC as exhibits to the registration statement on Form S-1 of which this prospectus forms a part.

#### **General**

We are authorized to issue 800 million shares of capital stock, designated as \$0.01 par value common stock, and 10 million shares of preferred stock, of which 4 million shares are authorized as Series A Convertible Preferred Stock with a stated value of \$100 per share and a par value of \$.01 per share.

#### **Common Stock**

The securities being offered by the selling stockholders are shares of our common stock. As of August 15, 2014, we had 223,809,099 shares of common stock issued and outstanding and held by 165 shareholders of record.

The holders of common stock are entitled to one vote per share on all matters to be voted upon by the shareholders, provided that no proxy shall be voted if executed more than one year prior to the date of the stockholders' meeting except as may otherwise be provided by our board of directors from time to time. Only stockholders of record at the close of business on day twenty prior to the date of the meeting are entitled to vote at the stockholders' meeting. Holders of our common stock do not have cumulative voting rights.

The holders of common stock are entitled to receive ratably any dividends that may be declared from time to time by our board of directors out of funds legally available for that purpose. In the event of our liquidation, dissolution or winding up, the holders of common stock are entitled to share ratably in all assets remaining after payment of liabilities. The common stock has no preemptive or conversion rights or other subscription rights and there are no redemption provisions applicable to our common stock. All outstanding shares of common stock are fully paid and non-assessable, and the shares of common stock offered in this offering will be fully paid and not liable for further call or assessment.

Except for directors, who are elected by receiving the highest number of affirmative votes of the shares entitled to be voted for them, or as otherwise required by Delaware law, and subject to the rights of the holders of preferred stock then outstanding (if any), all shareholder action is taken by the vote of a majority of the issued and outstanding shares of common stock present at a meeting of shareholders at which a quorum consisting of a majority of the issued and outstanding shares of common stock is present in person or proxy. In the absence of a quorum for the transaction of business, any meeting may be adjourned from time to time. The stockholders present at a duly called or held meeting may continue to do business until adjournment, notwithstanding the withdrawal of enough stockholders to leave less than a quorum. Our President or, in his absence, the Vice-President or any other person designated from time to time by the board of directors, shall preside at all meetings of stockholders.

#### **Series A Convertible Preferred Stock**

On February 4, 2014, the Company entered into a Securities Purchase Agreement with certain investors pursuant to which the Company agreed to offer and sell 20,550 shares of Series A Convertible Preferred Stock, par value \$0.01 (the "Preferred Shares"), in addition to warrants to purchase shares of the Company's common stock. On August 4, 2014, the Company issued additional warrants to such investors, which was required because the Company's common stock was not listed on NASDAQ within 180 days of the closing of the offering of the Preferred Shares.

In connection with the Company's offering of convertible promissory notes and accompanying warrants (see "Convertible Notes and Warrants" below), the minimum requisite number of holders of Preferred Shares executed a Waiver and Consent of, and Notice to, Holder of Preferred Stock of the Company with such holders as of July 23, 2014 (the "Waiver and Consent"), pursuant to which the Company agreed, among other things, to issue certain additional shares of its common stock to the holders of Preferred Shares upon the conversion of such Preferred Shares under the terms and conditions described therein. The terms and conditions of the Securities Purchase Agreement relating to the Preferred Shares, the Waiver and Consent and



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related documents are described herein under “Management’s Discussion and Analysis of Results of Operations and Financial Condition — Liquidity and Capital Resources — 2014 Sales of Preferred Stock and Warrants.”

### **Convertible Notes and Warrants**

On July 23, 2014, the Company entered into Securities Purchase Agreements with certain investors, including SOK Partners, LLC, an affiliate of the Company, pursuant to which the Company agreed to offer and sell an aggregate of \$733,173.60 in principal amount of senior convertible notes (the “Convertible Notes”), in addition to warrants to purchase shares of the Company’s common stock. The terms and conditions of such Securities Purchase Agreements, the Convertible Notes, the warrants and related documents described herein under “Management’s Discussion and Analysis of Results of Operations and Financial Condition — Liquidity and Capital Resources — 2014 Sales of Convertible Notes and Warrants.” Also, see the description of certain terms of these sales herein under “Selling Stockholders.”

On July 31, 2014, August 8, 2014, August 12, 2014, September 4, 2014 and September 5, 2014, the Company entered into Securities Purchase Agreements with certain affiliates of the Company and certain persons with whom the Company has a pre-existing relationship pursuant to which the Company agreed to offer and sell an aggregate of \$1,069,221.50 in principal amount of Convertible Notes, in addition to warrants to purchase shares of the Company’s common stock. These were sales of “Affiliate Securities” as described herein under “Management’s Discussion and Analysis of Results of Operations and Financial Condition — Liquidity and Capital Resources — 2014 Sales of Convertible Notes and Warrants.” As described therein, the terms of the applicable documents for the sales of Affiliate Securities were substantially the same as for the Securities Purchase Agreements, the Convertible Notes, the warrants and related documents, except for applicable dates. Also, see the description of certain terms of these sales herein under “Selling Stockholders.”

### **Dividends**

We currently intend to retain any future earnings to support the development and expansion of our business and do not anticipate paying common stock cash dividends in the foreseeable future. Our payment of any future common stock dividends will be at the discretion of our Board of Directors after taking into account various factors, including but not limited to, our financial condition, operating results, cash needs, growth plans and the terms of any credit agreements that we may be a party to at the time. In addition, our ability to pay dividends on our common stock may be limited by state law. Accordingly, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize certain returns on their investment.

The Company completed the offering of Preferred Shares in February 2014, issuing Series A Convertible Preferred Stock paying dividends at 6% of the Stated Value per annum on a quarterly basis (see “Series A Convertible Preferred Stock” above). The Company has paid such dividends in shares of common stock. See Note 3 to the Condensed Financial Statements for the six months ended June 30, 2014 included in this prospectus.

### **Registration Rights**

In connection with each of the private placements that closed in February 2014, July 2014 and August 2014, the Company agreed to register the resale of the shares of common stock underlying the Preferred Shares, Convertible Notes and warrants, within customary timeframes after the closings of such offerings.

### **Anti-Takeover Effects of Certain Provisions of Delaware Law**

Certain provisions of Delaware law described below could have an anti-takeover effect. These provisions are intended to provide management flexibility, to enhance the likelihood of continuity and stability in the composition of our board of directors and in the policies formulated by our board of directors and to discourage an unsolicited takeover if our board of directors determines that such a takeover is not in our best interests or the best interests of our shareholders. These provisions, however, could have the effect of discouraging certain attempts to acquire us that could deprive our shareholders of opportunities to sell their shares of our stock at higher values.

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Delaware law restricts certain business combination transactions between a shareholder acquiring 15% or more (designated as an “interested” shareholder) of the voting stock and any Delaware corporation with securities traded on a national exchange, quoted on the NASDAQ Stock Market or owned of record by at least 2,000 shareholders. Unless an exception is available, the statute provides that for three years after the 15% threshold is exceeded, the corporation cannot have a merger, sale of substantial assets, loan, substantial issuance of stock, plan of liquidation, or reincorporation involving the interested shareholder or its affiliates. Shareholders may opt out at any time by majority vote, but the decision is not effective for one year.

There are a number of important exceptions to the basic prohibition on business combination transactions. First, the Delaware statute does not prohibit a business combination if, prior to becoming an interested shareholder, the board of directors has approved the business combination or the transaction which resulted in the shareholder passing the 15% threshold. Second, a business combination is permissible if the interested shareholder acquires 85% of the target’s outstanding voting stock (excluding shares held by management or held in employee benefit plans in which the employees do not have a confidential right to vote) in the transaction in which the 15% threshold is exceeded. Third, a business combination is permissible if approved by the board and authorized at an annual or special meeting of shareholders, and not by written consent, by the affirmative vote of two-thirds of the outstanding shares held by disinterested shareholders. Finally, if the target corporation, with the support of the majority of its continuing directors, proposes at any time another merger or sale or does not oppose another tender offer for at least 50% of its shares, the interested shareholder is released from the three year prohibition and free to compete with the target-supported transaction. In addition, note that while Delaware law permits companies to opt out of its business combination statute, our Certificate of Incorporation does not include this opt-out provision.

### **Other Information Regarding Offerings of Preferred Shares and Convertible Notes**

#### ***Dollar Value of Underlying Securities and Potential Profits on Conversion***

The following table sets forth the potential profit to be realized upon conversion by the selling stockholders of the Preferred Shares based on the conversion price on July 23, 2014 (the date the conversion price of the Preferred Shares was adjusted as a result of the issuance of the Convertible Notes) and the closing price of our common stock on July 23, 2014.

#### **Potential Profit from Conversion of the Preferred Shares at the Option of the Selling Stockholders**

Per share market price as of July 23, 2014	\$	0.13
Per share conversion price as of July 23, 2014	\$	0.13
Total shares underlying Preferred Shares based on conversion price		15,807,692
Aggregate market value of underlying shares based on per share market price as of July 23, 2014	\$	2,055,000
Aggregate conversion price of underlying shares	\$	2,055,000
Aggregate cash purchase price for the Preferred Shares	\$	0
Total premium to market price of underlying shares		0%

The following table sets forth the potential profit to be realized upon conversion by the selling stockholders of the Convertible Notes based on the conversion price on July 23, 2014 (the first closing date for the sale of Convertible Notes, and the date on which a majority of such securities were sold) and the closing price of our common stock on July 23, 2014.

#### **Potential Profit from Conversion of the Convertible Notes at the Option of the Selling Stockholders**

Per share market price as of July 23, 2014	\$	0.13
Per share conversion price as of July 23, 2014	\$	0.094
Total shares underlying Convertible Notes based on conversion price		36,047,701
Aggregate market value of underlying shares based on per share market price as of July 23, 2014	\$	4,686,201
Aggregate conversion price of underlying shares	\$	3,388,484
Aggregate cash purchase price for the Convertible Notes	\$	1,297,717
Total discount to market price of underlying shares		38%

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The following table sets forth the potential profit to be realized upon exercise of the Warrants by the selling stockholders based on the exercise price at the applicable dates of issuance as set forth below and the per share closing price of our common stock on such dates.

### Potential Profit from Exercise of Warrants

	Warrants to Preferred Investors, February 4, 2014	Warrants to Convertible Notes Investors, July 23, 2014 <sup>(1)</sup>	Additional Warrants to Preferred Investors, August 4, 2014 <sup>(2)</sup>
Per share market price as of applicable date	\$ 0.24	\$ 0.13	\$ 0.14
Per share exercise price as of applicable date	\$ 0.13	\$ 0.165	\$ 0.13
Shares underlying Warrants	1,580,768	6,007,944	4,615,385
Aggregate market value of underlying shares based on market price as of applicable date	\$379,384.32	\$781,032.72	\$646,153.90
Aggregate exercise price of underlying shares	\$205,499.84	\$991,310.76	\$600,000.05
Total discount/premium to market price of underlying shares	46%	126.9%	7.1%

(1) Certain of such Convertible Notes and accompanying warrants were purchased on July 31, 2014, August 8, 2014, August 12, 2014, September 4, 2014 and September 5, 2014; however, information in this column is presented as though all of such purchases were made on July 23, 2014.

(2) Such additional Warrants were issued to the holders of Preferred Shares on August 4, 2014, which was required because the Company's common stock was not listed on NASDAQ within 180 days of the closing of the offering of the Preferred Shares.

### Possible Payments to Selling Stockholders in Connection with the Convertible Notes

In connection with the Convertible Notes, we are or may be required to make the following payments to the selling stockholders and their affiliates:

Payee	Maximum Interest Payments <sup>(1)</sup>	Maximum Early Redemption Premiums <sup>(2)</sup>
Selling Stockholders	\$ 216,286	\$ 2,590,929

(1) Represents the maximum amount of interest payable by the Company to the selling stockholders under the Convertible Notes assuming (a) that the Convertible Notes are not converted prior to the maturity date, and (b) that no event of default thereunder occurs.

(2) Represents the cash amount that would be payable by the Company if it were required to redeem the Convertible Notes as a result of an event of default or change of control assuming (a) that the applicable premium to be applied upon the event of default or change of control is 125%, and (b) that the event of default or change of control occurs on July 23, 2014. The default interest rate is 15% per annum upon the occurrence and continuance of an event of default.

## PLAN OF DISTRIBUTION

We are registering the shares of common stock issued to the selling stockholders and issuable upon conversion of the Preferred Shares, conversion of the Convertible Notes, or exercise of the warrants to permit the resale of these shares of common stock by the holders of the shares of common stock and warrants from time to time after the date of this prospectus. We will not receive any of the proceeds from these sales by the selling stockholders. However, we will receive the proceeds of any cash exercise of the warrants, and the conversion of any notes will reduce the outstanding principal and/or interest amount of certain indebtedness. We will bear all fees and expenses incident to our obligation to register these securities.

The selling stockholders, which as used herein includes donees, pledgees, transferees or other successors-in-interest selling shares of common stock or interests in shares of common stock received after the date of this prospectus from a selling stockholder as a gift, pledge, partnership distribution or other transfer, may, from time to time, sell, transfer or otherwise dispose of any or all of their shares of common stock or interests in shares of common stock on any stock exchange, market or trading facility on which the shares are traded or in private transactions. These dispositions may be at fixed prices, at prevailing market prices at the time of sale, at prices related to the prevailing market price, at varying prices determined at the time of sale, or at negotiated prices.

The selling stockholders may use any one or more of the following methods when disposing of shares or interests therein:

- ordinary brokerage transactions and transactions in which a broker-dealer solicits purchasers;
- block trades in which a broker-dealer will attempt to sell the shares as agent, but may position and resell a portion of the block as principal to facilitate the transaction;
- purchases by a broker-dealer as principal and resale by the broker-dealer for its account;
- an exchange distribution in accordance with the rules of the applicable exchange;
- privately negotiated transactions;
- short sales effected after the date the registration statement of which this Prospectus is a part becomes effective under the Securities Act of 1933, as amended;
- through the writing or settlement of options or other hedging transactions, whether through an options exchange or otherwise;
- where broker-dealers agree with the selling stockholders to sell a specified number of such shares at a stipulated price per share;
- a combination of any such methods of sale; and
- any other method permitted by applicable law.

The selling stockholders may, from time to time, pledge or grant a security interest in some or all of the shares of common stock owned by them and, if they default in the performance of their secured obligations, the pledgees or secured parties may offer and sell the shares of common stock, from time to time, under this prospectus, or under a supplement to this prospectus filed pursuant to Rule 424 or pursuant to another applicable provision of the Securities Act amending the list of selling stockholders to include the pledgee, transferee or other successors in interest as selling stockholders under this prospectus. The selling stockholders also may transfer the shares of common stock in other circumstances, in which case the transferees, pledgees or other successors in interest will be the selling beneficial owners for purposes of this prospectus.

In connection with the sale of our common stock or interests therein, the selling stockholders may enter into hedging transactions with broker-dealers or other financial institutions, which may in turn engage in short sales of the common stock in the course of hedging the positions they assume. The selling stockholders may also sell shares of our common stock short and deliver these securities to close out their short positions, or loan or pledge the common stock to broker-dealers that in turn may sell these securities. The selling

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stockholders may also enter into option or other transactions with broker-dealers or other financial institutions or the creation of one or more derivative securities which require the delivery to such broker-dealer or other financial institution of shares offered by this prospectus, which shares such broker-dealer or other financial institution may resell pursuant to this prospectus (as supplemented or amended to reflect such transaction) or deliver to close any short positions therein.

The aggregate proceeds to the selling stockholders from the sale of the common stock offered by them will be the purchase price of the common stock less discounts or commissions, if any. Each of the selling stockholders reserves the right to accept and, together with their agents from time to time, to reject, in whole or in part, any proposed purchase of common stock to be made directly or through agents. We will not receive any of the proceeds from this offering.

The selling stockholders also may resell all or a portion of the shares in open market or other transactions in reliance upon Rule 144 under the Securities Act of 1933, provided that they meet the criteria and conform to the requirements of that rule.

To the extent required by applicable regulations, the shares of our common stock to be sold, the names of the selling stockholders, the respective purchase prices and public offering prices, the names of any agents, dealers or underwriters, and any applicable commissions or discounts with respect to a particular offer, will be set forth in an accompanying prospectus supplement or, if appropriate, a post-effective amendment to the registration statement that includes this prospectus.

In order to comply with the securities laws of some states, if applicable, the common stock may be sold in these jurisdictions only through registered or licensed brokers or dealers. In addition, in some states the common stock may not be sold unless it has been registered or qualified for sale or an exemption from registration or qualification requirements is available and is complied with.

We have advised the selling stockholders that the anti-manipulation rules of Regulation M under the Exchange Act may apply to sales of shares in the market and to the activities of the selling stockholders and their affiliates. In addition, to the extent applicable, we will make copies of this prospectus (as it may be supplemented or amended from time to time) available to the selling stockholders for the purpose of satisfying the prospectus delivery requirements of the Securities Act. The selling stockholders may indemnify any broker-dealer that participates in transactions involving the sale of the shares against certain liabilities, including liabilities arising under the Securities Act.

We have agreed to indemnify selling stockholders against liabilities, including liabilities under the Securities Act and state securities laws, relating to the registration of the shares offered by this prospectus. We have agreed with the selling stockholders to keep the registration statement of which this prospectus constitutes a part effective until the earlier of (1) such time as all of the shares covered by this prospectus and held by such persons have been disposed of pursuant to and in accordance with the registration statement or pursuant to Rule 144 or (2) the date on which all of such shares may be sold without restriction pursuant to Rule 144 of the Securities Act.

## SELLING STOCKHOLDERS

This prospectus covers the disposition by the selling stockholders identified below, or their respective transferee(s), of a total of 78,709,975 shares of our common stock. The shares included in this offering are issuable upon the conversion of the Preferred Shares, conversion of Convertible Notes, or exercise of warrants originally issued, in connection with the following offerings:

- In February 2014, the Company completed a private placement offering of Series A Convertible Preferred Stock that could be converted at a predetermined exercise price for the Company's \$.01 par value common stock. See "Description of Securities — Series A Convertible Preferred Stock" above. Relating to this private placement, the following numbers of shares of common stock are included in the this registration statement: 15,807,692 shares issuable to the investors as Preferred Conversion Shares; an estimated 423,560 shares to be issued as dividends on the Preferred Shares through December 31, 2014; and 20,423,077 shares issuable upon exercise of the warrants; for an estimated total of 36,654,329 shares.
- In July 2014 and August 2014 and September 2014, the Company completed private placement offerings of Convertible Notes including Affiliate Securities that may be converted into shares of its common stock, and warrants that are exercisable into shares of its common stock. See "Description of Securities — Convertible Notes and Warrants" above. Relating to these private placements, the following numbers of shares of common stock are included in the this registration statement: 36,047,702 shares issuable to the investors upon conversion of the Convertible Notes; 6,007,944 shares issuable to the investors upon exercise of the warrants; for an estimated total of 42,055,646 shares. This prospectus covers the resale of 100% of the number of shares of common stock issuable pursuant to the Convertible Notes as of July 23, 2014 and 100% of the number of shares of common stock issuable pursuant to the Warrants as of July 23, 2014. Certain of such Convertible Notes and accompanying Warrants were issued on July 31, 2014, August 8, 2014, August 12, 2014, September 4, 2014 and September 5, 2014; however, information included in the table below is presented as though all of such issuances were made on July 23, 2014. Because the conversion price of the Convertible Notes will be adjusted from time to time based on the prevailing market price at the time of conversion, the number of shares that actually will be issued may be more or less than the number of shares being offered by this prospectus.

\$199,125 of the outstanding principal amount of the Convertible Notes (together with any accrued and unpaid interest with respect to such portion of the principal amount), which is equal to 13.5% of the purchase price of the Convertible Notes, shall be automatically extinguished (without any cash payment by the Company) if (i) the Company has properly filed a registration statement covering the resale by the holders of the Convertible Notes of shares of our common stock issued or issuable upon conversion of the Convertible Notes with the Securities and Exchange Commission (the "SEC"), and such registration statement has been declared effective by the SEC on or prior to 120 days after the closing date of the applicable convertible note offering, and (ii) no event of default, or an event that with the passage of time or giving of notice would constitute an event of default, has occurred on or prior to such date. In addition, the number of shares of the Company's common stock issuable upon the exercise of the warrants shall be reduced by 663,750 shares of our common stock (without any cash payment by the Company), which is equal to approximately 11.0% of the number of shares of our common stock initially available for issuance upon the exercise of the warrants, if (i) the Company has properly filed a registration statement with the SEC that has been declared effective by the SEC on or prior to the earlier of (x) the 60th calendar day after the closing date of the applicable convertible note offering (or the 120th calendar day after the closing of the applicable convertible note offering in the event that such registration statement is subject to review by the SEC) and (y) the fifth trading day after the date the Company is notified by the SEC that such registration statement will not be reviewed or will not be subject to further review (such date, the "Warrant Shares Initial Effective Date") and (ii) the prospectus contained therein is available for use by the warrant holders for the resale by such warrant holders of all of the shares of common stock issued or issuable upon exercise of the warrants or otherwise pursuant to the terms of the warrants as of the Warrant Shares Initial Effective Date.

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See the description of these private placements under the section captioned “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources”.

The selling stockholders may decide to sell all, some, or none of the securities listed below. We cannot provide you with any estimate of the number of securities that the selling stockholders will hold in the future. For purposes of this table, beneficial ownership is determined in accordance with the rules of the SEC, and includes voting power and investment power with respect to such securities.

The following table sets forth the number of shares of the common stock beneficially owned by each selling shareholder as of August 5, 2014 and after giving effect to this offering assuming all of the shares covered hereby are sold by the selling stockholders. Except as indicated in the footnotes to the table, the selling stockholders have not had any material relationship with us or our affiliates during the last three years. Except as indicated below, the selling stockholders are not registered broker-dealers or affiliates of broker-dealers.

Under the terms of the Preferred Shares, Convertible Notes and the Warrants, a selling stockholder may not convert the Preferred Shares or the Convertible Notes or exercise the Warrants to the extent such conversion or exercise would cause such selling stockholder, together with its affiliates, to beneficially own a number of shares of common stock which would exceed 4.99% of the Company’s then outstanding shares of common stock following such conversion or exercise, which limit may be increased to 19.99% (in the case of the Preferred Conversion Shares and the shares issuable upon the exercise of the accompanying warrants) and 9.99% (in the case of shares issuable upon the conversion of convertible promissory notes and the exercise of the accompanying warrants) at the election of such selling stockholder. The number of shares in the second column of the table below does not reflect this limitation.

Name and Address	Securities Beneficially Owned Prior to Offering <sup>(1)</sup>	Total Shares Offered By Selling Stockholders <sup>(2)</sup>	Securities Beneficially Owned After Offering <sup>(3)</sup>	% Beneficial Ownership After Offering <sup>(3)</sup>
William Pollert <sup>(4)</sup>	1,783,666	1,783,666	0	0
Herbert Lepor <sup>(5)</sup>	767,141	624,284	142,857	0
Seymour Fein <sup>(6)</sup>	2,142,038	713,466	1,428,572	0
Jamie Zimmerman <sup>(7)</sup>	2,675,498	2,675,498	0	0
Bessemer Trust N.A., Custodian, Martin S. Engelstein <sup>(8)(9)</sup>	6,777,754	4,634,896	2,142,858	0
Jennafer Engelstein <sup>(9)(10)</sup>	178,366	178,366	0	0
Jessa Engelstein Kwon <sup>(9)(11)</sup>	445,916	445,916	0	0
Lisa Campo-Engelstein <sup>(9)(12)</sup>	89,184	89,184	0	0
Broadlawn Advisors Pension Plan, Jon Blume, Trustee <sup>(13)</sup>	1,783,666	1,783,666	0	0
Olivier Morali <sup>(14)</sup>	1,783,666	1,783,666	0	0
Alix AM PTD <sup>(15)</sup>	15,161,158	15,161,158	0	0
Olivier Cojot <sup>(16)</sup>	3,567,331	3,567,331	0	0
Anthony Heller (Helmsbridge Holdings) <sup>(17)</sup>	1,783,666	1,783,666	0	0
Richard Liroff <sup>(18)</sup>	5,972,646	5,972,646	0	0
Victor Nitti <sup>(19)</sup>	713,466	713,466	0	0
Josh Kornberg <sup>(20)</sup>	93,239,074	445,916	92,793,158	38.3%
31 Group LLC <sup>(21)</sup>	14,256,153	14,256,153	0	0
SOK Partners LLC <sup>(22)</sup>	72,435,157	2,851,228	69,583,929	31.7%
Xstelos Corp. <sup>(23)</sup>	7,128,075	7,128,075	0	0
Evan Myrianthopoulos <sup>(24)</sup>	712,808	712,808	0	0
Brio Capital Master Fund, Ltd. <sup>(25)</sup>	11,404,920	11,404,920	0	0
<b>TOTAL</b>	<b>244,801,349</b>	<b>78,709,975</b>	<b>166,091,374</b>	

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- (1) Beneficial ownership is determined in accordance with SEC rules, beneficial ownership includes any shares as to which the shareholder has sole or shared voting power or investment power, and also any shares which the stockholder has the right to acquire within 60 days of the date hereof, whether through the exercise or conversion of any stock option, convertible security, warrant or other right. The indication herein that shares are beneficially owned is not an admission on the part of the stockholder that he, she or it is a direct or indirect beneficial owner of those shares. Assumes that all the principal and interest due on the Convertible Notes are converted, all of the Preferred Shares are converted, and all of the Warrants are exercised, without regard to (i) any conversion limitations contained therein, (ii) the \$199,125 reduction in the outstanding principal amount of the Convertible Notes or (iii) the 663,750 reduction in the number of shares of the Company's common stock issuable upon the exercise of the Warrants as a result, in the case of clauses (ii) and (iii), of the satisfaction of certain of the registration rights obligations.
- (2) Includes shares issuable as Preferred Conversion Shares, shares to be issued as dividends on shares of preferred stock, shares issuable upon the conversion of convertible promissory notes, and shares issuable upon the exercise of warrants, as the case may be for each selling stockholder.
- (3) Assumes the sale of all shares offered under this prospectus by the selling stockholders.
- (4) Includes 769,231 shares issuable as Preferred Conversion Shares, 20,611 shares to be issued as dividends on shares of preferred stock and 993,824 shares issuable upon the exercise of warrants.
- (5) Includes 269,231 shares issuable as Preferred Conversion Shares, 7,214 shares to be issued as dividends on shares of preferred stock and 347,839 shares issuable upon the exercise of warrants. Includes an option previously owned to purchase 142,857 shares of common stock.
- (6) Includes 307,692 shares issuable as Preferred Conversion Shares, 8,244 shares to be issued as dividends on shares of preferred stock and 397,530 shares issuable upon the exercise of warrants. Includes 1,428,572 shares of previously owned common stock.
- (7) Includes 1,153,846 shares issuable as Preferred Conversion Shares, 30,917 shares to be issued as dividends on shares of preferred stock and 1,490,735 shares issuable upon the exercise of warrants.
- (8) Includes 3,213,143 shares issuable as Preferred Conversion Shares, 20,611 shares to be issued as dividends on shares of preferred stock and 1,401,142 shares issuable upon the exercise of warrants.
- (9) Martin S. Engelstein is the father of Jennafer Engelstein, Jessa Engelstein Kwon and Lisa Campo Engelstein. Each of these persons disclaims beneficial ownership of the shares held by the others.
- (10) Includes 76,923 shares issuable as Preferred Conversion Shares, 2,061 shares to be issued as dividends on shares of preferred stock and 99,382 shares issuable upon the exercise of warrants.
- (11) Includes 192,308 shares issuable as Preferred Conversion Shares, 5,153 shares to be issued as dividends on shares of preferred stock and 248,455 shares issuable upon the exercise of warrants.
- (12) Includes 38,462 shares issuable as Preferred Conversion Shares, 1,031 shares to be issued as dividends on shares of preferred stock and 49,691 shares issuable upon the exercise of warrants.
- (13) Includes 769,231 shares issuable as Preferred Conversion Shares, 20,611 shares to be issued as dividends on shares of preferred stock and 993,824 shares issuable upon the exercise of warrants.
- (14) Includes 769,231 shares issuable as Preferred Conversion Shares, 20,611 shares to be issued as dividends on shares of preferred stock and 993,824 shares issuable upon the exercise of warrants.
- (15) Includes 6,538,462 shares issuable as Preferred Conversion Shares, 175,195 shares to be issued as dividends on shares of preferred stock and 8,447,501 shares issuable upon the exercise of warrants.
- (16) Includes 1,538,462 shares issuable as Preferred Conversion Shares, 41,222 shares to be issued as dividends on shares of preferred stock and 1,987,647 shares issuable upon the exercise of warrants.
- (17) Includes 769,231 shares issuable as Preferred Conversion Shares, 20,611 shares to be issued as dividends on shares of preferred stock and 993,824 shares issuable upon the exercise of warrants.
- (18) Includes 1,346,154 shares issuable as Preferred Conversion Shares, 36,070 shares to be issued as dividends on shares of preferred stock 2,146,510 shares issuable upon the exercise of warrants, and 2,443,912 shares issuable upon conversion of convertible promissory notes.
- (19) Includes 307,692 shares issuable as Preferred Conversion Shares, 8,244 shares to be issued as dividends on shares of preferred stock and 397,530 shares issuable upon the exercise of warrants.
- (20) Includes 302,308 shares held directly, options to purchase 22,906,921 shares of common stock that may



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be exercised within the next 60 days, 69,583,929 shares owned directly by SOK Partners, LLC (“SOK”), and 445,916 shares of common stock being offered, which are issued or issuable upon conversion of preferred stock purchased by Mr. Kornberg, exercise of the accompanying warrants and dividends paid or payable upon such preferred stock in the form of common stock. Mr. Kornberg and Dr. Samuel Herschkowitz are the managing partners of SOK. Mr. Kornberg is the Company’s Chief Executive Officer and Chairman of the Board.

- (21) Includes 12,219,560 shares issuable upon the conversion of convertible promissory notes and 2,036,593 shares issuable upon the exercise of warrants. The business address of 31 Group LLC (“31 Group”) is c/o Magna Management, 5 Hanover Square, New York, New York 10004. Mr. Joshua Sason is a member and the controlling person of 31 Group, with sole voting control and investment discretion over securities held by 31 Group, and may be deemed to share beneficial ownership of any securities beneficially owned by 31 Group. Mr. Sason disclaims beneficial ownership of these securities. We have been advised that neither 31 Group nor Mr. Sason is a member of the Financial Industry Regulatory Authority, or FINRA, or an independent broker-dealer. However, one of the other members of 31 Group is affiliated with Aegis Capital Corp. and one or more registered broker-dealers, none of whom are currently expected to participate in the sale of the securities offered hereby. The securities being registered hereunder are issuable (or were issued) upon conversion or exercise, as applicable, of notes and warrants purchased by 31 Group in the ordinary course of business, and at the time of purchase neither 31 Group nor any of its members or affiliates had any agreements or understandings, directly or indirectly, with any other person to distribute such notes or warrants or any of the securities being registered hereunder.
- (22) Includes 69,583,929 shares owned directly, 2,443,912 shares issuable upon the conversion of convertible promissory notes and 407,316 shares issuable upon the exercise of warrants. Mr. Kornberg and Dr. Samuel Herschkowitz are the managing partners of SOK Partners, LLC. Mr. Kornberg is the Company’s Chief Executive Officer and Chairman of the Board.
- (23) Includes 6,109,780 shares issuable upon the conversion of convertible promissory notes and 1,018,295 shares issuable upon the exercise of warrants.
- (24) Includes 610,978 shares issuable upon the conversion of convertible promissory notes and 101,830 shares issuable upon the exercise of warrants. Mr. Myrianthopoulos is a managing director of Aegis Capital to which 31 Group, LLC is affiliated.
- (25) Includes 9,775,648 shares issuable upon the conversion of convertible promissory notes and 1,629,272 shares issuable upon the exercise of warrants.

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### **LEGAL MATTERS**

Maslon Edelman Borman & Brand, LLP has rendered an opinion regarding the legality of the issuance of the shares of common stock being registered in this prospectus.

### **EXPERTS**

Our financial statements for the fiscal years ended December 31, 2013 and December 31, 2012, included herein, were audited by our independent auditors, Olsen Thielen & Co., Ltd., certified public accountants registered with the Public Company Accounting Oversight Board.

We have included our financial statements by reference in this prospectus in reliance on the reports of the above-named independent auditors, given upon their authority as experts in accounting and auditing.

### **WHERE YOU CAN FIND MORE INFORMATION**

We are subject to the reporting requirements of the Exchange Act. Reports filed with the SEC pursuant to the Exchange Act, including proxy statements, annual and quarterly reports, and other reports filed by the Company can be inspected and copied at the public reference facilities maintained by the SEC at the Headquarters Office, 100 F. Street N.E., Room 1580, Washington, D.C. 20549. The reader may obtain information on the operation of the public reference room by calling the SEC at 1-800-SEC-0330. The reader can request copies of these documents upon payment of a duplicating fee by writing to the SEC. Our filings are also available on the SEC's internet site at <http://www.sec.gov>, and the Company's website at [www.skylinemedical.com](http://www.skylinemedical.com).

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**Skyline Medical Inc.**

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors  
Skyline Medical, Inc.  
Eagan, MN

We have audited the accompanying balance sheets of Skyline Medical, Inc. (a development stage company) as of December 31, 2013 and 2012 and the related statements of operations, stockholders' deficit and cash flows for the years then ended and for the period from April 23, 2002 (inception), to December 31, 2013. Skyline Medical, Inc.'s management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Skyline Medical, Inc. (a development stage company) as of December 31, 2013 and 2012, and the results of its operations and its cash flows for the years then ended and from April 23, 2002 (inception) to December 31, 2013, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the company will continue as a going concern. As discussed in Note 1 to the financial statements, the company has incurred losses since inception, has an accumulated deficit and has not received significant revenue from sales of products and services. These factors raise substantial doubt about its ability to continue as a going concern. Management's plan in regard to these matters is also described in Note 1. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Olsen Thielen & Co., Ltd.

St. Paul, Minnesota  
March 27, 2014

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PART 1. FINANCIAL INFORMATION  
Item 1. Financial Statements

**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**BALANCE SHEETS**

	December 31, 2013	December 31, 2012
<b>ASSETS</b>		
Current Assets:		
Cash	\$ 101,953	\$ 13,139
Accounts receivable, net of Allowance for Doubtful Accounts of \$0 and \$4,073 in 2013 and 2012	97,245	39,711
Inventories	122,175	145,209
Prepaid expense and other assets	60,588	27,409
Total Current Assets	<u>381,961</u>	<u>225,468</u>
Fixed assets, net	158,110	3,521
Intangibles, net	53,355	140,588
Total Assets	<u>\$ 593,426</u>	<u>\$ 369,577</u>
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>		
Current Liabilities:		
Current portion of convertible debt, net of discounts of \$0 and \$21,138 (See Note 6)	\$ —	\$ 1,081,187
Accounts payable	1,062,108	733,595
Accrued expenses	2,057,957	1,599,519
Short-term note payable (See Note 9)	280,000	—
Deferred Revenue	69,000	—
Total Current Liabilities	<u>3,469,065</u>	<u>3,414,301</u>
Long-term debt and convertible debt, net of discounts of \$0 and \$0 (See Note 6)	—	89,300
Accrued Expenses	331,216	—
Liability for equity-linked financial instruments (See Note 8)	11,599	169,179
Total Liabilities	<u>3,811,880</u>	<u>3,672,780</u>
Commitments and Contingencies	—	—
Stockholders' Deficit:		
Common stock, \$.01 par value, 800,000,000 authorized, 219,937,619 and 104,247,228 outstanding	2,199,376	1,042,473
Additional paid-in capital	23,279,585	14,945,435
Deficit accumulated during development stage	<u>(28,697,415)</u>	<u>(19,291,111)</u>
Total Stockholders' Deficit	<u>(3,218,454)</u>	<u>(3,303,203)</u>
Total Liabilities and Stockholders' Deficit	<u>\$ 593,426</u>	<u>\$ 369,577</u>

See Notes to Financial Statements.

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF OPERATIONS**

	<u>Year Ended December 31,</u>		<u>Period From</u>
	<u>2013</u>	<u>2012</u>	<u>April 23, 2002</u>
			<u>(Inception) To</u>
			<u>December 31,</u>
			<u>2013</u>
Revenue	\$ 468,125	\$ 188,772	\$ 769,559
Cost of goods sold	<u>189,707</u>	<u>128,540</u>	<u>381,467</u>
Gross margin	278,418	60,232	388,092
General and administrative expense	7,530,037	6,285,905	23,280,400
Operations expense	1,096,969	761,047	3,387,550
Sales and marketing expense	578,793	172,970	1,640,248
Interest expense	636,503	259,349	1,562,959
Loss (gain) on valuation of equity-linked financial instruments	<u>(157,580)</u>	<u>3,116</u>	<u>(785,650)</u>
Total expense	<u>9,684,722</u>	<u>7,482,387</u>	<u>29,085,507</u>
Net loss available to common shareholders	\$ <u>(9,406,304)</u>	\$ <u>(7,422,155)</u>	\$ <u>(28,697,415)</u>
Loss per common share – basic and diluted	\$ <u>(0.06)</u>	\$ <u>(0.11)</u>	\$ <u>(1.51)</u>
Weighted average shares used in computation – basic and diluted	<u>151,958,618</u>	<u>69,587,814</u>	<u>18,952,512</u>

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM APRIL 23, 2002 (INCEPTION)**  
**To December 31, 2013**

	Shares	Amount	Paid-in Capital	Deficit	Total
Issuance of common stock 9/1/02, \$.0167 <sup>(1)</sup>	598,549	\$ 5,985	\$ 4,015	\$ —	\$ 10,000
Issuance of common 10/23/02, \$1.67/share	2,993	30	4,970		5,000
Net loss				(51,057)	(51,057)
Balance 12/31/02	601,542	\$ 6,015	\$ 8,985	\$ (51,057)	\$ (36,057)
Issuance of common 2/12/03, \$.0167 <sup>(2)</sup>	23,942	239	161		400
Issuance of common 6/11/03	21,548	216	34,784		35,000
Net loss				(90,461)	(90,461)
Balance 12/31/03	647,032	\$ 6,470	\$ 43,930	\$ (141,518)	\$ (91,118)
Issuance of common 5/25/04, \$.0167 <sup>(4)</sup>	6,567	66	44		110
Net loss				(90,353)	(90,353)
Balance 12/31/04	653,599	\$ 6,536	\$ 43,974	\$ (231,871)	\$ (181,361)
Issuance of common 12/14/05, \$.0167 <sup>(5)</sup>	14,964	150	100		250
Vested stock options and warrants			2,793		2,793
Net loss				(123,852)	(123,852)
Balance 12/31/05	668,563	\$ 6,686	\$ 46,867	\$ (355,723)	\$ (302,170)
Issuance of common 5/16 & 8/8, \$.0167 <sup>(6)</sup>	86,869	869	582		1,451
Issuance of common 10/19 & 23, \$.0167 <sup>(7)</sup>	38,906	389	261		650
Issuance of common 12/01, \$1.67 <sup>(8)</sup>	28,739	287	44,523		44,810
Vested stock options and warrants			13,644		13,644
Net loss				(273,026)	(273,026)
Balance 12/31/06	823,077	\$ 8,231	\$ 105,877	\$ (628,749)	\$ (514,641)
Issuance of common 1/30/07 @ \$1.67 <sup>(9)</sup>	599	6	994		1,000
Value of equity instruments issued with debt			132,938		132,938
Capital contributions resulting from waivers of debt			346,714		346,714
Vested stock options and warrants			73,907		73,907
Net loss				(752,415)	(752,415)
Balance 12/31/07	823,676	\$ 8,237	\$ 660,430	\$ (1,381,164)	\$ (712,497)
Issuance of common 6/11 to 9/30, \$.35 <sup>(10)</sup>	4,552,862	45,528	1,547,974		1,593,502
Shares issued to finders, agents	2,012,690	20,127	(20,127)		—
Shares issued to pay direct legal fees	285,714	2,857	(2,857)		—
Issuance of common due to anti-dilution provisions	205,899	2,059	(2,059)		—
Shares issued to pay investor relations services 6/23/08, \$.35	250,000	2,500	85,000		87,500
Vested stock options and warrants			354,994		354,994
Capital contributions resulting from waivers of debt			129,684		129,684
Net loss				(1,762,628)	(1,762,628)
Balance 12/31/08	8,130,841	\$ 81,308	\$ 2,753,039	\$ (3,143,792)	\$ (309,445)
Cumulative effect of adoption of EITF 07-5			(486,564)	6,654	(479,910)
Vested stock options and warrants			111,835		111,835
Shares issued 3/20/09 to pay for fund raising	125,000	1,250	(1,250)		—
Shares issued under PMM in 2009, \$.50	2,147,810	21,478	1,052,427		1,073,905
Capital contributions resulting from waivers of debt			84,600		84,600

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM APRIL 23, 2002 (INCEPTION)**  
**To December 31, 2013 – (continued)**

	Shares	Amount	Paid-in Capital	Deficit	Total
Value of equity-linked financial instruments issued in connection with PPMs			(222,296)		(222,296)
Value of equity instruments issued with debt			30,150		30,150
Shares issued to consultant for fund raising	30,000	300	(300)		—
Shares issued upon conversion of debt and interest, \$.27	935,446	9,354	247,100		256,454
Shares issued upon conversion of shareholder note, \$.35	14,024	140	4,766		4,906
Net loss				(2,892,230)	(2,892,230)
Balance 12/31/09	11,383,121	\$ 113,830	\$ 3,573,507	\$ (6,029,368)	\$ (2,342,030)
Shares issued in 2010 under PPM, \$.50	354,550	3,546	173,729		177,275
Shares issued to consultants for IR and consulting, \$.50	374,090	3,741	183,304		187,045
Value of equity instruments issued for consulting services			354,602		354,602
Vested stock options and warrants			11,382		11,382
Value of equity-linked financial instruments issued in connection with PPM in first quarter			(25,553)		(25,553)
Shares issued in May 2010 to consultant, \$.50	12,850	129	6,296		6,425
Shares issued in May 2010 to 2008 investors as a penalty for late registration, \$.50	710,248	7,102	348,022		355,124
Value of equity instruments issued with debt			119,474		119,474
Value of equity-linked financial instruments issued in connection with PPM in second quarter			(31,332)		(31,332)
Value of equity-linked financial instruments issued in connection with PPM in third quarter			(31,506)		(31,506)
Shares issued in September 2010 under PPM, \$.10	250,000	2,500	22,500		25,000
Shares issued to consultants in third quarter at \$.22 per share	488,860	4,889	102,660		107,549
Shares issued in November 2010 upon exercise of warrants at \$.135 per share	128,571	1,286	16,071		17,357
Shares issued in November 2010 to directors as compensation at \$.15 per share	300,000	3,000	42,000		45,000
Vested stock options in fourth quarter			161,107		161,107
Equity instruments issued to consultants in fourth quarter			26,234		26,234
Net loss				(1,352,709)	(1,352,709)
Balance 12/31/2010	14,002,290	\$ 140,023	\$ 5,052,497	\$ (7,382,077)	\$ (2,189,557)
Value of equity instruments issued with debt in first quarter			47,908		47,908
Shares issued at \$.075 per share under PPM	5,333,334	53,334	346,666		400,000
Shares issued at \$.085 per share under PPM	1,882,353	18,823	141,177		160,000
Shares issued at \$.09 per share under PPM	200,000	2,000	16,000		18,000
Shares issued at \$.10 per share under PPM	150,000	1,500	13,500		15,000

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM APRIL 23, 2002 (INCEPTION)**  
**To December 31, 2013 – (continued)**

	Shares	Amount	Paid-in Capital	Deficit	Total
Vested stock options and warrants in first quarter			1,937,638		1,937,638
Equity instruments issued to consultants in first quarter			91,504		91,504
Stock issued upon conversion of debt in first quarter	416,010	4,160	15,840		20,000
Stock issued to pay interest on debt	158,036	1,580	20,920		22,500
Shares issued at \$.07 per share under PPM	1,071,429	10,715	64,285		75,000
Stock issued upon conversion of debt and interest	941,034	9,410	22,590		32,000
Equity instruments issued to consultants			12,256		12,256
Equity instruments issued to consultants			147,116		147,116
Restricted stock issued to consultants	822,842	8,228	46,772		55,000
Shares issued at \$.06 per share under PPM	3,500,000	35,000	175,000		210,000
Shares issued at \$.20 per share under PPM	1,375,000	13,750	261,250		275,000
Shares issued upon exercise of stock options at \$.01	100,000	1,000			1,000
Shares issued at \$.35 per share IR compensation	575,000	5,750	195,500		201,250
Equity instruments upon conversion of Accounts Payable			20,000		20,000
Shares issued to private investor at \$.15 per share	1,546,667	15,467	216,533		232,000
Net loss				(4,486,879)	(4,486,879)
Balance 12/31/2011	32,074,000	\$ 320,740	\$ 8,844,952	\$(11,868,956)	\$ (2,703,264)
Shares issued to institutional investor upon conversion of Note Payable at \$.1342 per share	59,613	596	7,404		8,000
Shares issued to institutional investor upon conversion of Note Payable at \$.13 per share	107,692	1,077	12,923		14,000
Shares issued to institutional investor upon conversion of Note Payable at \$.088 per share	170,455	1,705	13,295		15,000
Shares issued to institutional investor upon conversion of Note Payable at \$.0446 per share	343,348	3,433	12,567		16,000
Shares issued to institutional investor upon conversion of Note Payable at \$.0446 per share	269,058	2,690	9,310		12,000
Shares issued to institutional investor upon conversion of Note Payable at \$.0446 per share	268,670	2,687	7,313		10,000
Shares issued to institutional investor upon conversion of Note Payable at \$.0397 per share	428,212	4,282	4,218		8,500
Shares issued to a private investor at \$.065 per share	9,230,770	92,308	507,692		600,000
Shares issued for consulting to the then interim CEO at \$.065 per share	300,000	3,000	16,500		19,500
Vested stock options and warrants			830,372		830,372

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM APRIL 23, 2002 (INCEPTION)**  
**To December 31, 2013 – (continued)**

	Shares	Amount	Paid-in Capital	Deficit	Total
Shares issued to an institutional investor upon conversion of Note Payable at \$.0286 per share	349,650	3,497	6,503		10,000
Shares issued to a private investor per a convertible note default at \$.15 per share	7,500,000	75,000	1,050,000		1,125,000
Shares issued to a private investor at \$.15 per share	263,333	2,633	36,867		39,500
Shares issued upon exercise of options at \$.01 per share	412,963	4,130			4,130
Stock issued upon conversion of debt at \$.15 per share	3,292,557	32,926	460,958		493,884
Stock issued upon conversion of debt at \$.065 per share	2,850,754	28,508	156,791		185,299
Shares issued to private investor upon conversion of Note Payable at \$.18 per share	316,898	3,169	53,873		57,042
Shares issued to private investor upon conversion of Note Payable at \$.052 per share	1,147,078	11,471	48,063		59,534
Shares issued to private investor upon conversion of Note Payable at \$.10 per share	565,834	5,658	50,926		56,584
Shares issued to a private investor upon conversion of Note Payable at \$.032 per share	1,572,327	15,723	34,277		50,000
Shares issued to an institutional investor upon conversion of Note Payable at \$.031 per share	387,097	3,871	8,129		12,000
Stock issued upon conversion of debt at \$.15 per share	397,267	3,973	55,617		59,590
Shares issued to a Director as compensation at \$.09 per share	277,778	2,778	22,222		25,000
Shares issued under PPM at \$.07 per share	9,870,666	98,707	592,239		690,946
Shares issued to institutional investor upon conversion of Note Payable at \$.0353 per share	509,915	5,099	12,901		18,000
Shares issued to a private investor upon conversion of Note Payable at \$.032 per share	283,718	2,837	6,185		9,022
Shares issued to an institutional investor upon conversion of Note Payable at \$.0297 per share including \$11,021 of interest.	740,741	7,407	25,614		33,021
Shares issued at \$.15 per share as Investor Relations compensation	625,000	6,250	87,500		93,750
Shares issued as settlement to remove anti-dilution agreement at \$.065 per share	26,500,000	265,000	1,457,500		1,722,500
Shares issued in settlement with former COO at \$.15 per share less shares cancelled at \$.09 per share	803,701	8,037	134,296		142,333
Equity value for options and warrants			150,189		150,189
Shares issued at \$.07 per share as Investor Relations compensation	300,000	3,000	18,000		21,000
Shares issued at \$.15 per share as conversion of debt	157,088	1,571	21,992		23,563

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM APRIL 23, 2002 (INCEPTION)**  
**To December 31, 2013 – (continued)**

	Shares	Amount	Paid-in Capital	Deficit	Total
Shares issued to a private investor exercising options at \$.01 per share	71,826	718			718
Shares issued to debtors as compensation at \$.10 per share	1,563,031	15,630	140,613		156,243
Value of equity instruments issued with debt			33,469		33,469
Shares issued upon conversion of Note Payable at \$.07 per share	236,092	2,361	14,165		16,526
Share true-up to certified shareholders list per the stock transfer agency	100	1			1
Net loss				(7,422,155)	(7,422,155)
Balance at 12/31/2012	104,247,228	\$ 1,042,473	\$ 14,945,435	\$(19,291,111)	\$ (3,303,203)
Shares issued to debtors as compensation at \$.15 per share	290,143	2,901	40,620		43,521
Shares issued under PPM to five investors at \$.07 per share	7,142,857	71,429	428,571		500,000
Shares issued to an escrow account underlying a debt agreement <sup>(11)</sup>	1,000,000	10,000			10,000
Shares issued to debtors as compensation at \$.15 per share	230,332	2,303	32,247		34,550
Shares issued to an institutional investor at \$.07 per share	7,142,858	71,429	428,571		500,000
Value of shares per an agreement with a former officer <sup>(12)</sup>			40,480		40,480
Shares issued to consultant as compensation at \$.067 per share	250,000	2,500	14,250		16,750
Value of Equity instruments issued with debt			392,556		392,556
Shares issued to former consultant exercising options at \$.01 per share	200,000	2,000			2,000
Shares issued to former CEO exercising options at \$.01 per share.	333,330	3,333			3,333
Shares issued upon conversion of four notes payable at \$.15 per share	1,041,622	10,416	145,827		156,243
Shares issued for interest to the four notes payable at \$.15 per share	74,462	745	10,425		11,170
Shares issued for cashless exercise of warrants at \$.12 per share	277,778	2,778			2,778
Shares issued for cashless exercise of warrants at \$.16 per share	163,334	1,633			1,633
Shares issued for cashless exercise of warrants at \$.15 per share	632,708	6,327			6,327
Shares issued for cashless exercise of warrants at \$.20 per share	261,848	2,618			2,618
Shares issued to 24 warrant holders exercised at a reduced price for \$.10 per share	10,444,898	104,449	940,041		1,044,490
Shares issued to 4 PPM investors converting notes at \$.12 per share	2,637,534	26,375	290,129		316,504
Shares issued to 10 PPM investors converting notes at \$.18 per share	5,405,431	54,054	966,146		1,020,200
Shares issued to consultant as compensation at \$.38 per share	150,000	1,500	55,500		57,000
Shares issued for two note conversions at \$.014 per share	71,066,331	710,663	284,265		994,928

See Notes to Financial Statements.

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM APRIL 23, 2002 (INCEPTION)**  
**To December 31, 2013 – (continued)**

	Shares	Amount	Paid-in Capital	Deficit	Total
Shares issued for warrant exercise at \$.15 per share	1,071,429	10,715	150,000		160,715
Shares issued for a cashless exercise of warrants at \$.10 per share	3,024,390	30,244			30,244
Shares issued to an investor for a cashless exercise of warrants at \$.17 per share	204,306	2,044			2,044
Shares issued for a cashless exercise of warrants at \$.075 per share	544,714	5,447			5,447
Shares issued to former Board Directors as compensation at \$.325 per share	100,000	1,000	99,000		100,000
Reduced warrant exercise compensation expense			2,140,946		2,140,946
Options issued as part of employee bonus			147,500		147,500
Shares issued to one investor for cashless warrant exercised at \$.12 per share	277,778	2,778			2,778
Shares issued for cashless warrant exercise at \$.13 per share	159,722	1,597			1,597
Shares issued for interest on two note conversions at \$.18 per share	40,918	409	6,956		7,365
Shares issued in settlement with a former noteholder at \$.27 per share	378,000	3,780	98,280		102,060
Shares issued for a stock option exercise at \$.065 per share	10,000	100	550		650
Shares issued to one warrant holder executed at a reduced price of \$.125 per share	1,000,000	10,000	115,000		125,000
Shares issued for option exercise at \$.07 per share	17,000	170	1,020		1,190
Shares issued for cashless warrant exercise at \$.075 per share	116,667	1,167			1,167
Vesting expense			1,505,270		1,505,270
Net loss				(9,406,304)	(9,406,304)
Balance at 12/31/13	<u>219,937,619</u>	<u>\$ 2,199,376</u>	<u>\$ 23,279,585</u>	<u>\$(28,697,415)</u>	<u>\$ (3,218,454)</u>

- (1) Founders shares, 1,000,000 pre-split.
- (2) 23,492 (40,000 pre-split) shares valued at \$.0167 per share as compensation for loan guarantees by management.
- (3) Investment including 670 shares issued as a 10% finder's fee.
- (4) For payment of patent legal fees.
- (5) Compensation for loan guarantees by management.
- (6) For vendor contractual consideration.
- (7) Employment agreements.
- (8) Investment.
- (9) Conversion of convertible notes by management.
- (10) Investment, "October 2008 financing".
- (11) The shares reduce by 1/3 yearly and are returned to the Company as the debt is paid.
- (12) The Company purchased shares previously issued to a former officer equal to the cost of withholding taxes advanced by the Company. The value here represents the net pay from the transaction that was retained by the Company.

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENTS OF CASH FLOWS**

	<u>Year Ended December 31,</u>		<u>April 23, 2002</u>
	<u>2013</u>	<u>2012</u>	<u>(Inception) To</u> <u>December 31,</u> <u>2013</u>
Cash flow from operating activities:			
Net loss	(9,406,304)	(7,422,155)	(28,697,415)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	148,761	1,079	159,405
Vested stock options and warrants	3,700,070	830,372	7,197,742
Equity instruments issued for management and consulting	239,290	3,919,828	6,029,058
Stock-based registration payments	—	—	355,124
Capital contributions resulting from waivers of debt	—	—	476,398
Amortization of debt discount	413,695	57,518	756,497
(Gain) loss on valuation of equity-linked instruments	(157,580)	3,116	(785,650)
Changes in assets and liabilities:			
Accounts receivable	(57,534)	10,583	(97,245)
Inventories	23,034	(47,604)	(122,175)
Prepaid expense and other assets	(33,179)	2,739	(60,588)
Notes payable to shareholders	—	—	(14,957)
Accounts payable	429,033	421,104	2,147,872
Accrued expenses	776,548	1,039,255	2,494,237
Deferred revenue	69,000	—	69,000
Net cash used in operating activities:	<u>(3,855,166)</u>	<u>(1,184,165)</u>	<u>(10,092,697)</u>
Cash flow from investing activities:			
Purchase of fixed assets	(162,761)	—	(175,019)
Purchase of intangibles	(53,355)	—	(195,850)
Net cash used in investing activities:	<u>(216,116)</u>	<u>—</u>	<u>(370,869)</u>
Cash flow from financing activities:			
Proceeds from long-term and convertible debt	1,822,718	528,525	3,935,209
Repayment of convertible debt	—	(150,000)	(250,000)
Principal payments on long-term debt	—	—	(75,667)
Issuance of common stock	2,337,378	695,794	6,955,977
Net cash provided by (used in) financing activities:	<u>4,160,096</u>	<u>1,074,319</u>	<u>10,565,519</u>
Net increase (decrease) in cash	88,814	(109,846)	101,953
Cash at beginning of period	13,139	122,985	—
Cash at end of period	<u>101,953</u>	<u>13,139</u>	<u>101,953</u>
Non cash transactions:			
Conversion of debt to accrued liabilities	415,775	100,000	515,775
Common stock issued for accrued interest/bonus	402,669	106,310	620,839
Conversion of accounts payable to convertible debt	—	—	546,600
Common stock issued to satisfy debt	2,318,568	817,800	3,538,935
Stock/warrant issued to satisfy accounts payable/Liabilities	<u>100,521</u>	<u>418,644</u>	<u>539,165</u>

See Notes to Financial Statements.

**SKYLINE MEDICAL, INC.  
(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations and Continuance of Operations**

Skyline Medical, Inc. (the “Company”) was incorporated under the laws of the State of Minnesota in 2002. Effective August 6, 2013, the Company changed its name to Skyline Medical Inc. Pursuant to an Agreement and Plan of Merger dated effective December 16, 2013, the Company merged with and into a Delaware corporation with the same name that was its wholly-owned subsidiary, with such Delaware Corporation as the surviving corporation of the merger. The Company has developed an environmentally safe system for the collection and disposal of infectious fluids that result from surgical procedures and post-operative care. The Company also makes ongoing sales of our proprietary cleaning fluid and filters to users of our systems. In April 2009, the Company received 510(k) clearance from the FDA to authorize the Company to market and sell its STREAMWAY FMS products.

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. The Company has suffered recurring losses from operations and has a stockholders’ deficit. These factors raise substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Since inception to December 31, 2013, the Company raised approximately \$6,956,000 in equity and \$3,935,000 in debt financing, including \$2,337,000 in equity and \$1,823,000 in convertible debt in 2013. In 2014, the Company has completed a private offering of units of preferred stock and warrants. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources”.

**Recent Accounting Developments**

We reviewed all significant newly issued accounting pronouncements and determined they are either not applicable to our business or that no material effect is expected on our financial position and results of our operations.

**Valuation of Intangible Assets**

We review identifiable intangible assets for impairment in accordance with ASC 350 — *Intangibles — Goodwill and Other*, whenever events or changes in circumstances indicate the carrying amount may not be recoverable. Our intangible assets are currently solely the costs of obtaining trademarks and patents. Events or changes in circumstances that indicate the carrying amount may not be recoverable include, but are not limited to, a significant change in the medical device marketplace and a significant adverse change in the business climate in which we operate. If such events or changes in circumstances are present, the undiscounted cash flows method is used to determine whether the intangible asset is impaired. Cash flows would include the estimated terminal value of the asset and exclude any interest charges. If the carrying value of the asset exceeds the undiscounted cash flows over the estimated remaining life of the asset, the asset is considered impaired, and the impairment is measured by reducing the carrying value of the asset to its fair value using the discounted cash flows method. The discount rate utilized is based on management's best estimate of the related risks and return at the time the impairment assessment is made.

Our accounting estimates and assumptions bear various risks of change, including the length of the current economic downturn facing the United States, the expansion of the slowdown in consumer spending in the U.S. medical markets despite the early expressed opinions of financial experts that the medical market would not be as affected as other markets and failure to gain acceptance in the medical market.

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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

**Accounting Policies and Estimates**

The presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Presentation of Taxes Collected from Customers**

Sales taxes are imposed on the Company's sales to nonexempt customers. The Company collects the taxes from customers and remits the entire amounts to the governmental authorities. The Company's accounting policy is to exclude the taxes collected and remitted from revenues and expenses.

**Shipping and Handling**

Shipping and handling charges billed to customers are recorded as revenue. Shipping and handling costs are recorded within cost of goods sold on the statement of operations.

**Advertising**

Advertising costs are expensed as incurred. There were no advertising expenses for 2013 and 2012.

**Research and Development**

Research and development costs are charged to operations as incurred. Research and development costs were approximately \$235,000 and \$15,000 for 2013 and 2012, respectively.

**Revenue Recognition**

The Company recognizes revenue in accordance with the SEC's Staff Accounting Bulletin Topic 13 Revenue Recognition and ASC 605 — Revenue Recognition.

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable and collectability is probable. Delivery is considered to have occurred upon either shipment of the product or arrival at its destination based on the shipping terms of the transaction. The Company's standard terms specify that shipment is FOB Skyline and the Company will, therefore, recognize revenue upon shipment in most cases. This revenue recognition policy applies to shipments of the STREAMWAY FMS units as well as shipments of cleaning solution and filters. When these conditions are satisfied, the Company recognizes gross product revenue, which is the price it charges generally to its customers for a particular product. Under the Company's standard terms and conditions, there is no provision for installation or acceptance of the product to take place prior to the obligation of the customer. The customer's right of return is limited only to the Company's standard one-year warranty whereby the Company replaces or repairs, at its option, and it would be rare that the STREAMWAY FMS unit or significant quantities of cleaning solution and filters may be returned. Additionally, since the Company buys the STREAMWAY FMS units, cleaning solution and filters from "turnkey" suppliers, the Company would have the right to replacements from the suppliers if this situation should occur.

**Receivables**

Receivables are reported at the amount the Company expects to collect on balances outstanding. The Company provides for probable uncollectible amounts through charges to earnings and credits to the valuation based on management's assessment of the current status of individual accounts, changes to the valuation allowance have not been material to the financial statements.



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**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

**Inventories**

Inventories are stated at the lower of cost or market, with cost determined on a first-in, first-out basis. Inventory balances are as follows:

	December 31, 2013	December 31, 2012
Finished goods	\$ 56,818	\$ 91,008
Raw materials	18,603	39,543
Work-In-Process	46,754	14,658
Total	<u>\$ 122,175</u>	<u>\$ 145,209</u>

**Property and Equipment**

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation of property and equipment is computed using the straight-line method over the estimated useful lives of the respective assets. Estimated useful asset life by classification is as follows:

	Years
Computers and office equipment	3 – 7
Leasehold improvements	5
Manufacturing Tooling	3 – 7

The Company's investment in Fixed Assets consists of the following:

	December 31, 2013	December 31, 2012
Computers and office equipment	\$ 61,505	\$ 12,258
Leasehold Improvements	23,614	
Manufacturing Tooling	89,900	
Total	175,019	12,258
Less: Accumulated Depreciation	16,909	8,737
Total Fixed Assets, Net	<u>\$ 158,110</u>	<u>\$ 3,521</u>

Upon retirement or sale, the cost and related accumulated depreciation are removed from the balance sheet and the resulting gain or loss is reflected in operations. Maintenance and repairs are charged to operations as incurred.

**Intangible Assets**

Intangible assets consist of trademarks and patent costs. These assets are not subject to amortization until the property patented is in production. The assets are reviewed for impairment annually, and impairment losses, if any, are charged to operations when identified. The Company wrote-off the entire original STREAMWAY System patent of \$140,588 in 2013.

**Income Taxes**

The Company accounts for income taxes in accordance with ASC 740 — *Income Taxes* ("ASC 740"). Under ASC 740, deferred tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities and net operating loss and credit carryforwards using enacted tax rates in effect for the year in which the differences are expected to impact taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

The Company reviews income tax positions expected to be taken in income tax returns to determine if there are any income tax uncertainties. The Company recognizes tax benefits from uncertain tax positions only if it is more likely than not that the tax positions will be sustained on examination by taxing authorities, based on technical merits of the positions. The Company has identified no income tax uncertainties.

Tax years subsequent to 2010 remain open to examination by federal and state tax authorities.

**Patents and Intellectual Property**

On January 25<sup>th</sup>, 2014 the Company filed a non-provisional PCT Application No. PCT/US2014/013081 claiming priority from the U.S. Provisional Patent Application, number 61756763 which was filed one year earlier on January 25<sup>th</sup>, 2013. The PCT makes it possible to seek patent protection for an invention simultaneously in each of 148 countries, including the United States, by filing this “international” patent application instead of filing several separate national or regional patent applications.

Our PCT patent application is for the new model of the surgical fluid waste management system that has embodiments, based on our patent attorney’s recommendations, that are patentable over all prior art and will not infringe on any existing patents. This PCT Application adds features that are novel and non-obvious over all the Company’s previously filed applications. A feature claimed in the Patent is the ability to maintain continuous suction to the surgical field while simultaneously measuring, recording and evacuating fluid to the facilities sewer drainage system. This provides for continuous operation of the STREAMWAY System unit in suctioning waste fluids, which means that the unit never has to be shut off or paused during a surgical operation, for example, to empty a fluid collection container or otherwise dispose of the collected fluid.

**Subsequent Events**

*Sale of Convertible Preferred Stock and Warrants.* In February 2014, we raised \$2,055,000 less offering expenses from a private place of convertible preferred stock. As of February 4, 2014, Skyline Medical Inc. (the “Company”) entered into a Securities Purchase Agreement with certain investors (the “Purchasers”) pursuant to which the Company agreed to offer and sell 20,550 shares of Series A Convertible Preferred Stock, par value \$0.01 (the “Preferred Shares”), and warrants (the “Warrants”) to acquire an aggregate of approximately 1,600,000 shares of the Company’s common stock, par value \$0.01 (“Common Stock”). The Preferred Shares are convertible into shares of Common Stock at an initial conversion price of \$0.26 per share of Common Stock. The Warrants are exercisable at an exercise price of \$0.325 per share and expire five years from the closing date. The Company received gross proceeds of \$2,055,000, before offering expenses. The closing of the sale of the Preferred Shares and Warrants (collectively, the “Securities”) occurred as of February 4, 2014 (the “Closing”). If the Company’s Common Stock is not listed on the Nasdaq Stock Market, the New York Stock Exchange, or the NYSE MKT within 180 days of the Closing, the Company shall issue additional Warrants to purchase additional shares of Common Stock, equal to 30% of the shares of Common Stock which the Preferred Shares purchased by each Purchaser purchased are convertible.

The Securities Purchase Agreement requires the Company to register the resale of the shares of Common Stock underlying the Preferred Shares (the “Underlying Shares”) and the Common Stock underlying the Warrants (the “Warrant Shares”). The Company is required to prepare and file a registration statement with the Securities and Exchange Commission within 90 days of the closing of the offering, and to use commercially reasonable efforts to have the registration statement declared effective within 105 days if there is no review by the Securities and Exchange Commission, and within 150 days in the event of such review.

**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

The Securities were offered and sold without registration under the Securities Act of 1933, as amended (the “Securities Act”), or state securities laws, in reliance on the exemptions provided by Section 4(a)(2) of the Securities Act and Regulation D promulgated thereunder. The Securities may not be offered or sold in the United States without an effective registration statement or pursuant to an exemption from applicable registration requirements. Neither this Current Report on Form 8-K, nor the exhibits attached hereto is an offer to sell or the solicitation of an offer to buy the Securities.

The Preferred Shares are convertible at the option of the holder into the number of shares of Common Stock determined by dividing the stated value of the Preferred Shares being converted by the conversion price of \$0.26, subject to adjustment for stock splits, reverse stock splits and similar recapitalization events. If the Company issues additional shares of Common Stock, other than certain stock that is excluded under the terms of the Securities Purchase Agreement, in one or more capital raising transactions with an aggregate purchase price of at least \$100,000 for a price less than the then existing conversion price for the Preferred Shares (the “New Issuance Price”), then the then existing conversion price shall be reduced to the New Issuance Price, provided, however, that under no circumstances shall the New Issuance Price be less than \$0.13 or reduced to a price level that would be in breach of the listing rules of any stock exchange or that would have material adverse effect on the Corporation’s ability to list its Common Stock on a stock exchange, including but not limited to the change of accounting treatment of the Preferred Stock. The Preferred Shares contain certain limitations on conversion so that the holder will not own more than 4.99% of the number of shares of the Common Stock outstanding immediately after giving effect to the issuance of shares of Common Stock issuable upon conversion of Preferred Shares held by the applicable holder, with the percentage subject to increase in certain circumstances. The Preferred Shares are eligible to vote with the Common Stock on an as-converted basis, but only to the extent that the Preferred Shares are eligible for conversion without exceeding the Beneficial Ownership Limitation. The Preferred Shares are entitled to receive dividends on a pari passu basis with the Common Stock, when, and if declared. Upon any liquidation, dissolution or winding-up of the Company, whether voluntary or involuntary (a “Liquidation”), after the satisfaction in full of the debts of the Company and the payment of any liquidation preference owed to the holders of shares of Common Stock ranking prior to the Preferred Shares upon liquidation, the holders of the Preferred Shares shall receive, prior and in preference to the holders of any junior securities, an amount equal to \$2,055,000 times 1.2, plus all declared but unpaid dividends.

The Warrants are exercisable on any day on or after the date of issuance, have an exercise price of \$0.26 per share, subject to adjustment, and a term of five years from the date they are first exercisable. However, a holder will be prohibited from exercising a Warrant if, as a result of such exercise, the holder, together with its affiliates, would exceed the Beneficial Ownership Limitation as described above for the Preferred Shares. If any Warrant has not been fully exercised prior to the first anniversary of the Closing and if during such period the Company has not installed or received firm purchase orders (accepted by the Company) for at least 500 STREAMWAY® Automated Surgical Fluid Disposal Systems, then, the number of Common Stock for which such Warrant may be exercised shall be increased 2.5 times.

*Settlement with Group of Warrantholders.* In September 2013, the Company received a request to issue 4,993,814 shares of its common stock to a group of partnerships and individuals in connection with the cashless exercise of stock purchase warrants covering a total of 6,184,412 shares. In processing the exercise, the Company commenced an internal investigation regarding the warrants and withheld delivery of the certificates for a substantial majority of the shares, pending the outcome of the investigation.

After investigation, the Company disagreed with the group’s position that all of such shares should be delivered in connection with the exercise. Following negotiations, effective March 3, 2014, the Company and the group entered into a settlement agreement that resulted in, among other things, a net reduction of 1,264,988 shares. This reduction is reflected as outstanding on the balance sheet as of December 31, 2013.

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**SKYLINE MEDICAL, INC.  
(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 2 — DEVELOPMENT STAGE OPERATIONS**

The Company was formed April 23, 2002. Since inception through December 31, 2013, 219,937,619 shares of common stock have been issued between par value and \$1.67. Operations since incorporation have primarily been devoted to raising capital, obtaining financing, development of the Company's product, administrative services, customer acceptance and sales and marketing strategies.

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS**

In connection with the financing completed in October 2008, the Company has effected two reverse stock splits, one on June 6, 2008 and another on October 20, 2008. In accordance with SAB Topic 4C, all stock options and warrants and their related exercise prices are stated at their post-reverse stock split values.

The Company has an equity incentive plan, which allows issuance of incentive and non-qualified stock options to employees, directors and consultants of the Company, where permitted under the plan. The exercise price for each stock option is determined by the Board of Directors. Vesting requirements are determined by the Board of Directors when granted and currently range from immediate to three years. Options under this plan have terms ranging from three to ten years.

*Accounting for share-based payment*

The Company has adopted ASC 718 — *Compensation — Stock Compensation* ("ASC 718"). Under ASC 718 stock-based employee compensation cost is recognized using the fair value based method for all new awards granted after January 1, 2006 and unvested awards outstanding at January 1, 2006. Compensation costs for unvested stock options and non-vested awards that were outstanding at January 1, 2006, are being recognized over the requisite service period based on the grant-date fair value of those options and awards, using a straight-line method. We elected the modified-prospective method under which prior periods are not retroactively restated.

ASC 718 requires companies to estimate the fair value of stock-based payment awards on the date of grant using an option-pricing model or other acceptable means. The Company uses the Black-Scholes option valuation model which requires the input of significant assumptions including an estimate of the average period of time employees will retain vested stock options before exercising them, the estimated volatility of the Company's common stock price over the expected term, the number of options that will ultimately be forfeited before completing vesting requirements, the expected dividend rate and the risk-free interest rate. Changes in the assumptions can materially affect the estimate of fair value of stock-based compensation and, consequently, the related expense recognized. The assumptions the Company uses in calculating the fair value of stock-based payment awards represent the Company's best estimates, which involve inherent uncertainties and the application of management's judgment. As a result, if factors change and the Company uses different assumptions, the Company's equity-based compensation expense could be materially different in the future.

Since the Company's common stock has no significant public trading history, and the Company has experienced no significant option exercises in its history, the Company is required to take an alternative approach to estimating future volatility and estimated life and the future results could vary significantly from the Company's estimates. The Company compiled historical volatilities over a period of 2 to 7 years of 15 small-cap medical companies traded on major exchanges and 10 mid-range medical companies on the OTC Bulletin Board and combined the results using a weighted average approach. In the case of ordinary options to employees the Company determined the expected life to be the midpoint between the vesting term and the legal term. In the case of options or warrants granted to non-employees, the Company estimated the life to be the legal term unless there was a compelling reason to make it shorter.

**SKYLINE MEDICAL, INC.  
(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

When an option or warrant is granted in place of cash compensation for services, the Company deems the value of the service rendered to be the value of the option or warrant. In most cases, however, an option or warrant is granted in addition to other forms of compensation and its separate value is difficult to determine without utilizing an option pricing model. For that reason the Company also uses the Black-Scholes option-pricing model to value options and warrants granted to non-employees, which requires the input of significant assumptions including an estimate of the average period the investors or consultants will retain vested stock options and warrants before exercising them, the estimated volatility of the Company's common stock price over the expected term, the number of options and warrants that will ultimately be forfeited before completing vesting requirements, the expected dividend rate and the risk-free interest rate. Changes in the assumptions can materially affect the estimate of fair value of stock-based consulting and/or compensation and, consequently, the related expense recognized.

Since the Company has limited trading history in its stock and no first-hand experience with how its investors and consultants have acted in similar circumstances, the assumptions the Company uses in calculating the fair value of stock-based payment awards represent its best estimates, which involve inherent uncertainties and the application of management's judgment. As a result, if factors change and the Company uses different assumptions, the Company's equity-based consulting and interest expense could be materially different in the future.

*Valuation and accounting for options and warrants*

The Company determines the grant date fair value of options and warrants using a Black-Scholes option valuation model based upon assumptions regarding risk-free interest rate, expected dividend rate, volatility and estimated term. For grants issued during 2008, the Company used a 2.0 to 4.5% risk-free interest rate, 0% dividend rate, 53 – 66% volatility and estimated term of 2.5 to 7.5 years. Values computed using these assumptions ranged from \$.102 per share to \$.336 per share. Warrants or options awarded for services rendered are expensed over the period of service (normally the vesting period) as compensation expense for employees or an appropriate consulting expense category for awards to consultants and directors. Warrants granted in connection with a common equity financing are included in stockholders' equity, provided that there is no re-pricing provision that requires them to be treated as a liability (See Note 8) and warrants granted in connection with a debt financing are treated as a debt discount and amortized using the interest method as interest expense over the term of the debt.

Warrants issued in connection with the \$100,000 convertible debt that closed March 1, 2007 created a debt discount of \$40,242 that was being amortized as additional interest over its 5-year term. Warrants issued in connection with the \$170,000 convertible "bridge" debt that closed in July 2007 created a calculated debt discount of \$92,700 that was fully expensed over its loan term that matured April 30, 2008.

The Company issued \$100,000 in convertible debt in October 2009 and issued a warrant, in connection with the debt, for 200,000 shares of common stock at \$.65 per share. The Company determined that the warrant had an initial value of \$30,150 that was treated as a debt discount and amortized as additional interest expense over the 24-month term of the note.

The Company also issued \$200,000 in convertible debt in June 2010 and issued a warrant, in connection with the debt, to purchase 1,111,112 shares of common stock at \$.46 per share. The Company determined that the value of the June 2010 warrant was \$96,613. This value was treated as a debt discount and amortized as additional interest expense over the 22-month term of the note.

The Company also issued \$32,000 in convertible debt in September 2010 and issued a warrant to purchase 320,000 shares of common stock at \$.18 per share. The Company determined that this warrant had a value of \$15,553 that was treated as a debt discount and amortized as additional interest expense over the 18-month term of the note.

**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

The Company also issued \$16,800 in convertible debt in December 2010 and issued a warrant to purchase 200,000 shares of common stock at \$.084 per share. The Company determined that this warrant had a value of \$7,232 that was treated as a debt discount and amortized as additional interest expense over the 24-month term of the note.

In January 2011, the Company issued three convertible notes of \$50,000 each and also issued warrants to purchase 1,595,239 common shares at \$.20 per share. The value of the warrants was determined to be \$47,908 and was being treated as a debt discount and amortized as additional interest expense over the 24-month term of the notes.

For grants of stock options and warrants in 2011 the Company used a 0.34 to 2.44% risk-free interest rate, 0% dividend rate, 54 – 66% volatility and estimated term of 3 to 10 years. Values computed using these assumptions ranged from \$0.0126 to \$0.3412 per share.

In November 2012, the Company issued four convertible notes of \$27,500, \$27,500, \$51,243 and \$50,000, respectively. The note holders were issued shares of our common stock at \$.10 per share value in consideration for the notes. Though short term the value of the notes are being treated as a debt discount with an aggregate discount of \$33,469 and amortized as additional interest expense over the six month term of the notes.

For grants of stock options and warrants in 2012 the Company used a 0.33% to 1.80% risk-free interest rate, 0% dividend rate, 54%, 59% or 66% volatility and estimated terms of 3, 5 or 10 years. Value computed using these assumptions ranged from \$0.0111 to \$0.096 per share.

In January 2013, in connection with a private placement offering the Company issued 8% convertible one year promissory notes in an aggregate principal amount of \$300,000 convertible into 2,500,000 shares of common stock assuming a conversion rate of \$.12 per share and five year warrants to purchase up to an aggregate 2,500,000 shares of the corporation's common stock at an exercise price of \$.15 per share. The value of the notes were treated as a debt discount with an aggregate discount of \$77,644, and amortized as an additional interest expense over the twelve month term of the notes. In addition, we issued to the placement agent for these sales five year warrants to purchase an aggregate of 200,000 shares of common stock at an exercise price of \$.12 per share.

In January and March 2013, in connection with a separate and new private placement offering we issued 7,142,857 shares of common stock at \$.07 per share and warrants to purchase 7,142,857 shares of common stock at \$.15 per share to 5 investors in return for their \$500,000 investment in the Company.

On March 15, 2013 the Company completed the private sale of 7,142,858 shares of the Company's common stock, par value \$.01 per share, at \$.07 per share for an aggregate purchase price of \$500,000, warrants to purchase 7,142,858 shares of common stock at an exercise price of \$.08 per share, and warrants to purchase 3,571,429 shares of common stock at an exercise price of \$.15 per share.

In April 2013, the Company issued 200,000 shares of common stock, par value \$.01 per share, to a former consultant exercising options; the Company issued 333,330 shares of common stock, par value \$.01 per share, at \$.01 per share to the former CEO exercising options.

In May 2013, the Company converted four (4) notes totaling \$156,243, plus \$11,169 in interest; issued in November 2012, the noteholders received 1,116,084 shares of common stock, par value \$.01, at \$.10 per share. One of the noteholders was Dr. Samuel Horowitz who received 357,163 shares.

**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

In May and June 2013 in connection with a private placement offering we issued 8% convertible one year promissory notes in an aggregate principal amount of \$1,000,000 convertible into 6,000,000 shares of common stock assuming a conversion rate of \$.18 per share and five year warrants to purchase up to an aggregate of 4,611,111 shares of the corporation's common stock at an exercise price of \$.198 per share. The value of the notes net of discount was \$275,640 in 2013; due in May and June 2014. In addition, we issued to the placement agent for these sales five year warrants to purchase an aggregate of 444,444 shares of common stock at an exercise price of \$.18 per share.

In August and September 2013 the Company entered into agreements with holders of certain of its outstanding warrants to purchase the Company's common stock to amend the exercise price of the warrant to \$0.10 per share in connection with the agreement of each such holder to exercise the warrants in full. Prior to the amendments, the exercise prices of such warrants ranged from \$0.15 to \$0.46 per share. Twenty-four warrants were exercised with a reduced exercise price, and nineteen warrants were exercised pursuant to a net exercise provision. Together such warrant exercises resulted in aggregate cash proceeds of \$1,044,490 to the Company, and the issuance of an aggregate 10,444,898 shares of common stock through the reduced warrant exercise and 6,533,788 shares which were issued pursuant to a net exercise provision.

In October 2013 the Company entered into agreements with a holder of certain of its outstanding warrants to purchase the Company's common stock to amend the exercise price of the warrant to \$.125 per share in connection with the agreement of the holder to exercise the warrants in full. Prior to the amendments, the exercise price of such warrants was \$.25 per share. Two warrants were exercised with a reduced exercise price. Together the warrant exercises resulted in aggregate cash proceeds of \$125,000 to the Company, and the issuance of an aggregate 1,000,000 shares of common stock.

For grants of stock options and warrants in 2013 the Company used a 0.78% to 2.04% risk-free interest rate, 0% dividend rate, 59% or 66% volatility and estimated terms of 5 or 10 years. Value computed using these assumptions ranged from \$0.119 to \$0.242 per share.

The following summarizes transactions for stock options and warrants for the periods indicated:

	Stock Options <sup>(1)</sup>		Warrants <sup>(1)</sup>	
	Number of Shares	Average Exercise Price	Number of Shares	Average Exercise Price
Outstanding at December 31, 2005	17,956	\$ 1.67	20,950	\$ 2.62
Issued	23,942	1.67	71,826	0.85
Outstanding at December 31, 2006	41,898	1.67	92,776	1.25
Issued	5,984	1.67	28,502	0.35
Outstanding at December 31, 2007	47,882	1.67	121,278	1.04
Issued	1,243,292	0.2	5,075,204	0.45
Expired			(11,971)	3.76
Outstanding at December 31, 2008	1,291,174	0.26	5,184,511	0.45
Issued	205,000	0.37	2,188,302	0.65
Outstanding at December 31, 2009	1,496,174	0.27	7,372,813	0.49
Issued	2,210,000	0.17	3,435,662	0.34
Expired	(207,956)	0.43	(8,979)	1.67
Exercised			(128,571)	0.46
Outstanding at December 31, 2010	3,498,218	0.19	10,670,925	0.44
Issued	2,483,334	0.01	18,222,243	0.14
Expired	(83,941)	0.73	(2,010,917)	0.48

**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

	Stock Options <sup>(1)</sup>		Warrants <sup>(1)</sup>	
	Number of Shares	Average Exercise Price	Number of Shares	Average Exercise Price
Exercised	(100,000)	0.01		
Outstanding at December 31, 2011	5,797,611	0.11	26,882,251	0.23
Issued	9,514,286	0.08	11,688,166	0.15
Expired	(2,235,368)	0.11	(3,366,455)	0.50
Exercised	(412,963)	0.01	(71,826)	0.01
Outstanding at December 31, 2012	12,663,566	0.09	35,132,136	0.13
Issued	17,986,157	0.09	25,739,682	0.12
Expired	(1,159,995)	0.24	(8,326,862)	0.18
Exercised	(560,330)	0.01	(17,901,127)	0.11
Outstanding at December 31, 2013	28,929,398	\$ 0.09	34,643,829	\$ 0.14

(1) Adjusted for the reverse stock splits in total at June 6, 2008 and October 20, 2008.

At December 31, 2013, 27,658,652 stock options are fully vested and currently exercisable with a weighted average exercise price of \$0.085 and a weighted average remaining term of 8.80 years. There are 34,643,829 warrants that are fully vested and exercisable. Stock-based compensation recognized in 2013 and 2012 was \$3,700,070 and \$830,372, respectively. The Company has \$166,905 of unrecognized compensation expense related to non-vested stock options that are expected to be recognized over the next 22 months.

The following summarizes the status of options and warrants outstanding at December 31, 2013:

Range of Exercise Prices	Shares	Weighted Average Remaining Life
Options:		
\$0.01	550,000	7.52
\$0.017	325,187	4.43
\$0.065	10,000	9.20
\$0.07	197,286	9.44
\$0.075	14,400,000	9.21
\$0.079	1,740,508	9.22
\$0.08	9,300,000	8.63
\$0.88	400,000	8.07
\$0.1325	226,415	9.54
\$0.14	242,857	9.54
\$0.15	676,666	7.16
\$0.17	5,000	9.36
\$0.27	370,373	10.00
\$0.29	100,000	9.77
\$0.318	94,338	9.75
\$0.33	100,000	9.73
\$0.3415	20,000	9.75
\$0.35	75,000	0.37
\$0.585	95,768	0.44
Total	28,929,398	



**SKYLINE MEDICAL, INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO FINANCIAL STATEMENTS**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

<u>Range of Exercise Prices</u>	<u>Shares</u>	<u>Weighted Average Remaining Life</u>
<b>Warrants:</b>		
\$0.01	200,000	1.94
\$0.075	2,666,667	0.85
\$0.08	7,714,286	4.20
\$0.10	1,428,572	0.33
\$0.12	200,000	4.90
\$0.15	16,648,284	3.98
\$0.16	150,000	0.38
\$0.17	1,294,118	0.27
\$0.18	533,333	2.83
\$0.198	1,770,833	4.41
\$0.20	1,237,500	0.18
\$0.25	375,000	0.77
\$0.46	83,207	0.30
\$0.769	342,029	0.50
<b>Total</b>	<u>34,643,829</u>	

Stock options and warrants expire on various dates from January 2014 to December 2023.

Under the terms of the Company's agreement with investors in the October 2008 financing, 1,920,000 shares of common stock were the maximum number of shares allocated to the Company's existing shareholders at the time of the offering (also referred to as the original shareholders or the "Founders"). Since the total of the Company's fully diluted shares of common stock was greater than 1,920,000 shares, in order for the Company to proceed with the offering, the Board of Directors approved a reverse stock split of 1-for-1.2545. After this split was approved, additional options and warrants were identified, requiring a second reverse stock split in order to reach the 1,920,000 shares. The second reverse stock split on the reduced 1-for-1.2545 balance was determined to be 1-for-1.33176963. Taken together, if only one reverse stock split was performed, the number would have been a reverse stock split of 1-for-1.670705.

On June 6, 2008, the Board of Directors approved the first reverse stock split. The authorized number of shares of common stock of 20,000,000 was proportionately divided by 1.2545 to arrive at 15,942,607.

On October 20, 2008, the Board of Directors (i) approved the second reverse stock split pursuant to which the authorized number of shares of common stock of 15,942,607 was proportionately divided by 1.33177 to arrive at 11,970,994 shares and (ii) approved a resolution to increase the number of authorized shares of the Company's common stock from 11,970,994 to 40,000,000, which was approved by the Company's shareholders holding a majority of the shares entitled to vote thereon at a special meeting of shareholders held on December 3, 2008.

The shareholders approved an increase in authorized shares to 80 million shares in an annual shareholder meeting held on June 22, 2010 and approved an increase in authorized shares to 200 million shares in a special shareholder meeting held on September 7, 2011.

The shareholders approved an increase in authorized shares to 300 million shares in a special shareholder meeting held on January 15, 2013.

The shareholders approved an amendment of the Company's 2012 Stock Incentive Plan to increase the reserve of shares authorized for issuance to 50 million shares and to increase the threshold of limitation on certain grants to 20 million shares on April 15, 2013.

**SKYLINE MEDICAL, INC.**  
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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

An increase from 300 million to 800 million authorized shares, and an amendment of the Company's 2012 Stock Incentive Plan to increase the reserve of shares authorized for issuance to 100 million shares was approved at the September 10, 2013 annual meeting.

**Stock Options and Warrants Granted by the Company**

The following table is the listing of stock options and warrants as of December 31, 2013 by year of grant:

Stock Options:

Year	Shares	Price
2008	420,955	\$ .017 – .585
2009	75,000	.35
2010	410,000	.15
2011	550,000	.01
2012	9,497,286	.07 – .08
2013	17,976,157	0.065 – 0.3415
<b>Total</b>	<b>28,929,398</b>	<b>\$ .01 – .585</b>

Warrants:

Year	Shares	Price
2008	342,029	\$ 0.46 – 0.769
2009	83,207	.46
2010	200,000	.01
2011	8,597,690	.075 – .25
2012	5,352,451	.15 – 0.20
2013	20,068,452	0.08 – .198
<b>Total</b>	<b>34,643,829</b>	<b>\$ .01 – .769</b>

**NOTE 4 — LOSS PER SHARE**

The following table presents the shares used in the basic and diluted loss per common share computations:

	Year Ended December 31,		From
	2013	2012	April 23, 2002 (Inception) To December 31, 2013
Numerator:			
Net loss available in basic and diluted calculation	\$ (9,406,304)	\$ (7,422,155)	\$ (28,697,415)
Denominator:			
Weighted average common shares outstanding-basic	151,958,618	69,587,814	18,952,512
Effect of dilutive stock options and warrants <sup>(1)</sup>	—	—	—
Weighted average common shares outstanding-diluted	151,958,618	69,587,814	18,952,512
Loss per common share-basic and diluted	<u>\$ (0.06)</u>	<u>\$ (0.11)</u>	<u>\$ (1.51)</u>

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**SKYLINE MEDICAL, INC.**  
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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 4 — LOSS PER SHARE – (continued)**

(1) The number of shares underlying options and warrants outstanding as of December 31, 2013 and December 31, 2012 are 63,583,227 and 47,795,702, respectively. The effect of the shares that would be issued upon exercise of such options and warrants has been excluded from the calculation of diluted loss per share because those shares are anti-dilutive.

**NOTE 5 — INCOME TAXES**

The provision for income taxes consists of an amount for taxes currently payable and a provision for tax consequences deferred to future periods. Deferred income taxes are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

There is no income tax provision in the accompanying statements of operations due to the cumulative operating losses that indicate a 100% valuation allowance for the deferred tax assets and state income taxes is appropriate.

Federal and state income tax return operating loss carryovers as of December 31, 2013 were approximately \$13,969,000 and will begin to expire in 2017.

The valuation allowance has been recorded due to the uncertainty of realization of the benefits associated with the net operating losses. Future events and changes in circumstances could cause this valuation allowance to change.

The components of deferred income taxes at December 31, 2013 and December 31, 2012 are as follows:

	<b>December 31, 2013</b>	<b>December 31, 2012</b>
Deferred Tax Asset:		
Net Operating Loss	\$ 3,259,000	\$ 2,209,000
Other	59,000	73,000
Total Deferred Tax Asset	3,318,000	2,282,000
Less Valuation Allowance	3,318,000	2,282,000
Net Deferred Income Taxes	\$ —	\$ —

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**SKYLINE MEDICAL, INC.**  
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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 6 — LONG-TERM DEBT**

Long-term debt is as follows:

	December 31, 2013	December 31, 2012
Note payable issued on October 26, 2009, net of a discount of \$0 and \$0 discount, with interest at 8% to March 31, 2012 when the remaining balance was payable and convertible into shares of common stock at \$.35 per share. The note was renegotiated in February 2013.	—	100,000
Note payable issued on June 12, 2010 with interest at 12% to March 31, 2012 when the remaining balance was payable, and is convertible into shares of common stock at \$.18 per share. The note was renegotiated in February 2013.	—	200,000
Note payable issued on December 23, 2010, with interest at 10%, matured December 23, 2012 and was convertible into shares of common stock at \$.084 per share. The note was renegotiated in February 2013.	—	16,800
Note payable issued on September 21, 2010 with interest at 12%, matured March 30, 2012 and was convertible into shares of common stock at \$.18 per share. The note was renegotiated in February 2013.	—	32,000
Note payable issued January 1, 2011 to a law firm that accepted this note in full payment of their past due legal fees. The note bears interest at 6%, matures January 1, 2015 and is convertible into shares of common stock at \$.15 per share. The note was renegotiated in March 2013, and has been paid in full.	—	89,300
On November 6, 2012 the Company issued four convertible notes at 20% interest, each, net of an aggregate discount of \$21,138, due on April 6, 2013. The four notes were converted into 1,041,622 shares at \$0.10 per share.	—	122,774
<b>Total</b>	<b>—</b>	<b>560,874</b>
Less amount due within one year	—	471,574
<b>Long-Term Debt</b>	<b>\$ —</b>	<b>\$ 89,300</b>

Cash payments for interest were \$55,198 and \$31,008 for 2013 and 2012, respectively.

The four renegotiated notes above, totaling \$450,958 in principal and interest, will be paid for the next two (2) years as follows: \$120,000 in 2014 and \$120,000 in 2015. The remaining balance including attorney's fees and interest is due on February 1, 2016. The debt is secured by 666,667 shares of common stock held in escrow. The escrow account releases 1/3 or 333,333 shares per year to the Company if there is no default. If a default occurs the entire amount of stock left in escrow at the time of default is released to the former note holders.

**NOTE 7 — RENT OBLIGATION**

The Company leases its principal office under a lease that can be cancelled after three years with proper notice per the lease and an amortized schedule of adjustments that will be due to the landlord. The lease extends five years and expires January 2018. In addition to rent, the Company pays real estate taxes and repairs and maintenance on the leased property. Rent expense was \$61,150 and \$45,961 for 2013 and 2012, respectively.

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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 7 — RENT OBLIGATION – (continued)**

The Company's rent obligation for the next five years are as follows:

2014	\$ 36,000
2015	\$ 37,000
2016	\$ 38,000
2017	\$ 39,000
2018	\$ 3,000

**NOTE 8 — LIABILITY FOR EQUITY-LINKED FINANCIAL INSTRUMENTS**

The Company adopted ASC 815 — *Derivatives and Hedging* ("ASC 815") on January 1, 2009. ASC 815 mandates a two-step process for evaluating whether an equity-linked financial instrument or embedded feature is indexed to the entity's own stock. It was effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years, which was the Company's first quarter of 2009. Many of the warrants issued by the Company contain a strike price adjustment feature, which upon adoption of ASC 815, changed the classification (from equity to liability) and the related accounting for warrants with a \$479,910 estimated fair value of as of January 1, 2009. An adjustment was made to remove \$486,564 from paid-in capital (the cumulative values of the warrants on their grant dates), a positive adjustment of \$6,654 was made to accumulated deficit, representing the gain on valuation from the grant date to January 1, 2009, and \$479,910 was booked as a liability. The warrants issued in 2012 and 2011 do not contain a strike price adjustment feature and, therefore, are not treated as a liability.

The January 1, 2009 valuation was computed using the Black-Scholes valuation model based upon a 2.5-year expected term, an expected volatility of 63%, an exercise price of \$.46 per share, a stock price of \$.35, a zero dividend rate and a 1.37% risk free interest rate. Subsequent to January 1, 2009 these warrants were re-valued at the end of each quarter and a gain or loss was recorded based upon their increase or decrease in value during the quarter. Likewise, new warrants that were issued during 2009 and 2010 were valued, using the Black-Scholes valuation model on their date of grant and an entry was made to reduce paid-in capital and increase the liability for equity-linked financial instruments. These warrants were also re-valued at the end of each quarter based upon their expected life, the stock price, the exercise price, assumed dividend rate, expected volatility and risk free interest rate. A significant reduction in the liability was realized in 2010 primarily due to a reduction from \$.50 to \$.22 per share in the underlying stock price. The Company realized an increase in the liability for existing warrants during 2011 primarily due to a reduction in the spread between the exercise price and the market price of the underlying shares. In 2012, there was a slight increase to the liability due to the extension of warrants. In 2013 there was a significant decrease as a result of the older warrants expiring or getting exercised.

The inputs to the Black-Scholes model during 2009 through 2013 were as follows:

Stock price	\$.35
Exercise price	\$.769
Expected life	.50 years
Expected volatility	54%
Assumed dividend rate	—%
Risk-free interest rate	.13% to 2.97%

**SKYLINE MEDICAL, INC.**  
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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 8 — LIABILITY FOR EQUITY-LINKED FINANCIAL INSTRUMENTS – (continued)**

The original valuations, annual gain (loss) and end of year valuations are shown below:

	Initial Value	Annual Gain (Loss)	Value at 12/31/09	2010 Gain (Loss)	Value at 12/31/10	2011 Gain (Loss)	Value at 12/31/2011	2012 Gain (Loss)	Value at 12/31/2012	2013 Gain (Loss)	Value at 12/31/2013
January 1 2009 adoption	\$ 479,910	\$(390,368)	\$ 870,278	\$ 868,772	\$ 1,506	\$(88,290)	\$ 89,796	\$(21,856)	\$111,652	\$ 100,053	\$ 11,599
Warrants issued in quarter ended 6/30/2009	169,854	20,847	149,007	147,403	1,604	(4,689)	6,293	6,293	—	—	—
Warrants issued in quarter ended 9/30/2009	39,743	(738)	40,481	40,419	62	(1,562)	1,624	910	714	714	—
Warrants issued in quarter ended 12/31/2009	12,698	617	12,081	12,053	28	(724)	752	415	337	337	—
Subtotal	702,205		1,071,847								
Warrants issued in quarter ended 3/31/2010	25,553			25,014	539	(5,570)	6,109	3,701	2,408	2,408	—
Warrants issued in quarter ended 6/30/2010	31,332			30,740	592	(6,122)	6,714	6,083	631	631	—
Warrants issued in quarter ended 9/30/2010	31,506			20,891	10,615	(44,160)	54,775	1,338	53,437	53,437	—
Total	\$ 790,596	\$(369,642)	\$1,071,847	\$1,145,292	\$14,946	\$(151,117)	\$166,063	\$(3,116)	\$169,179	\$ 157,580	\$ 11,599

**NOTE 9 — RELATED PARTY TRANSACTIONS**

The Audit Committee has the responsibility to review and approve all transactions to which a related party and the Company may be a party prior to their implementation, to assess whether such transactions meet applicable legal requirements. Rick Koenigsberger, a director, is a holder of membership units in SOK Partners.

The Company, entered into agreements, in 2008, with our Chairman of the Board, Lawrence Gadbow, and in 2009 with a board member, Peter Morawetz, to pay Mr. Gadbow \$25,000 and Dr. Morawetz \$30,000 upon the Company raising \$3 million in new equity. Mr. Gadbow received 277,778 shares at \$.09 per share in June 2012 as compensation in lieu of the \$25,000 cash for raising \$3 million in new equity. Mr. Gadbow was paid the balance due under his separation agreement from 2008. This amount was \$46,000 upon signing the agreement in 2008 payable at \$2,000 per month; the payments to Mr. Gadbow are complete. Mr. Gadbow also received a warrant for 30,000 shares at \$.15 per share on June 30, 2012 as compensation for service as Chairman. Mr. Gadbow and Dr. Morawetz have both resigned from the Board in the third quarter of 2013. Both Mr. Gadbow and Dr. Morawetz received 50,000 shares of common stock each at \$.325 per share; 20,000 of these shares were for compensation from serving as Board members and the remaining 30,000 shares were issued to satisfy previous contractual agreements.

*Convertible Note Issuances to Dr. Samuel Herschkowitz and SOK Partners, LLC*

On September 11, 2013, both the Herschkowitz Note and the SOK Note (each as defined below in this Note 9) were converted in full by the holders thereof at \$0.014 per share. The principal and interest balance of the Herschkowitz Note of \$314,484 was converted into 22,463,172 shares of common stock. The principal and interest balance of the SOK Note of \$680,444 was converted into 48,603,721 shares of common stock. The collateral that secured these notes was released back to the Company.

The remaining disclosure of this Note 9 provides historical information regarding the Herschkowitz Note, the SOK Note and certain other convertible note issuances.

On March 28, 2012, the Company, entered into a Convertible Note Purchase Agreement, dated as of March 28, 2012 (the "SOK Purchase Agreement") with SOK Partners, LLC ("SOK Partners"), and an investment partnership. Josh Komberg, who is a member of the Company's Board of Directors, and Dr. Samuel Herschkowitz are affiliates of the manager of SOK Partners and Ricardo Koenigsberger, a director, is a holder of membership units of SOK Partners. Pursuant to the SOK Purchase Agreement, the Company issued a 20.0% convertible note due August 2012 in the principal amount of up to \$600,000. Principal and

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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 9 — RELATED PARTY TRANSACTIONS – (continued)**

accrued interest on the note is due and payable on August 28, 2012. The Company's obligations under the note are secured by the grant of a security interest in substantially all tangible and intangible assets of the Company. The SOK Purchase Agreement and the note include customary events of default that include, among other things, non-payment defaults, covenant defaults, inaccuracy of representations and warranties, cross-defaults to other indebtedness and bankruptcy and insolvency defaults. The occurrence of an event of default could result in the acceleration of the Company's obligations under the note, and interest rate of twenty-four (24%) percent per annum accrues if the note is not paid when due.

On March 28, 2012, the Company received an advance of \$84,657 under the note, including a cash advance of \$60,000 net of a prepayment of interest on the first \$300,000 in advances under the note. The holder of the note is entitled to convert the note into shares of common stock of the Company at an initial conversion price per share of \$0.065 per share, subject to adjustment in the event of (1) certain issuances of common stock or convertible securities at a price lower than the conversion price of the note, and (2) recapitalizations, stock splits, reorganizations and similar events. In addition, the Company is required to issue two installments of an equity bonus to SOK Partners in the form of common stock valued at the rate of \$0.065 per share. In March 2012, the Company issued the first equity bonus to SOK Partners, consisting of 4,615,385 shares of common stock, with a second installment due within five business days after SOK Partners has made aggregate advances under the note of at least \$300,000. In May 2012 the Company issued the second installment consisting of 4,615,385 shares of common stock subsequent to SOK Partners surpassing the aggregate advances of \$300,000. Until the maturity date of the note, if the Company obtains financing from any other source without the consent of SOK Partners, then the Company is required to issue additional bonus equity in an amount equal to \$600,000 less the aggregate advances on the note made prior to the breach. The principal balance of the SOK Note was \$357,282 as of December 31, 2012.

As long as any amount payable under the SOK Note remains outstanding, SOK Partners or its designee is entitled to appoint a new member to the Company's Board of Directors, who will be appointed upon request. Mr. Koenigsberger was appointed to the Board by SOK Partners on June 25, 2012.

On March 28, 2012, the Company signed an Amended and Restated Note Purchase Agreement, dated as of December 20, 2011, with Dr. Samuel Herschkowitz (as amended, the "Herschkowitz Purchase Agreement"). Pursuant to the Herschkowitz Purchase Agreement, the Company issued a 20.0% convertible note due June 20, 2012 in the principal amount of \$240,000 for previous advances under the note. The Company's obligations under the note are secured by the grant of a security interest in substantially all tangible and intangible assets of the Company. The Company has previously issued to Dr. Herschkowitz an equity bonus consisting of 1,546,667 shares of common stock. An additional 7,500,000 shares were transferred to Dr. Herschkowitz effective in April 2012, upon the occurrence of an event of default on the note. On August 13, 2012, the Company entered into a settlement and forbearance agreement described below, relating to the defaults under the Herschkowitz Note and other matters.

As long as any amount payable under the Herschkowitz Note remains outstanding, Dr. Herschkowitz or his designee is entitled to appoint a special advisor to the Company's Board of Directors, to be appointed as a member upon request. Pursuant to this authority, Josh Kornberg was appointed to the Board on March 9, 2012. In addition, pursuant to this authority, Mr. Koenigsberger was appointed to the Board on June 25, 2012.

Pursuant to a letter dated April 12, 2012, Dr. Herschkowitz advised the Company of the occurrence of numerous events of default under the terms of the Herschkowitz Note and the Herschkowitz Note Purchase Agreement. As a result of such events of default, Dr. Herschkowitz asserted significant rights as a secured creditor of the Company, including his rights as a secured creditor with a security interest in substantially all assets of the Company. Without a settlement relating to the defaults and other matters, Dr. Herschkowitz could have taken action to levy upon the Company's assets, including patents and other intellectual property.

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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 9 — RELATED PARTY TRANSACTIONS – (continued)**

In addition, the Company and Atlantic Partners Alliance LLC (“APA”) were parties to a letter agreement dated March 14, 2012, providing APA and its affiliates (including Dr. Herschkowitz and SOK) with rights to avoid dilution relating to additional issuances of equity securities by the Company through July 14, 2012, evidencing the parties’ intent that APA would be provided with significant protection against dilution. This protection was in recognition of APA’s investments in the Company involving a high degree of risk and the Company’s contemplated need for restructuring its indebtedness, which were anticipated to result, and have resulted, in significant dilution. The parties acknowledged that Dr. Herschkowitz and SOK would not have made their historical cash investments in the Company to the same degree had the dilution protection not been provided, and the investments by these parties have enabled the Company to avoid insolvency. Since the respective dates of the Herschkowitz Note Purchase Agreement and the SOK Note Purchase Agreement, the Company had issued in excess of 16,000,000 shares of common stock to parties other than APA and its affiliates, resulting in significant dilution.

Effective August 15, 2012, the Company entered into a letter agreement with Dr. Herschkowitz, APA and SOK (the “Forbearance Agreement”). Under the Forbearance Agreement, among other things, (i) Dr. Herschkowitz agreed to forbear from asserting his rights as a secured creditor to substantially all of the Company’s assets, resulting from the Company’s defaults; (ii) the Company issued an aggregate 26.5 million shares of common stock to Dr. Herschkowitz and SOK and adjusted the conversion price of their convertible notes to \$0.014 per share from \$0.065 per share, to satisfy the Company’s obligations to adjust for dilution; (iii) Dr. Herschkowitz and SOK agreed to extend the maturity of their notes to December 31, 2012; (iv) the Company agreed to pay certain compensation to Dr. Herschkowitz upon the achievement of financial milestones and (v) Dr. Herschkowitz clarified and waived certain of his rights, including the right to interest at a penalty rate upon default.

In the Forbearance Agreement, Dr. Herschkowitz agreed to forbear from exercising any of his rights arising under the Herschkowitz Note or the Herschkowitz Note Purchase Agreement with respect to the existing defaults against the Company, subject to the limitations set forth in the letter agreement and without releasing or waiving any future breach of the letter agreement. He further agreed to forbear from exercising any rights with respect to events of default, security interests in the collateral and other similar remedies against the Company or his interests under the Herschkowitz Note or the Herschkowitz Note Purchase Agreement until the occurrence of an event of default under the Herschkowitz Note: (a) that does not constitute an existing default and (b) occurs and accrues after the date of the letter agreement.

Dr. Herschkowitz and the Company acknowledged that 7.5 million shares of the Company’s common stock, constituting the “penalty shares” under the Herschkowitz Note Purchase Agreement, were delivered to Dr. Herschkowitz in April 2012 as provided in the Herschkowitz Note Purchase Agreement upon an event of default. Notwithstanding a provision that would have increased the rate of interest from 20% to 24% upon an event of default, Dr. Herschkowitz agreed that the Company would not pay the increased rate of interest but would accrue interest at 20% until a subsequent event of default.

Under the Forbearance Agreement, the Herschkowitz Note and the SOK Note were amended as follows: (i) the due dates of the notes were extended to December 31, 2012 from the previous due dates of June 20, 2012 and August 28, 2012, respectively; (ii) Dr. Herschkowitz will release his security agreement after payment of all currently outstanding promissory notes to parties other than SOK; and (iii) the Herschkowitz Note was amended to add certain events of default relating to judgments against the Company or other creditors taking action with respect to the collateral. In consideration of the extension additional milestone fees were revised as described below. Pursuant to a Forbearance and Settlement Agreement with these parties dated August 15, 2012, as subsequently amended, the due date of these notes were extended to August 31, 2013.



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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 9 — RELATED PARTY TRANSACTIONS – (continued)**

APA and its affiliates agreed to terminate the letter agreement regarding dilution dated March 14, 2012. In consideration of the various provisions of the letter agreement and in recognition of the understanding of the parties regarding dilution and the agreements of APA and its affiliates to forbear and to extend the due dates of the notes, the Company (i) issued 13,250,000 shares to Dr. Herschkowitz, (ii) issued 13,250,000 shares to SOK, and (iii) the conversion price of the Herschkowitz Note and the SOK Note, respectively was changed to \$0.014 per share from \$0.065 per share.

In the event that the Company consummated the following series of transactions on or prior to June 30, 2013: (i) a merger or similar transaction with a public shell company, (ii) raising between \$2 million and \$4 million through an offering of the securities of the public shell company concurrent with or subsequent to the shell merger and (iii) listing the Company's shares on NASDAQ pursuant to an underwritten offering of the Company's securities resulting in gross proceeds of between \$5 million and \$30 million, then the Company would have to be required to deliver to Dr. Herschkowitz the following compensation: (A) \$75,000 upon consummating the shell merger, (B) \$150,000 upon consummating the qualifying financing round and (C) 3% of the gross proceeds of the NASDAQ underwriting, which payment shall under no circumstances be less than \$200,000 or greater than \$1,000,000. The Company was also required to reimburse Dr. Herschkowitz at his actual out-of-pocket cost for reasonable expenses incurred in connection with the shell transactions, with a maximum limit of \$10,000 for such expenses.

In connection with the extension of the due date for the Herschkowitz Note and the SOK Note on March 6, 2013, the milestone fees were revised. The following fees were payable to Dr. Herschkowitz in the event that the Company consummates the following series of transactions on or prior to December 31, 2013: (i) financing raising not less than \$1 million, compensation of \$75,000; (ii) a going private transaction, compensation of \$200,000 or greater and (iii) 3% of the gross proceeds of the NASDAQ underwriting, which payment shall under no circumstances be less than \$200,000 or greater than \$3,000,000. In May 2013 Dr. Herschkowitz received \$75,000 after the Company surpassed raising \$1 million.

As a result of the transactions under the Forbearance Agreement and other investments, Dr. Herschkowitz, SOK and their affiliates currently own shares of common stock and securities representing beneficial ownership of more than 65% of the Company's outstanding common stock, giving such parties significant control over election of the Board of Directors and other matters.

On November 6, 2012, the Company issued and sold convertible promissory notes in the total principal amount of \$156,243 to Dr. Herschkowitz and certain of his assignees. The Company issued to these parties an aggregate 1,562,430 shares of common stock in consideration of placement of the notes. The notes bear interest at a rate of 20% per annum and are secured by a security interest in the Company's accounts receivable, patents and certain patent rights and are convertible into common stock upon certain mergers or other fundamental transactions at a conversion price based on the trading price prior to the transaction. The proceeds from this transaction were used to pay off approximately \$155,000 in principal amount of secured indebtedness. Such notes were converted in April 2013 in to 1,041,622 shares of common stock at \$.10 per share.

In December 2013 the Company received an additional \$300,000 in debt financing from SOK Partners under a non-convertible grid note due February 28, 2014, with 10% interest based on a 365 day year. Dr. Herschkowitz received 10% of the gross proceeds in advance, and the Company received \$250,000 in three tranches in December 2013. In January 2014, the Company received an additional \$20,000 from SOK Partners completing the grid note maximum. Should the company default on the note the interest rate will increase to 20% interest based on a 365 day year. In February 2014, the Company wired \$305,589.04 to SOK Partners in complete payment of the grid note, including interest.

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**NOTES TO FINANCIAL STATEMENTS**

**NOTE 10 — RETIREMENT SAVINGS PLANS**

We have a pre-tax salary reduction/profit-sharing plan under the provisions of Section 401(k) of the Internal Revenue Code, which covers employees meeting certain eligibility requirements. In fiscal 2012, its inception year, and again in 2013, we matched 100% of the employee's contribution up to 4.0% of their earnings. The employer contribution was \$32,790 and \$1,654 in 2013 and 2012. There were no discretionary contributions to the plan in 2013 and 2012.

**NOTE 11 — COMMITMENTS AND CONTINGENCIES**

*Marshall Ryan & Mid-State Stainless, Inc. v. Skyline Medical Inc. & Dr. Samuel Herschkowitz.* On March 5, 2014, plaintiffs filed an action in District Court in Hennepin County, Minnesota against the Company and one of its stockholders, Dr. Samuel Herschkowitz. Marshall Ryan, one of the plaintiffs, is an engineer who worked with the Company on design of certain of its products. The action alleges, among other things, breach of a consulting agreement, a manufacturing agreement and a supply agreement between plaintiffs and the Company, various claims of fraud and negligent misrepresentation and breach of the duty of good faith and fair dealing. The Company believes the claims are without merit and is preparing its response.

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PART 1. FINANCIAL INFORMATION  
Item 1. Condensed Financial Statements

**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**CONDENSED BALANCE SHEETS**  
**(Unaudited)**

	June 30, 2014	December 31, 2013
<b>ASSETS</b>		
Current Assets:		
Cash	\$ 40,151	\$ 101,953
Accounts Receivable	149,640	97,245
Inventories	360,663	122,175
Prepaid Expense and other assets	149,524	60,588
Total Current Assets	<u>699,977</u>	<u>381,961</u>
Fixed Assets, net	204,658	158,110
Intangibles, net	68,137	53,355
Total Assets	<u>\$ 972,772</u>	<u>\$ 593,426</u>
<b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>		
Current Liabilities:		
Accounts payable	1,625,330	1,062,108
Accrued expenses	2,194,486	2,057,957
Short-term note payable net of discounts of \$46,072 and \$0 (See Note 8)	81,124	280,000
Deferred Revenue	5,000	69,000
Total Current Liabilities	<u>3,905,940</u>	<u>3,469,065</u>
Accrued Expenses	290,344	331,216
Liability for equity-linked financial instruments (See Note 9)	130	11,599
Total Liabilities	<u>\$ 4,196,414</u>	<u>\$ 3,811,880</u>
Commitments and Contingencies	—	—
Stockholders' Deficit:		
Series A Convertible Preferred Stock, \$.01 par value, \$100 Stated Value, 40,000 authorized, 20,550 outstanding	206	—
Common stock, \$.01 par value, 800,000,000 authorized, 222,869,997 and 219,937,619 outstanding	2,228,700	2,199,376
Additional paid-in capital	26,647,135	23,279,585
Deficit accumulated during development stage	(32,099,683)	(28,697,415)
Total Stockholders' Deficit	<u>(3,223,642)</u>	<u>(3,218,454)</u>
Total Liabilities and Stockholders' Deficit	<u>\$ 972,772</u>	<u>\$ 593,426</u>

See Notes to Condensed Financial Statements.

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**CONDENSED STATEMENTS OF OPERATIONS**  
**(Unaudited)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Revenue	\$ 318,293	\$ 150,856	\$ 388,513	\$ 278,583
Cost of goods sold	98,365	67,335	129,448	108,939
Gross Margin	219,928	83,521	259,065	169,644
General and administrative expense	1,330,222	888,133	2,509,504	2,711,216
Operations expense	291,584	204,928	556,859	409,395
Sales and marketing expense	319,303	108,593	524,223	195,562
Interest expense	14,773	126,654	32,897	222,206
Loss (gain) on valuation of equity-linked financial instruments	—	(69,251)	(11,468)	(88,673)
Total expense	1,955,882	1,259,057	3,612,014	3,446,705
Net income (loss) available to common shareholders	\$ (1,735,954)	\$ (1,175,535)	\$ (3,352,949)	\$ (3,277,061)
Loss per common share basic and diluted	\$ (0.01)	\$ (0.01)	\$ (0.02)	\$ (0.03)
Weighted average shares used in computation, basic and diluted	222,620,910	121,267,500	221,922,352	111,045,552

See Notes to Condensed Financial Statements.

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENT OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM DECEMBER 31, 2012**  
**TO JUNE 30, 2014**  
**(Unaudited)**

	Preferred Stock	Common Stock		Paid-in Capital	Deficit	Total
		Shares	Amount			
Balance at 12/31/2012	\$ —	104,247,228	\$ 1,042,473	\$ 14,945,435	\$(19,291,111)	\$(3,303,203)
Shares issued to debtors as compensation at \$.15 per share		290,143	2,901	40,620		43,521
Shares issued under PPM to five investors at \$.07 per share		7,142,857	71,429	428,571		500,000
Shares issued to an escrow account underlying a debt agreement		1,000,000	10,000			10,000
Shares issued to debtors as compensation at \$.15 per share		230,332	2,303	32,247		34,550
Shares issued to an institutional investor at \$.07 per share		7,142,858	71,429	428,571		500,000
Value of shares per an agreement with a former officer				40,480		40,480
Shares issued to consultant as compensation at \$.067 per share		250,000	2,500	14,250		16,750
Value of Equity instruments issued with debt				392,556		392,556
Shares issued to former consultant exercising options at \$.01 per share		200,000	2,000			2,000
Shares issued to former CEO exercising options at \$.01 per share.		333,330	3,333			3,333
Shares issued upon conversion of four notes payable at \$.15 per share		1,041,622	10,416	145,827		156,243
Shares issued for interest to the four notes payable at \$.15 per share		74,462	745	10,425		11,170
Shares issued for cashless exercise of warrants at \$.12 per share		277,778	2,778			2,778
Shares issued for cashless exercise of warrants at \$.16 per share		163,334	1,633			1,633
Shares issued for cashless exercise of warrants at \$.15 per share		632,708	6,327			6,327
Shares issued for cashless exercise of warrants at \$.20 per share		261,848	2,618			2,618
Shares issued to 24 warrant holders exercised at a reduced price for \$.10 per share		10,444,898	104,449	940,041		1,044,490
Shares issued to 4 PPM investors converting notes at \$.12 per share		2,637,534	26,375	290,129		316,504
Shares issued to 10 PPM investors converting notes at \$.18 per share		5,405,431	54,054	966,146		1,020,200
Shares issued to consultant as compensation at \$.38 per share		150,000	1,500	55,500		57,000
Shares issued for two note conversions at \$.014 per share		71,066,331	710,663	284,265		994,928

See Notes to Condensed Financial Statements.

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENT OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM DECEMBER 31, 2012**  
**TO JUNE 30, 2014 – (continued)**  
**(Unaudited)**

	Preferred Stock	Common Stock		Paid-in Capital	Deficit	Total
		Shares	Amount			
Shares issued for warrant exercise at \$.15 per share		1,071,429	10,715	150,000		160,715
Shares issued for a cashless exercise of warrants at \$.10 per share		3,024,390	30,244			30,244
Shares issued to an investor for a cashless exercise of warrants at \$.17 per share		204,306	2,044			2,044
Shares issued for a cashless exercise of warrants at \$.075 per share		544,714	5,447			5,447
Shares issued to former Board Directors as compensation at \$.325 per share		100,000	1,000	99,000		100,000
Reduced warrant exercise compensation expense				2,140,946		2,140,946
Options issued as part of employee bonus				147,500		147,500
Shares issued to one investor for cashless warrant exercised at \$.12 per share		277,778	2,778			2,778
Shares issued for cashless warrant exercise at \$.13 per share		159,722	1,597			1,597
Shares issued for interest on two note conversions at \$.18 per share		40,918	409	6,956		7,365
Shares issued in settlement with a former noteholder at \$.27 per share		378,000	3,780	98,280		102,060
Shares issued for a stock option exercise at \$.065 per share		10,000	100	550		650
Shares issued to one warrant holder executed at a reduced price of \$.125 per share		1,000,000	10,000	115,000		125,000
Shares issued for option exercise at \$.07 per share		17,000	170	1,020		1,190
Shares issued for cashless warrant exercise at \$.075 per share		116,667	1,167			1,167
Vesting expense				1,505,270		1,505,270
Net loss					(9,406,304)	(9,406,304)
Balance at 12/31/13	\$ —	219,937,619	\$ 2,199,376	\$ 23,279,585	\$(28,697,415)	\$(3,218,454)
Shares issued for cashless warrant exercise at \$.20 per share		129,630	1,296			1,296
Shares issued for option exercise at \$.0167 per share		325,187	3,252	2,178		5,430
Shares issued at \$.275 per share as Investor Relations compensation		150,000	1,500	39,750		41,250
Shares issued for cashless warrant exercise at \$.17 per share		249,252	2,493			2,493
Shares issued for an option exercise at \$.07 per share		20,000	200	1,200		1,400
Shares issued for cashless warrant exercise at \$.01 per share		163,062	1,630			1,630

See Notes to Condensed Financial Statements.

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**STATEMENT OF STOCKHOLDERS' DEFICIT**  
**PERIOD FROM DECEMBER 31, 2012**  
**TO JUNE 30, 2014 – (continued)**  
**(Unaudited)**

	Preferred Stock	Common Stock		Paid-in Capital	Deficit	Total
		Shares	Amount			
Shares issued for warrant exercise at \$.18 per share		200,000	2,000	34,000		36,000
Shares issued at \$.25 per share as Investor Relations compensation		100,000	1,000	24,000		25,000
Reduction in escrow account per settlement agreement		(333,334)	(3,333)			(3,333)
Shares issued for cashless warrant exercise at \$.10 per share		360,444	3,605			3,605
Shares issued for cashless warrant exercise at \$.075 per share		233,334	2,333			2,333
Shares issued for cashless warrant exercise at \$.17 per share		22,409	224			224
Shares issued to 16 shareholders of Series A Convertible Preferred Stock Dividends as converted to common shares at \$.26 per share		72,760	728	18,191	(18,919)	—
Vesting Expense				352,762		352,762
Options issued as part of employee bonus				694,500		694,500
Shares issued for combined cashless and cash warrant exercise @ \$.15 per share.		583,334	5,833	46,667		52,500
Issuance of Preferred stock	206			2,054,795		2,055,001
Shares issued to Investor Relations consultant exercisable at \$.15 per share		160,000	1,600	22,400		24,000
Shares issued to Investor Relations consultant exercisable at \$.25 per share		100,000	1,000	24,000		25,000
Shares issued for cashless warrant exercise at \$.18 per share		279,366	2,794			2,794
Shares issued to 16 shareholders of Series A Convertible Preferred Stock Dividends as converted to common shares at \$.26 per share		116,934	1,169	29,232	(30,400)	—
Value of equity instruments issued with debt				23,876		23,876
Net loss					(3,352,949)	(3,352,949)
Balance at 6/30/2014	\$ 206	222,869,997	\$ 2,228,700	\$ 26,647,136	\$(32,099,683)	\$(3,223,642)

See Notes to Condensed Financial Statements.

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**CONDENSED STATEMENTS OF CASH FLOWS**  
**(Unaudited)**

	Six Months Ended	
	June 30,	
	2014	2013
Cash flow from operating activities:		
Net loss	(3,352,949)	(3,277,061)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	25,829	141,482
Vested stock options and warrants	369,636	1,378,090
Equity instruments issued for management and consulting	111,917	67,230
Amortization of debt discount	—	92,538
(Gain) loss on valuation of equity-linked instruments	(11,468)	(88,673)
Changes in assets and liabilities:		
Accounts receivable	(52,395)	(62,180)
Inventories	(238,488)	37,173
Prepaid expense and other assets	(88,936)	(8,176)
Notes payable to shareholders	—	—
Accounts payable	563,223	(28,993)
Accrued expenses	790,157	(379,465)
Deferred Revenue	(64,000)	5,000
Net cash used in operating activities:	(1,947,473)	(2,123,035)
Cash flow from investing activities:		
Purchase of fixed assets	(72,377)	(9,826)
Purchase of intangibles	(14,782)	(48,545)
Net cash used in investing activities:	(87,159)	(58,371)
Cash flow from financing activities:		
Proceeds from long-term and convertible debt	125,000	1,300,000
Principal payments on notes payable	(300,000)	—
Issuance of preferred stock	2,055,000	—
Issuance of common stock	92,831	1,005,333
Net cash provided by (used in) financing activities	1,972,831	2,305,333
Net increase (decrease) in cash	(61,802)	123,927
Cash at beginning of period	101,953	13,139
Cash at end of period	40,151	137,066
Non cash transactions:		
Conversion of debt to accrued liabilities	—	415,775
Common stock issued for accrued interest/bonus	694,500	23,394
Common stock issued to satisfy debt	—	178,568
Stock/warrant issued to satisfy accounts payable/Liabilities	—	43,521

See Notes to Condensed Financial Statements.



**SKYLINE MEDICAL INC.  
(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of Operations and Continuance of Operations**

BioDrain Medical, Inc. (the “Company”) was incorporated under the laws of the State of Minnesota in 2002. Effective August 6, 2013, the Company changed its name to Skyline Medical Inc. Pursuant to an Agreement and Plan of Merger dated effective December 16, 2013, the Company merged with and into a Delaware corporation with the same name that was its wholly-owned subsidiary, with such Delaware Corporation as the surviving corporation of the merger. The Company has developed an environmentally safe system for the collection and disposal of infectious fluids that result from surgical procedures and post-operative care. The Company also makes ongoing sales of our proprietary cleaning fluid and filters to users of our systems. In April 2009, the Company received 510(k) clearance from the FDA to authorize the Company to market and sell its STREAMWAY FMS products.

The accompanying financial statements have been prepared assuming the Company will continue as a going concern. The Company has suffered recurring losses from operations and has a stockholders’ deficit. These factors raise substantial doubt about its ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Since inception to June 30, 2014, the Company has raised approximately \$9,104,000 in equity, inclusive of \$2,055,000 from a private placement of Series A Convertible Preferred Stock, and \$4,060,000 in debt financing. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources”.

**Recent Accounting Developments**

In May 2014, the Financial Accounting Standards Board (“FASB”) issued ASU 2014-09, *Revenue from Contracts with Customers* and created a new topic in the FASB Accounting Standards Codification (“ASC”), Topic 606. The new standard provides a single comprehensive revenue recognition framework for all entities and supersedes nearly all existing U.S. GAAP revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity should recognize revenue in a manner that depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard is designed to create greater comparability for financial statement users across industries and also requires enhanced disclosures. The amendments are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. We are currently evaluating the impact this guidance may have on our financial statements and related disclosures.

In June 2014, the FASB issued ASU 2014-10, *Development Stage Entities* (Topic 915): Elimination of Certain Financial Reporting Requirements. ASU 2014-10 eliminates the distinction of a development stage entity and certain related disclosure requirements, including the elimination of inception-to-date information on the statements of operations, cash flows and stockholders’ equity. The amendments in ASU 2014-10 will be effective prospectively for annual reporting periods beginning after December 15, 2014, and interim periods within those annual periods, however early adoption is permitted. The Company evaluated and adopted ASU 2014-10 for the reporting period ended June 30, 2014.

In June 2014, the FASB issued ASU 2014-12, *Compensation — Stock Compensation* providing explicit guidance on how to account for share-based payments granted to employees in which the terms of the award provide that a performance target that affects vesting could be achieved after the requisite service period. The amendments in this Update are effective for annual periods and interim periods within those annual periods beginning after December 15, 2015. Early adoption is permitted. We are currently evaluating the impact this guidance may have on our financial statements.

**SKYLINE MEDICAL INC.  
(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

We reviewed all other significant newly issued accounting pronouncements and determined they are either not applicable to our business or that no material effect is expected on our financial position and results of our operations.

**Valuation of Intangible Assets**

We review identifiable intangible assets for impairment in accordance with ASC 350 — *Intangibles — Goodwill and Other*, whenever events or changes in circumstances indicate the carrying amount may not be recoverable. Our intangible assets are currently solely the costs of obtaining trademarks and patents. Events or changes in circumstances that indicate the carrying amount may not be recoverable include, but are not limited to, a significant change in the medical device marketplace and a significant adverse change in the business climate in which we operate. If such events or changes in circumstances are present, the undiscounted cash flows method is used to determine whether the intangible asset is impaired. Cash flows would include the estimated terminal value of the asset and exclude any interest charges. If the carrying value of the asset exceeds the undiscounted cash flows over the estimated remaining life of the asset, the asset is considered impaired, and the impairment is measured by reducing the carrying value of the asset to its fair value using the discounted cash flows method. The discount rate utilized is based on management's best estimate of the related risks and return at the time the impairment assessment is made.

Our accounting estimates and assumptions bear various risks of change, including the length of the current economic downturn facing the United States, the expansion of the slowdown in consumer spending in the U.S. medical markets despite the early expressed opinions of financial experts that the medical market would not be as affected as other markets and failure to gain acceptance in the medical market.

**Accounting Policies and Estimates**

The presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Presentation of Taxes Collected from Customers**

Sales taxes are imposed on the Company's sales to nonexempt customers. The Company collects the taxes from customers and remits the entire amounts to the governmental authorities. The Company's accounting policy is to exclude the taxes collected and remitted from revenues and expenses.

**Shipping and Handling**

Shipping and handling charges billed to customers are recorded as revenue. Shipping and handling costs are recorded within cost of goods sold on the statement of operations.

**Advertising**

Advertising costs are expensed as incurred. Advertising expenses were \$1,250 and \$7,793 in the three and six months ended June 30, 2014 and there were no advertising expenses in the three and six months ended June 30, 2013.

**Research and Development**

Research and development costs are charged to operations as incurred. Research and development expenses were \$131,285 and \$249,636 in the three and six months ended June 30, 2014 and \$75,264 and \$133,541 for June 30, 2013.

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

**Revenue Recognition**

The Company recognizes revenue in accordance with the SEC’s Staff Accounting Bulletin Topic 13 Revenue Recognition and ASC 605 — Revenue Recognition.

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable and collectability is probable. Delivery is considered to have occurred upon either shipment of the product or arrival at its destination based on the shipping terms of the transaction. The Company’s standard terms specify that shipment is FOB Skyline and the Company will, therefore, recognize revenue upon shipment in most cases. This revenue recognition policy applies to shipments of the STREAMWAY FMS units as well as shipments of cleaning solution and filters. When these conditions are satisfied, the Company recognizes gross product revenue, which is the price it charges generally to its customers for a particular product. Under the Company’s standard terms and conditions, there is no provision for installation or acceptance of the product to take place prior to the obligation of the customer. The customer’s right of return is limited only to the Company’s standard one-year warranty whereby the Company replaces or repairs, at its option, and it would be rare that the STREAMWAY FMS unit or significant quantities of cleaning solution and filters may be returned. Additionally, since the Company buys the STREAMWAY FMS units, cleaning solution and filters from “turnkey” suppliers, the Company would have the right to replacements from the suppliers if this situation should occur.

**Receivables**

Receivables are reported at the amount the Company expects to collect on balances outstanding. The Company provides for probable uncollectible amounts through charges to earnings and credits to the valuation based on management’s assessment of the current status of individual accounts, changes to the valuation allowance have not been material to the financial statements.

**Inventories**

Inventories are stated at the lower of cost or market, with cost determined on a first-in, first-out basis. Inventory balances are as follows:

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Finished goods	\$ 88,285	\$ 56,818
Raw materials	230,092	18,603
Work-In-Process	42,286	46,754
Total	<u>\$ 360,663</u>	<u>\$ 122,175</u>

**Property and Equipment**

Property and equipment are stated at cost less accumulated depreciation and amortization. Depreciation of property and equipment is computed using the straight-line method over the estimated useful lives of the respective assets. Estimated useful asset life by classification is as follows:

	<b>Years</b>
Computers and office equipment	3 – 7
Leasehold improvements	5
Manufacturing tooling	3 – 7

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

The Company's investment in Fixed Assets consists of the following:

	June 30, 2014	December 31, 2013
Computers and office equipment	\$ 126,234	\$ 61,505
Leasehold improvements	23,874	23,614
Manufacturing tooling	97,288	89,900
Total	247,396	175,019
Less: Accumulated depreciation	42,738	16,909
Total Fixed Assets, Net	<u>\$ 204,658</u>	<u>\$ 158,110</u>

Upon retirement or sale, the cost and related accumulated depreciation are removed from the balance sheet and the resulting gain or loss is reflected in operations. Maintenance and repairs are charged to operations as incurred.

**Intangible Assets**

Intangible assets consist of trademarks and patent costs. These assets are not subject to amortization until the property patented is in production. The assets are reviewed for impairment annually, and impairment losses, if any, are charged to operations when identified. The Company wrote-off the entire original STREAMWAY System patent of \$140,588 in 2013.

**Income Taxes**

The Company accounts for income taxes in accordance with ASC 740 — Income Taxes ("ASC 740"). Under ASC 740, deferred tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities and net operating loss and credit carryforwards using enacted tax rates in effect for the year in which the differences are expected to impact taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized.

The Company reviews income tax positions expected to be taken in income tax returns to determine if there are any income tax uncertainties. The Company recognizes tax benefits from uncertain tax positions only if it is more likely than not that the tax positions will be sustained on examination by taxing authorities, based on technical merits of the positions. The Company has identified no income tax uncertainties.

Tax years subsequent to 2010 remain open to examination by federal and state tax authorities.

**Patents and Intellectual Property**

On January 25<sup>th</sup>, 2014 the Company filed a non-provisional PCT Application No. PCT/US2014/013081 claiming priority from the U.S. Provisional Patent Application, number 61756763 which was filed one year earlier on January 25<sup>th</sup>, 2013. The PCT makes it possible to seek patent protection for an invention simultaneously in each of 148 countries, including the United States, by filing this "international" patent application instead of filing several separate national or regional patent applications.

Our PCT patent application is for the new model of the surgical fluid waste management system that has embodiments, based on our patent attorney's recommendations, that are patentable over all prior art and will not infringe on any existing patents. This PCT Application adds features that are novel and non-obvious over all the Company's previously filed applications. A feature claimed in the Patent is the ability to maintain continuous suction to the surgical field while simultaneously measuring, recording and evacuating fluid to the facilities sewer drainage system. This provides for continuous operation of the STREAMWAY System unit in suctioning waste fluids, which means that the unit never has to be shut off or paused during a surgical operation, for example, to empty a fluid collection container or otherwise dispose of the collected fluid.

**SKYLINE MEDICAL INC.  
(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (continued)**

**Subsequent Events**

On July 23, 2014, Skyline Medical Inc. (the “**Company**”) entered into a Securities Purchase Agreement (the “**Investor Securities Purchase Agreement**”) with an institutional investor (the “**Investor**”), pursuant to which on that date the Company issued and sold (i) a senior convertible note, in an original principal amount of \$610,978 (the “**Investor Note**”), which Investor Note shall be convertible into a certain amount of shares (the “**Investor Conversion Shares**”) of the Company’s common stock, par value \$0.01 (the “**Common Stock**”), in accordance with the terms of the Investor Note, and (ii) a warrant (the “**Investor Warrant**”) to initially acquire up to 2,036,593 additional shares of Common Stock (the “**Investor Warrant Shares**”, and collectively with the Investor Note, the Investor Warrant and the Investor Conversion Shares, the “**Investor Securities**”). The aggregate purchase price was \$500,000 (an approximately 22.2% original issue discount) (the “**Investor Convertible Notes Offering**”).

On July 23, 2014, the Company also entered into a Securities Purchase Agreement (the “**SOK Securities Purchase Agreement**”) with SOK Partners, LLC, an affiliate of the Company (“**SOK**”), pursuant to which on that date the Company issued and sold (i) a senior convertible note, in an original principal amount of \$122,196 (the “**SOK Note**”), which SOK Note shall be convertible into a certain amount of shares (the “**SOK Conversion Shares**”) of Common Stock, in accordance with the terms of the SOK Note, and (ii) a warrant (the “**SOK Warrant**”) to initially acquire up to 407,318 additional shares of Common Stock (the “**SOK Warrant Shares**”, and collectively with the SOK Note, the SOK Warrant and the SOK Conversion Shares, the “**SOK Securities**”). The aggregate purchase price was \$100,000 (an approximately 22.2% original issue discount) (the “**SOK Convertible Notes Offering**”).

See “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources” for a discussion of the above transactions.

**Interim Financial Statements**

The Company has prepared the unaudited interim financial statements and related unaudited financial information in the footnotes in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial statements. These interim financial statements reflect all adjustments consisting of normal recurring accruals, which, in the opinion of management, are necessary to present fairly the Company’s financial position, the results of its operations and its cash flows for the interim periods. These interim financial statements should be read in conjunction with the annual financial statements and the notes thereto contained in the Form 10-K filed with the SEC on March 27, 2014. The nature of the Company’s business is such that the results of any interim period may not be indicative of the results to be expected for the entire year.

**NOTE 2 — DEVELOPMENT STAGE OPERATIONS**

The Company was formed April 23, 2002. Since inception to August 4, 2014, 222,975,766 shares of common stock have been issued between par value and \$1.67. Operations since incorporation have been devoted to raising capital, obtaining financing, development of the Company’s product, and administrative services.

**SKYLINE MEDICAL INC.  
(A DEVELOPMENT STAGE COMPANY)**

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**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS**

The Company has an equity incentive plan, which allows issuance of incentive and non-qualified stock options to employees, directors and consultants of the Company, where permitted under the plan. The exercise price for each stock option is determined by the Board of Directors. Vesting requirements are determined by the Board of Directors when granted and currently range from immediate to three years. Options under this plan have terms ranging from three to ten years.

On February 4, 2014, (the "Closing Date") we raised \$2,055,000 in gross proceeds from a private placement of Series A Convertible Preferred Stock, par value \$0.01 (the "Preferred Shares") pursuant to a Securities Purchase Agreement with certain investors (the "Purchasers") purchased 20,550 Preferred Shares, and warrants (the "Warrants") to acquire an aggregate of approximately 1,600,000 shares of Common Stock. The Preferred Shares are convertible into shares of Common Stock at an initial conversion price of \$0.26 per share of Common Stock. The Warrants are exercisable at an exercise price of \$0.325 per share and expire five years from the Closing Date. If the Common Stock is not listed on the Nasdaq Stock Market, the New York Stock Exchange, or the NYSE MKT within 180 days of the Closing, the Company shall issue additional Warrants to purchase additional shares of Common Stock, equal to 30% of the shares of Common Stock which the Preferred Shares each Purchaser purchased are convertible into. As of August 4, 2014, the Company issued additional warrants to purchase 4,615,385 shares to the Purchasers in connection with this provision.

The Securities Purchase Agreement requires the Company to register the resale of the shares of Common Stock underlying the Preferred Shares (the "Underlying Shares") and the Common Stock underlying the Warrants (the "Warrant Shares"). The Company is required to prepare and file a registration statement with the Securities and Exchange Commission within 132 days of the Closing Date (as extended by subsequent consent of the Purchasers), and to use commercially reasonable efforts to have the registration statement declared effective within 147 days if there is no review by the Securities and Exchange Commission, and within 192 days in the event of such review. Pursuant to the Registration Rights Agreement this deadline was extended to a filing deadline of 45 days from July 23, 2014, and an effectiveness deadline of the earlier of (A) 60 calendar days from July 23, 2014 (or 120 calendar days from July 23, 2014 if the registration is subject to review by SEC) and (B) the fifth Trading Day after the Company is notified by the SEC that the Registration Statement will not be reviewed or will not be subject to further review.

The Preferred Shares are convertible at the option of the holder into the number of shares of Common Stock determined by dividing the stated value of the Preferred Shares being converted by the conversion price of \$0.26, subject to adjustment for stock splits, reverse stock splits and similar recapitalization events. If the Company issues additional shares of Common Stock, other than certain stock that is excluded under the terms of the Securities Purchase Agreement, in one or more capital raising transactions with an aggregate purchase price of at least \$100,000 for a price less than the then existing conversion price for the Preferred Shares (the "New Issuance Price"), then the then existing conversion price shall be reduced to the New Issuance Price, provided, however, that under no circumstances shall the New Issuance Price be less than \$0.13 or reduced to a price level that would be in breach of the listing rules of any stock exchange or that would have material adverse effect on the Corporation's ability to list its Common Stock on a stock exchange, including but not limited to the change of accounting treatment of the Preferred Stock. The Preferred Shares contain certain limitations on conversion so that the holder will not own more than 4.99% of the number of shares of the Common Stock outstanding immediately after giving effect to the issuance of shares of Common Stock issuable upon conversion of Preferred Shares held by the applicable holder, with the percentage subject to increase in certain circumstances. The Preferred Shares are eligible to vote with the Common Stock on an as-converted basis, but only to the extent that the Preferred Shares are eligible for conversion without exceeding the Beneficial Ownership Limitation. The Preferred Shares are entitled to receive dividends on a pari passu basis with the Common Stock, when, and if declared. Upon any liquidation, dissolution or

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**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

winding-up of the Company, whether voluntary or involuntary (a "Liquidation"), after the satisfaction in full of the debts of the Company and the payment of any liquidation preference owed to the holders of shares of Common Stock ranking prior to the Preferred Shares upon liquidation, the holders of the Preferred Shares shall receive, prior and in preference to the holders of any junior securities, an amount equal to \$2,055,000 times 1.2, plus all declared but unpaid dividends.

The Warrants are exercisable on any day on or after the date of issuance, have an exercise price of \$0.325 per share, subject to adjustment, and a term of five years from the date they are first exercisable. However, a holder will be prohibited from exercising a Warrant if, as a result of such exercise, the holder, together with its affiliates, would exceed the Beneficial Ownership Limitation as described above for the Preferred Shares. If any Warrant has not been fully exercised prior to the first anniversary of the Closing and if during such period the Company has not installed or received firm purchase orders (accepted by the Company) for at least 500 STREAMWAY® Automated Surgical Fluid Disposal Systems, then, the number of shares of Common Stock for which such Warrant may be exercised shall be increased 2.5 times.

*Accounting for share-based payment*

The Company has adopted ASC 718 — Compensation — Stock Compensation ("ASC 718"). Under ASC 718 stock-based employee compensation cost is recognized using the fair value based method for all new awards granted after January 1, 2006 and unvested awards outstanding at January 1, 2006. Compensation costs for unvested stock options and non-vested awards that were outstanding at January 1, 2006, are being recognized over the requisite service period based on the grant-date fair value of those options and awards, using a straight-line method. We elected the modified-prospective method under which prior periods are not retroactively restated.

ASC 718 requires companies to estimate the fair value of stock-based payment awards on the date of grant using an option-pricing model or other acceptable means. The Company uses the Black-Scholes option valuation model which requires the input of significant assumptions including an estimate of the average period of time employees will retain vested stock options before exercising them, the estimated volatility of the Company's common stock price over the expected term, the number of options that will ultimately be forfeited before completing vesting requirements, the expected dividend rate and the risk-free interest rate. Changes in the assumptions can materially affect the estimate of fair value of stock-based compensation and, consequently, the related expense recognized. The assumptions the Company uses in calculating the fair value of stock-based payment awards represent the Company's best estimates, which involve inherent uncertainties and the application of management's judgment. As a result, if factors change and the Company uses different assumptions, the Company's equity-based compensation expense could be materially different in the future.

Since the Company's common stock has no significant public trading history, and the Company has experienced no significant option exercises in its history, the Company is required to take an alternative approach to estimating future volatility and estimated life and the future results could vary significantly from the Company's estimates. The Company compiled historical volatilities over a period of 2 to 7 years of 15 small-cap medical companies traded on major exchanges and 10 mid-range medical companies on the OTC Bulletin Board and combined the results using a weighted average approach. In the case of ordinary options to employees the Company determined the expected life to be the midpoint between the vesting term and the legal term. In the case of options or warrants granted to non-employees, the Company estimated the life to be the legal term unless there was a compelling reason to make it shorter.

When an option or warrant is granted in place of cash compensation for services, the Company deems the value of the service rendered to be the value of the option or warrant. In most cases, however, an option or warrant is granted in addition to other forms of compensation and its separate value is difficult to determine without utilizing an option pricing model. For that reason the Company also uses the Black-Scholes

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**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

option-pricing model to value options and warrants granted to non-employees, which requires the input of significant assumptions including an estimate of the average period the investors or consultants will retain vested stock options and warrants before exercising them, the estimated volatility of the Company's common stock price over the expected term, the number of options and warrants that will ultimately be forfeited before completing vesting requirements, the expected dividend rate and the risk-free interest rate. Changes in the assumptions can materially affect the estimate of fair value of stock-based consulting and/or compensation and, consequently, the related expense recognized.

Since the Company has limited trading history in its stock and no first-hand experience with how its investors and consultants have acted in similar circumstances, the assumptions the Company uses in calculating the fair value of stock-based payment awards represent its best estimates, which involve inherent uncertainties and the application of management's judgment. As a result, if factors change and the Company uses different assumptions, the Company's equity-based consulting and interest expense could be materially different in the future.

*Valuation and accounting for options and warrants*

The Company determines the grant date fair value of options and warrants using a Black-Scholes option valuation model based upon assumptions regarding risk-free interest rate, expected dividend rate, volatility and estimated term.

In January 2013, in connection with a private placement offering we issued 8% convertible one year promissory notes in an aggregate principal amount of \$300,000 convertible into 2,500,000 shares of common stock assuming a conversion rate of \$.12 per share and five year warrants to purchase up to an aggregate of 2,500,000 shares of the corporation's common stock at an exercise price of \$.15 per share. The value of the notes are being treated as a debt discount with an aggregate discount of \$77,644, and amortized as an additional interest expense over the twelve month term of the notes. In addition, we issued to the placement agent for these sales five year warrants to purchase an aggregate of 200,000 shares of common stock at an exercise price of \$.12 per share.

In January and March 2013, in connection with a separate and new private placement offering we issued 7,142,857 shares of common stock at \$.07 per share and warrants to purchase 7,142,857 shares of common stock at \$.15 per share to 5 investors in return for their \$500,000 investment in the Company.

On March 15, 2013 the Company completed the private sale of 7,142,858 shares of the Company's common stock, par value \$.01 per share, at \$.07 per share for an aggregate purchase price of \$500,000, warrants to purchase 7,142,858 shares of common stock at an exercise price of \$.08 per share, and warrants to purchase 3,571,429 shares of common stock at an exercise price of \$.15 per share.

In April 2013, the Company issued 200,000 shares of common stock, par value \$.01 per share, to a former consultant exercising options; the Company issued 333,330 shares of common stock, par value \$.01 per share, at \$.01 per share to the former CEO exercising options.

In May 2013, the Company converted four (4) notes totaling \$156,243, plus \$11,169 in interest; issued in November 2012, the noteholders received 1,116,084 shares of common stock, par value \$.01, at \$.10 per share. One of the noteholders was Dr. Samuel Horowitz who received 357,163 shares.

In May and June 2013 in connection with a private placement offering we issued 8% convertible one year promissory notes in an aggregate principal amount of \$1,000,000 convertible into 6,000,000 shares of common stock assuming a conversion rate of \$.18 per share and five year warrants to purchase up to an aggregate of 4,611,111 shares of the corporation's common stock at an exercise price of \$.198 per share. The value of the notes net of discount was \$275,640 in 2013; due in May and June 2014. In addition, we issued to



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**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

the placement agent for these sales five year warrants to purchase an aggregate of 444,444 shares of common stock at an exercise price of \$.18 per share.

In August and September 2013 the Company entered into agreements with holders of certain of its outstanding warrants to purchase the Company's common stock to amend the exercise price of the warrant to \$0.10 per share in connection with the agreement of each such holder to exercise the warrants in full. Prior to the amendments, the exercise prices of such warrants ranged from \$0.15 to \$0.46 per share. Twenty-four warrants were exercised with a reduced exercise price, and nineteen warrants were exercised pursuant to a net exercise provision. Together such warrant exercises resulted in aggregate cash proceeds of \$1,044,490 to the Company, and the issuance of an aggregate 10,444,898 shares of common stock through the reduced warrant exercise and 6,533,788 shares which were issued pursuant to a net exercise provision.

In October 2013 the Company entered into agreements with a holder of certain of its outstanding warrants to purchase the Company's common stock to amend the exercise price of the warrant to \$.125 per share in connection with the agreement of the holder to exercise the warrants in full. Prior to the amendments, the exercise price of such warrants was \$.25 per share. Two warrants were exercised with a reduced exercise price. Together the warrant exercises resulted in aggregate cash proceeds of \$125,000 to the Company, and the issuance of an aggregate 1,000,000 shares of common stock.

For grants of stock options and warrants in 2013 the Company used a 0.78% to 2.04% risk-free interest rate, 0% dividend rate, 59% or 66% volatility and estimated terms of 5 or 10 years. Value computed using these assumptions ranged from \$0.119 to \$0.242 per share.

In January 2014 the Company issued 325,187 shares of common stock to the former CEO at \$.0167 per share upon his exercising options.

In January through March 2014, 9 warrant holders exercised warrants through a cashless exercise for a total of 1,158,131 shares of common stock.

In January and February 2014 the Company issued warrants to purchase 1,615,383 shares pursuant to a February 4, 2014 private placement whereby the Company issued 20,550 shares of Series A Convertible Preferred Stock raising gross proceeds of \$2,055,000. The warrants are at an exercise price of \$0.325.

In February 2014 the Company issued a warrant to purchase 111,111 shares of common stock at an exercise price of \$0.27 to a major shareholder Dr. Samuel Herschkowitz. The warrant is in consideration for a bridge loan extended in December 2013 that has been paid in February 2014.

On March 31, 2014, the Company issued dividends to the Purchasers of the Preferred Shares as described above. The dividends are at an annual rate of 6% of the stated value of the Preferred Shares paid on a quarterly basis in the form of common stock per a stipulated \$0.26 per share. As a result 72,760 shares of common stock were issued to 16 holders of Preferred Shares.

In March 2014, the Company issued 333,334 shares of common stock to a warrant holder for a partial cash exercise at \$0.15 per share; issued 250,000 shares to the holder via the cashless exercise of the remainder of the warrant.

In June 2014, the Company issued 279,366 shares of common stock to a warrant holder exercising cashless warrants.

On June 30, 2014, the Company issued dividends to the Purchasers of the Preferred Shares as described above. The dividends are at an annual rate of 6% of the stated value of the Preferred Shares paid on a quarterly basis in the form of common stock per a stipulated \$0.26 per share. As a result 116,934 shares of common stock were issued to 16 holders of Preferred Shares.

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**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

On June 30, 2014, the Company issued a warrant to purchase 407,318 shares of common stock at an exercise price of \$0.165 to SOK Partners, LLC, in consideration for a bridge loan. The warrant has a Black-Scholes debt discount of \$23,876.

For grants of stock options and warrants in 2014 the Company used a 1.44% to 2.75% risk-free interest rate, 0% dividend rate, 59% to 66% volatility and estimated terms of 5 to 10 years. Value computed using these assumptions ranged from \$0.0586 to \$0.1837 per share.

The following summarizes transactions for stock options and warrants for the periods indicated:

	Stock Options		Warrants	
	Number of Shares	Average Exercise Price	Number of Shares	Average Exercise Price
Outstanding at December 31, 2012	12,663,566	0.09	35,132,136	0.13
Issued	17,986,157	0.09	25,739,682	0.12
Expired	(1,159,995)	0.24	(8,326,862)	0.18
Exercised	(560,330)	0.01	(17,901,127)	0.11
Outstanding at December 31, 2013	28,929,398	0.09	34,643,829	0.14
Issued	5,115,061	0.11	2,133,812	0.27
Expired	(495,768)	0.34	(4,171,733)	0.16
Exercised	(345,187)	0.02	(2,220,831)	0.13
Outstanding at June 30, 2014	<u>33,203,504</u>	<u>\$ 0.10</u>	<u>30,385,077</u>	<u>\$ 0.15</u>

At June 30, 2014, 31,341,741 stock options are fully vested and currently exercisable with a weighted average exercise price of \$0.10 and a weighted average remaining term of 8.79 years. All warrants are fully vested and exercisable. Stock-based compensation recognized for the six months ending June 2014 and June 30, 2013 was \$352,762 and \$1,378,541, respectively. The Company has \$259,398 of unrecognized compensation expense related to non-vested stock options that are expected to be recognized over a weighted average period of approximately 18 months.

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**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

The following summarizes the status of options and warrants outstanding at June 30, 2014:

<b>Range of Exercise Prices</b>	<b>Shares</b>	<b>Weighted Average Remaining Life</b>
<b>Options:</b>		
\$0.01	550,000	7.02
\$0.065	10,000	8.70
\$0.07	177,286	9.12
\$0.075	14,400,000	8.71
\$0.079	1,740,508	8.72
\$0.08	9,300,000	8.13
\$0.088	400,000	7.57
\$0.1325	226,415	9.04
\$0.14	242,857	9.04
\$0.15	1,110,000	7.97
\$0.17	755,000	9.79
\$0.185	162,162	9.76
\$0.20	250,000	9.72
\$0.23	3,019,565	9.69
\$0.25	250,000	9.65
\$0.27	370,373	9.51
\$0.29	100,000	9.28
\$0.318	94,338	9.26
\$0.33	25,000	9.24
\$0.3415	20,000	9.25
<b>Total</b>	<b><u>33,203,504</u></b>	
<b>Warrants:</b>		
\$0.01	30,000	1.44
\$0.075	2,083,333	0.07
\$0.08	7,714,286	3.71
\$0.12	200,000	3.58
\$0.15	15,314,951	3.52
\$0.165	407,318	1.38
\$0.18	333,333	3.97
\$0.198	1,770,833	3.92
\$0.20	87,500	0.60
\$0.25	375,000	0.27
\$0.27	111,111	3.21
\$0.325	1,615,383	4.76
\$0.769	342,029	0.01
<b>Total</b>	<b><u>30,385,077</u></b>	

Stock options and warrants expire on various dates from July 2014 to June 2024.

The shareholders approved an increase in authorized shares to 80 million shares in an annual shareholder meeting held on June 22, 2010 and approved an increase in authorized shares to 200 million shares in a special shareholder meeting held on September 7, 2011.

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**NOTES TO CONDENSED FINANCIAL STATEMENTS**

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**NOTE 3 — STOCKHOLDERS' DEFICIT, STOCK OPTIONS AND WARRANTS – (continued)**

The shareholders approved an increase in authorized shares to 300 million shares in a special shareholder meeting held on January 15, 2013.

The shareholders approved an amendment of the Company's 2012 Stock Incentive Plan to increase the reserve of shares authorized for issuance to 50 million shares and to increase the threshold of limitation on certain grants to 20 million shares on April 15, 2013.

An increase from 300 million to 800 million authorized shares, and an amendment of the Company's 2012 Stock Incentive Plan to increase the reserve of shares authorized for issuance to 100 million shares was approved at the September 10, 2013 annual meeting.

**Stock Options and Warrants Granted by the Company**

The following table is the listing of stock options and warrants as of June 30, 2014 by year of grant:

Stock Options:

<b>Year</b>	<b>Shares</b>	<b>Price</b>
2010	410,000	\$ .15
2011	550,000	.01
2012	9,477,286	.07 – .08
2013	17,901,157	.065 – .3415
2014	4,865,061	.15 – .25
<b>Total</b>	<b>33,203,504</b>	<b>\$ .01 – .3415</b>

Warrants:

<b>Year</b>	<b>Shares</b>	<b>Price</b>
2008	342,029	\$ .769
2010	30,000	.01
2011	2,458,333	.075 – .25
2012	5,352,451	.15 – .20
2013	20,068,452	.08 – .198
2014	2,133,812	.165 – .325
<b>Total</b>	<b>30,385,077</b>	<b>\$ .01 – .769</b>

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**NOTE 4 — LOSS PER SHARE**

The following table presents the shares used in the basic and diluted loss per common share computations:

	<u>Three Months Ended June 30,</u>		<u>Six Months Ended June 30,</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Numerator:				
Net loss available in basic and diluted calculation	\$ (1,735,954)	\$ (1,175,535)	\$ (3,352,949)	\$ (3,277,061)
Denominator:				
Weighted average common shares outstanding-basic	222,620,910	121,267,500	221,922,352	111,045,552
Effect of diluted stock options and warrants <sup>(1)</sup>	—	—	—	—
Weighted average common shares outstanding-basic	222,620,910	121,267,500	221,922,352	111,045,552
Loss per common share-basic and diluted	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>	<u>\$ (0.02)</u>	<u>\$ (0.03)</u>

(1) The number of shares underlying options and warrants outstanding as of June 30, 2014 and June 30, 2013 are 63,588,581 and 84,320,276 respectively. The effect of the shares that would be issued upon exercise of such options and warrants has been excluded from the calculation of diluted loss per share because those shares are anti-dilutive.

**NOTE 5 — INCOME TAXES**

The provision for income taxes consists of an amount for taxes currently payable and a provision for tax consequences deferred to future periods. Deferred income taxes are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred income tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled.

There is no income tax provision in the accompanying statements of operations due to the cumulative operating losses that indicate a 100% valuation allowance for the deferred tax assets and state income taxes is appropriate.

During September 2013, the Company experienced an “ownership change” as defined in Section 382 of the Internal Revenue Code which could potentially limit the ability to utilize the Company’s net operating losses (NOLs). The general limitation rules allow the Company to utilize its NOLs subject to an annual limitation that is determined by multiplying the federal long-term tax-exempt rate by the Company’s value immediately before the ownership change.

At June 30, 2014, the Company had approximately \$16.0 million of gross NOLs to reduce future federal taxable income, the majority of which are expected to be available for use in 2015, subject to the Section 382 limitation described above. The federal NOLs will expire beginning in 2022 if unused. The Company also had approximately \$17.1 million of gross NOLs to reduce future state taxable income at June 30, 2014, which will expire in years 2022 through 2034 if unused. The Company’s net deferred tax assets, which include the NOLs, are subject to a full valuation allowance. At June 30, 2014, the federal and state valuation allowances were \$7.1 million and \$1.5 million, respectively.

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**NOTES TO CONDENSED FINANCIAL STATEMENTS**

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**NOTE 5 — INCOME TAXES – (continued)**

The components of deferred income taxes at June 30, 2014 and December 31, 2013 are as follows:

	June 30, 2014	December 31, 2013
Deferred Tax Asset:		
Net Operating Loss	\$ 7,920,000	\$ 3,259,000
Other	648,000	59,000
Total Deferred Tax Asset	8,568,000	3,318,000
Less Valuation Allowance	8,568,000	3,318,000
Net Deferred Income Taxes	\$ —	\$ —

**NOTE 6 — RENT OBLIGATION**

The Company leases its principal office under a lease that can be cancelled after three years with proper notice per the lease and an amortized schedule of adjustments that will be due to the landlord. The lease extends five years and expires January 2018. In addition to rent, the Company pays real estate taxes and repairs and maintenance on the leased property. Rent expense was \$15,447 and \$33,056, for the three and six months ended June 30, 2014 and was \$15,173 and \$35,159 for the three and six months ended June 30, 2013 respectively.

The Company's rent obligation for the next five years is as follows:

2015	\$ 37,000
2016	\$ 38,000
2017	\$ 39,000
2018	\$ 3,600
2019	\$ —

**NOTE 7 — LIABILITY FOR EQUITY-LINKED FINANCIAL INSTRUMENTS**

The Company adopted ASC 815 — Derivatives and Hedging (“ASC 815”) on January 1, 2009. ASC 815 mandates a two-step process for evaluating whether an equity-linked financial instrument or embedded feature is indexed to the entity's own stock. It was effective for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years, which was the Company's first quarter of 2009. Many of the warrants issued by the Company contain a strike price adjustment feature, which upon adoption of ASC 815, changed the classification (from equity to liability) and the related accounting for warrants with a \$479,910 estimated fair value of as of January 1, 2009. An adjustment was made to remove \$486,564 from paid-in capital (the cumulative values of the warrants on their grant dates), a positive adjustment of \$6,654 was made to accumulated deficit, representing the gain on valuation from the grant date to January 1, 2009, and \$479,910 was booked as a liability. The warrants issued in 2011 do not contain a strike price adjustment feature and, therefore, are not treated as a liability.

The January 1, 2009 valuation was computed using the Black-Scholes valuation model based upon a 2.5-year expected term, an expected volatility of 63%, an exercise price of \$.46 per share, a stock price of \$.35, a zero dividend rate and a 1.37% risk free interest rate. Subsequent to January 1, 2009 these warrants were re-valued at the end of each quarter and a gain or loss was recorded based upon their increase or decrease in value during the quarter. Likewise, new warrants that were issued during 2009 and 2010 were valued, using the Black-Scholes valuation model on their date of grant and an entry was made to reduce paid-in capital and increase the liability for equity-linked financial instruments. These warrants were also re-valued at the end of each quarter based upon their expected life, the stock price, the exercise price,

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**SKYLINE MEDICAL INC.**  
**(A DEVELOPMENT STAGE COMPANY)**

**NOTES TO CONDENSED FINANCIAL STATEMENTS**

(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)

**NOTE 7 — LIABILITY FOR EQUITY-LINKED FINANCIAL INSTRUMENTS – (continued)**

assumed dividend rate, expected volatility and risk free interest rate. A significant reduction in the liability was realized in 2010 primarily due to a reduction from \$.50 to \$.22 per share in the underlying stock price. The Company realized a slight increase in the liability for existing warrants during the first quarter of 2012. In 2013 there was a significant decrease in the liability primarily due to current expirations and the amount of warrants reaching expiration in the near term. In the first quarter 2014 the liability continued to decrease, and was stable in the second quarter 2014.

The inputs to the Black-Scholes model during 2009 through 2014 were as follows:

Stock price	\$.06 to \$.50
Exercise price	\$.01 to \$.325
Expected life	2.0 to 6.5 years
Expected volatility	59%
Assumed dividend rate	—%
Risk-free interest rate	.13% to 2.97%

The original valuations, annual gain/(loss) and end of year valuations are shown below:

	Annual		Value at 12/31/09	2010 Gain (Loss)	Value at 12/31/10	2011 Gain (Loss)	Value at 12/31/2011	2012 Gain (Loss)	Value at 12/31/2012	2013 Gain (Loss)	Value at 12/31/2013	2014 Gain (Loss)	Value at 6/30/2014
	Initial Value	Gain (Loss)											
January 1, 2009 adoption	\$ 479,910	\$(390,368)	\$ 870,278	\$ 868,772	\$ 1,506	\$(88,290)	\$ 89,796	\$(21,856)	\$ 111,652	\$ 100,053	\$ 11,599	\$ 11,469	\$ 130
Warrants issued in quarter ended 6/30/2009	169,854	20,847	149,007	147,403	1,604	(4,689)	6,293	6,293	—	—	—	—	—
Warrants issued in quarter ended 9/30/2009	39,743	(738)	40,481	40,419	62	(1,562)	1,624	910	714	714	—	—	—
Warrants issued in quarter ended 12/31/2009	12,698	617	12,081	12,053	28	(724)	752	415	337	337	—	—	—
Subtotal	702,205		1,071,847										
Warrants issued in quarter ended 3/31/2010	25,553			25,014	539	(5,570)	6,109	3,701	2,408	2,408	—	—	—
Warrants issued in quarter ended 6/30/2010	31,332			30,740	592	(6,122)	6,714	6,083	631	631	—	—	—
Warrants issued in quarter ended 9/30/2010	31,506			20,891	10,615	(44,160)	54,775	1338	53,437	53,437	—	—	—
Total	\$ 790,596	\$(369,642)	\$ 1,071,847	\$ 1,145,292	\$ 14,946	\$(151,117)	\$ 166,063	\$(3,116)	\$ 169,179	\$ 157,580	\$ 11,599	\$ 11,469	\$ 130

**NOTE 8 — RELATED PARTY TRANSACTIONS**

The Company, entered into agreements, in 2008, with our Chairman of the Board, Lawrence Gadbaw, and in 2009 with a board member, Peter Morawetz, to pay Mr. Gadbaw \$25,000 and Dr. Morawetz \$30,000 upon the Company raising \$3 million in new equity. Mr. Gadbaw received 277,778 shares at \$.09 per share in June 2012 as compensation in lieu of the \$25,000 cash for raising \$3 million in new equity. Mr. Gadbaw was paid the balance due under his separation agreement from 2008. This amount was \$46,000 upon signing the agreement in 2008 payable at \$2,000 per month; the payments to Mr. Gadbaw are complete. Mr. Gadbaw also received a warrant for 30,000 shares at \$.15 per share on June 30, 2012 as compensation for service as Chairman. Mr. Gadbaw and Dr. Morawetz have both resigned from the Board in the third quarter of 2013. Both Mr. Gadbaw and Dr. Morawetz received 50,000 shares of common stock each at \$.325 per share; 20,000 of these shares were for compensation from serving as Board members and the remaining 30,000 shares were issued to satisfy previous contractual agreements.

**SKYLINE MEDICAL INC.  
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**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 8 — RELATED PARTY TRANSACTIONS – (continued)**

*Convertible Note Issuances to Dr. Samuel Herschkowitz and SOK Partners, LLC*

On July 23, 2014, the Company also entered into a Securities Purchase Agreement (the “**SOK Securities Purchase Agreement**”) with SOK Partners, LLC, an affiliate of the Company (“**SOK**”), pursuant to which the Company agreed to issue and sell (i) a senior convertible note, in an original principal amount of \$122,195.60 (the “**SOK Note**”), which SOK Note shall be convertible into a certain amount of shares (the “**SOK Conversion Shares**”) of Common Stock, in accordance with the terms of the SOK Note, and (ii) a warrant (the “**SOK Warrant**”) to initially acquire up to 407,318 additional shares of Common Stock (the “**SOK Warrant Shares**”, and collectively with the SOK Note, the SOK Warrant and the SOK Conversion Shares, the “**SOK Securities**”) for an aggregate purchase price of \$100,000 (an approximately 22.2% original issue discount) (the “**SOK Convertible Notes Offering**”).

The SOK Note, the SOK Warrant, the SOK Securities Purchase Agreement and the SOK Registration Rights Agreement contain terms and conditions substantially identical to that of the Investor Note, the Investor Warrant, the Investor Securities Purchase Agreement and the Investor Registration Rights Agreement (as defined below), respectively, which are described in greater detail under “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources”.

On September 11, 2013, both the Herschkowitz Note and the SOK Note (each as defined below in this Note 8) were converted in full by the holders thereof at \$0.014 per share. The principal and interest balance of the Herschkowitz Note of \$314,484 was converted into 22,463,172 shares of common stock. The principal and interest balance of the SOK Note of \$680,444 was converted into 48,603,721 shares of common stock. The collateral that secured these notes was released back to the Company.

The remaining disclosure of this Note 8 provides historical information regarding the Herschkowitz Note, the SOK Note and certain other convertible note issuances.

On March 28, 2012, the Company, entered into a Convertible Note Purchase Agreement, dated as of March 28, 2012 (the “**SOK Purchase Agreement**”) with SOK Partners, LLC (“**SOK Partners**”), and an investment partnership. Josh Komberg, who is a member of the Company’s Board of Directors, and Dr. Samuel Herschkowitz are affiliates of the manager of SOK Partners and Ricardo Koenigsberger, a director, is a holder of membership units of SOK Partners. Pursuant to the SOK Purchase Agreement, the Company issued a 20.0% convertible note due August 2012 in the principal amount of up to \$600,000. Principal and accrued interest on the note is due and payable on August 28, 2012. The Company’s obligations under the note are secured by the grant of a security interest in substantially all tangible and intangible assets of the Company. The SOK Purchase Agreement and the note include customary events of default that include, among other things, non-payment defaults, covenant defaults, inaccuracy of representations and warranties, cross-defaults to other indebtedness and bankruptcy and insolvency defaults. The occurrence of an event of default could result in the acceleration of the Company’s obligations under the note, and interest rate of twenty-four (24%) percent per annum accrues if the note is not paid when due.

On March 28, 2012, the Company received an advance of \$84,657 under the note, including a cash advance of \$60,000 net of a prepayment of interest on the first \$300,000 in advances under the note. The holder of the note is entitled to convert the note into shares of common stock of the Company at an initial conversion price per share of \$0.065 per share, subject to adjustment in the event of (1) certain issuances of common stock or convertible securities at a price lower than the conversion price of the note, and (2) recapitalizations, stock splits, reorganizations and similar events. In addition, the Company is required to issue two installments of an equity bonus to SOK Partners in the form of common stock valued at the rate of \$0.065 per share. In March 2012, the Company issued the first equity bonus to SOK Partners, consisting of 4,615,385 shares of common stock, with a second installment due within five business days after SOK Partners has made aggregate advances under the note of at least \$300,000. In May 2012 the Company issued



**SKYLINE MEDICAL INC.  
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**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 8 — RELATED PARTY TRANSACTIONS – (continued)**

the second installment consisting of 4,615,385 shares of common stock subsequent to SOK Partners surpassing the aggregate advances of \$300,000. Until the maturity date of the note, if the Company obtains financing from any other source without the consent of SOK Partners, then the Company is required to issue additional bonus equity in an amount equal to \$600,000 less the aggregate advances on the note made prior to the breach. The principal balance of the SOK Note was \$357,282 as of December 31, 2012.

As long as any amount payable under the SOK Note remains outstanding, SOK Partners or its designee is entitled to appoint a new member to the Company's Board of Directors, who will be appointed upon request. Mr. Koenigsberger was appointed to the Board by SOK Partners on June 25, 2012.

On March 28, 2012, the Company signed an Amended and Restated Note Purchase Agreement, dated as of December 20, 2011, with Dr. Samuel Herschkowitz (as amended, the "Herschkowitz Purchase Agreement"). Pursuant to the Herschkowitz Purchase Agreement, the Company issued a 20.0% convertible note due June 20, 2012 in the principal amount of \$240,000 for previous advances under the note. The Company's obligations under the note are secured by the grant of a security interest in substantially all tangible and intangible assets of the Company. The Company has previously issued to Dr. Herschkowitz an equity bonus consisting of 1,546,667 shares of common stock. An additional 7,500,000 shares were transferred to Dr. Herschkowitz effective in April 2012, upon the occurrence of an event of default on the note. On August 13, 2012, the Company entered into a settlement and forbearance agreement described below, relating to the defaults under the Herschkowitz Note and other matters.

As long as any amount payable under the Herschkowitz Note remains outstanding, Dr. Herschkowitz or his designee is entitled to appoint a special advisor to the Company's Board of Directors, to be appointed as a member upon request. Pursuant to this authority, Josh Kornberg was appointed to the Board on March 9, 2012. In addition, pursuant to this authority, Mr. Koenigsberger was appointed to the Board on June 25, 2012.

Pursuant to a letter dated April 12, 2012, Dr. Herschkowitz advised the Company of the occurrence of numerous events of default under the terms of the Herschkowitz Note and the Herschkowitz Note Purchase Agreement. As a result of such events of default, Dr. Herschkowitz asserted significant rights as a secured creditor of the Company, including his rights as a secured creditor with a security interest in substantially all assets of the Company. Without a settlement relating to the defaults and other matters, Dr. Herschkowitz could have taken action to levy upon the Company's assets, including patents and other intellectual property.

In addition, the Company and Atlantic Partners Alliance LLC ("APA") were parties to a letter agreement dated March 14, 2012, providing APA and its affiliates (including Dr. Herschkowitz and SOK) with rights to avoid dilution relating to additional issuances of equity securities by the Company through July 14, 2012, evidencing the parties' intent that APA would be provided with significant protection against dilution. This protection was in recognition of APA's investments in the Company involving a high degree of risk and the Company's contemplated need for restructuring its indebtedness, which were anticipated to result, and have resulted, in significant dilution. The parties acknowledged that Dr. Herschkowitz and SOK would not have made their historical cash investments in the Company to the same degree had the dilution protection not been provided, and the investments by these parties have enabled the Company to avoid insolvency. Since the respective dates of the Herschkowitz Note Purchase Agreement and the SOK Note Purchase Agreement, the Company had issued in excess of 16,000,000 shares of common stock to parties other than APA and its affiliates, resulting in significant dilution.

Effective August 15, 2012, the Company entered into a letter agreement with Dr. Herschkowitz, APA and SOK (the "Forbearance Agreement"). Under the Forbearance Agreement, among other things, (i) Dr. Herschkowitz agreed to forbear from asserting his rights as a secured creditor to substantially all of the Company's assets, resulting from the Company's defaults; (ii) the Company issued an aggregate 26.5 million shares of common stock to Dr. Herschkowitz and SOK and adjusted the conversion price of their convertible

**SKYLINE MEDICAL INC.  
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**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 8 — RELATED PARTY TRANSACTIONS – (continued)**

notes to \$0.014 per share from \$0.065 per share, to satisfy the Company's obligations to adjust for dilution; (iii) Dr. Herschkowitz and SOK agreed to extend the maturity of their notes to December 31, 2012; (iv) the Company agreed to pay certain compensation to Dr. Herschkowitz upon the achievement of financial milestones and (v) Dr. Herschkowitz clarified and waived certain of his rights, including the right to interest at a penalty rate upon default.

In the Forbearance Agreement, Dr. Herschkowitz agreed to forbear from exercising any of his rights arising under the Herschkowitz Note or the Herschkowitz Note Purchase Agreement with respect to the existing defaults against the Company, subject to the limitations set forth in the letter agreement and without releasing or waiving any future breach of the letter agreement. He further agreed to forbear from exercising any rights with respect to events of default, security interests in the collateral and other similar remedies against the Company or his interests under the Herschkowitz Note or the Herschkowitz Note Purchase Agreement until the occurrence of an event of default under the Herschkowitz Note: (a) that does not constitute an existing default and (b) occurs and accrues after the date of the letter agreement.

Dr. Herschkowitz and the Company acknowledged that 7.5 million shares of the Company's common stock, constituting the "penalty shares" under the Herschkowitz Note Purchase Agreement, were delivered to Dr. Herschkowitz in April 2012 as provided in the Herschkowitz Note Purchase Agreement upon an event of default. Notwithstanding a provision that would have increased the rate of interest from 20% to 24% upon an event of default, Dr. Herschkowitz agreed that the Company would not pay the increased rate of interest but would accrue interest at 20% until a subsequent event of default.

Under the Forbearance Agreement, the Herschkowitz Note and the SOK Note were amended as follows: (i) the due dates of the notes were extended to December 31, 2012 from the previous due dates of June 20, 2012 and August 28, 2012, respectively; (ii) Dr. Herschkowitz will release his security agreement after payment of all currently outstanding promissory notes to parties other than SOK; and (iii) the Herschkowitz Note was amended to add certain events of default relating to judgments against the Company or other creditors taking action with respect to the collateral. In consideration of the extension additional milestone fees were revised as described below. Pursuant to a Forbearance and Settlement Agreement with these parties dated August 15, 2012, as subsequently amended, the due date of these notes were extended to August 31, 2013.

APA and its affiliates agreed to terminate the letter agreement regarding dilution dated March 14, 2012. In consideration of the various provisions of the letter agreement and in recognition of the understanding of the parties regarding dilution and the agreements of APA and its affiliates to forbear and to extend the due dates of the notes, the Company (i) issued 13,250,000 shares to Dr. Herschkowitz, (ii) issued 13,250,000 shares to SOK, and (iii) the conversion price of the Herschkowitz Note and the SOK Note, respectively was changed to \$0.014 per share from \$0.065 per share.

In the event that the Company consummated the following series of transactions on or prior to June 30, 2013: (i) a merger or similar transaction with a public shell company, (ii) raising between \$2 million and \$4 million through an offering of the securities of the public shell company concurrent with or subsequent to the shell merger and (iii) listing the Company's shares on NASDAQ pursuant to an underwritten offering of the Company's securities resulting in gross proceeds of between \$5 million and \$30 million, then the Company would have to be required to deliver to Dr. Herschkowitz the following compensation: (A) \$75,000 upon consummating the shell merger, (B) \$150,000 upon consummating the qualifying financing round and (C) 3% of the gross proceeds of the NASDAQ underwriting, which payment shall under no circumstances be less than \$200,000 or greater than \$1,000,000. The Company was also required to reimburse Dr. Herschkowitz at his actual out-of-pocket cost for reasonable expenses incurred in connection with the shell transactions, with a maximum limit of \$10,000 for such expenses.

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**NOTES TO CONDENSED FINANCIAL STATEMENTS**

**(Amounts presented at and for the six months ended June 30, 2014 and June 30, 2013 are unaudited)**

**NOTE 8 — RELATED PARTY TRANSACTIONS – (continued)**

In connection with the extension of the due date for the Herschkowitz Note and the SOK Note on March 6, 2013, the milestone fees were revised. The following fees were payable to Dr. Herschkowitz in the event that the Company consummates the following series of transactions on or prior to December 31, 2013: (i) financing raising not less than \$1 million, compensation of \$75,000; (ii) a going private transaction, compensation of \$200,000 or greater and (iii) 3% of the gross proceeds of the NASDAQ underwriting, which payment shall under no circumstances be less than \$200,000 or greater than \$3,000,000. In May 2013 Dr. Herschkowitz received \$75,000 after the Company surpassed raising \$1 million.

As a result of the transactions under the Forbearance Agreement and other investments, Dr. Herschkowitz, SOK and their affiliates currently own shares of common stock and securities representing beneficial ownership of more than 57% of the Company's outstanding common stock, giving such parties significant control over election of the Board of Directors and other matters.

On November 6, 2012, the Company issued and sold convertible promissory notes in the total principal amount of \$156,243 to Dr. Herschkowitz and certain of his assignees. The Company issued to these parties an aggregate 1,562,430 shares of common stock in consideration of placement of the notes. The notes bear interest at a rate of 20% per annum and are secured by a security interest in the Company's accounts receivable, patents and certain patent rights and are convertible into common stock upon certain mergers or other fundamental transactions at a conversion price based on the trading price prior to the transaction. The proceeds from this transaction were used to pay off approximately \$155,000 in principal amount of secured indebtedness. Such notes were converted in April 2013 in to 1,041,622 shares of common stock at \$.10 per share.

In December 2013, the Company received an additional \$300,000 in debt financing from SOK Partners under a non-convertible grid note due February 28, 2014, with 10% interest based on a 365 day year. Dr. Herschkowitz received 10% of the gross proceeds in advance, and the Company received \$250,000 in three tranches in December 2013. In January 2014, the Company received an additional \$20,000 from SOK Partners completing the grid note maximum. Should the company default on the note the interest rate will increase to 20% interest based on a 365 day year. In February 2014, the Company paid \$305,589.04 to SOK Partners in complete payment of the grid note, including interest.

In connection with the sale of the Preferred Shares on February 4, 2014 as described in Note 3, Josh Komberg, our CEO, was one of the Purchasers. Mr. Komberg purchased 19,231 Preferred Shares for a purchase price of \$25,000 and received warrants to purchase 3,846 shares of common stock.

**NOTE 9 — RETIREMENT SAVINGS PLAN**

We have a pre-tax salary reduction/profit-sharing plan under the provisions of Section 401(k) of the Internal Revenue Code, which covers employees meeting certain eligibility requirements. In fiscal 2012, 2013 and again in 2014, we matched 100%, of the employee's contribution up to 4% of their earnings. The employer contribution was \$8,171 and \$12,304 for the three months ending June 30, 2014 and June 30, 2013, respectively, and was \$15,494 and \$18,097, for the six months ending June 30, 2014 and June 30, 2013, respectively.

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**SKYLINE MEDICAL INC.  
(A DEVELOPMENT STAGE COMPANY)**

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**NOTE 10 — COMMITMENTS AND CONTINGENCIES**

On July 17, 2014, Skyline Medical Inc. (the “Company”) and a stockholder entered into a settlement agreement and release (the “Settlement Agreement”) with Marshall Ryan (“Ryan”) and a company related to Ryan (together, the “Plaintiffs”). The settlement relates to a previously disclosed lawsuit by the Plaintiffs initiated in March 2014. Ryan is an engineer who previously worked with the Company on design of certain of the Company’s products. The lawsuit alleged among other things, breach of a 2008 consulting agreement, a 2006 manufacturing agreement and a 2006 supply agreement among the Plaintiffs and the Company, various claims of fraud and negligent misrepresentation, and breach of the duty of good faith and fair dealing.

Under the Settlement Agreement, the parties have agreed that the lawsuit will be dismissed. The Company has agreed to pay Ryan an aggregate of \$500,000 in various cash installments through April 25, 2015, which amount includes \$200,000 in installments that are payable during the remainder of 2014. The Settlement Agreement, among other things, extinguishes any prior claims of Plaintiffs for royalties or other alleged rights to payments under their prior agreements with the Company. Payment of the outstanding balance under the Settlement Agreement will be accelerated if the Company raises \$2 million or more of gross dollars in a single funding round or raises aggregate funding of \$4 million of gross dollars on or before April 10, 2015. If the Company defaults on the required cash payments and fails to cure as provided in the Settlement Agreement, then Ryan will have the option to either sue Skyline to enforce the Settlement Agreement or rescind the Settlement Agreement, including returning all payments previously made thereunder.

The Settlement Agreement also contains mutual releases covering claims other than a breach of the Settlement Agreement. In the Settlement Agreement, Ryan fully, unconditionally and irrevocably affirms and ratifies the Company’s rights to Ryan’s prior patent assignments, and disclaims any right, title or interest in the Company’s Streamway product including any claims to royalties both past and future. In addition, the parties confirmed that the patents related to the Streamway product belong exclusively to Skyline and remain in full force and effect.

**NOTE 11 — SUPPLEMENTAL CASH FLOW DATA**

Cash payments for interest were \$3,468 and \$15,522 for the three months ended June 30, 2014 and June 30, 2013, and \$21,606 and \$41,930 for the six months ended June 30, 2014 and June 30, 2013.

**Prospectus**  
**SKYLINE MEDICAL INC.**  
**78,709,975 shares of Common Stock**

**The date of this prospectus is September 8, 2014**

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