UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2018

Commission File Number 001-37525

NUVECTRA CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware	**30-0513847**
(State of Incorporation)	**(I.R.S. Employer Identification No.)**

5830 Granite Parkway, Suite 1100
Plano, Texas 75024
(Address of principal executive offices) (Zip code)

(214) 474-3103
(Registrant's telephone number, including area code)

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

Indicate by checkmark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

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

Large accelerated filer ☐	Accelerated filer ☒
Non-accelerated filer ☐	Smaller reporting company ☒
	Emerging growth company ☒

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

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

As of October 19, 2018, shares outstanding of the Company's common stock, $0.001 par value per share, totaled 17,608,955.

Nuvectra Corporation
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As of and for the Quarterly Period Ended September 30, 2018

PART I—FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

NUVECTRA CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS—Unaudited
(in thousands except share and per share data)

	As of	
	September 30, 2018	**December 31, 2017**
ASSETS		
Current assets:		
Cash and cash equivalents	$ 101,858	$ 28,165
Trade accounts receivable, net of allowance for doubtful accounts of $637 and $417 in 2018 and 2017, respectively	11,394	10,875
Inventories	4,476	4,978
Prepaid expenses and other current assets	1,420	1,011
Total current assets	119,148	45,029
Property, plant and equipment, net	5,655	6,219
Intangible assets, net	1,204	1,428
Goodwill	38,182	38,182
Other long-term assets	—	245
Total assets	$ 164,189	$ 91,103
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 230	$ 2,043
Accrued liabilities	9,977	8,827
Accrued compensation	5,409	4,392
Short-term debt	—	789
Total current liabilities	15,616	16,051
Other long-term liabilities	516	993
Long-term debt, net	43,824	25,886
Total liabilities	59,956	42,930
Commitments and contingencies (Note 8)		
Stockholders' equity:		
Common stock, $0.001 par value, 100,000,000 shares authorized; 17,573,669 and 10,849,385 shares issued and outstanding in 2018 and 2017, respectively	18	11
Additional paid-in capital	217,329	125,999
Accumulated other comprehensive loss	—	(1)
Accumulated deficit	(113,114)	(77,836)
Total stockholders' equity	104,233	48,173
Total liabilities and stockholders' equity	$ 164,189	$ 91,103

The accompanying notes are an integral part of these condensed consolidated financial statements.

NUVECTRA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE LOSS — Unaudited
(in thousands except per share data)

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Sales:				
Product	$ 13,813	$ 7,431	$ 36,686	$ 18,684
Service	403	186	1,253	1,196
Total sales	14,216	7,617	37,939	19,880
Cost of sales:				
Product	6,361	4,019	16,577	9,393
Service	236	132	1,064	708
Total cost of sales	6,597	4,151	17,641	10,101
Gross profit	7,619	3,466	20,298	9,779
Operating expenses:				
Selling, general and administrative expenses	15,221	11,358	40,814	33,349
Research, development and engineering costs, net	4,385	3,136	11,891	10,730
Total operating expenses	19,606	14,494	52,705	44,079
Operating loss	(11,987)	(11,028)	(32,407)	(34,300)
Interest expense, net	986	422	2,772	1,190
Other expense, net	11	179	88	499
Loss before provision for income taxes	(12,984)	(11,629)	(35,267)	(35,989)
Provision for income taxes	(17)	9	11	9
Net loss	$ (12,967)	$ (11,638)	$ (35,278)	$ (35,998)
Other comprehensive gain:				
Unrealized holding gain on investments arising during period	—	—	1	2
Other comprehensive gain	—	—	1	2
Comprehensive loss	$ (12,967)	$ (11,638)	$ (35,277)	$ (35,996)
Basic and diluted net loss per share	$ (0.87)	$ (1.09)	$ (2.55)	$ (3.43)
Basic and diluted weighted average shares outstanding	14,840	10,697	13,852	10,497

The accompanying notes are an integral part of these condensed consolidated financial statements.

NUVECTRA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS—Unaudited
(in thousands)

	Nine Months Ended	
	September 30, 2018	**September 30, 2017**
Cash flows from operating activities:		
Net loss	$ (35,278)	$ (35,998)
Adjustments to reconcile net loss to net cash used in operating activities:		
Provision for uncollectible accounts	287	419
Write-downs of excess and obsolete inventories	753	349
Depreciation and amortization	1,374	1,172
Debt related amortization included in interest expense	798	491
Stock-based compensation	1,908	1,711
Changes in operating assets and liabilities:		
Trade accounts receivable	(806)	(3,917)
Inventories	(251)	1,874
Prepaid expenses and other current assets	(409)	(758)
Accounts payable and other current liabilities	(837)	(5,870)
Accrued compensation	1,017	1,304
Other long-term liabilities	35	(24)
Net cash used in operating activities	(31,409)	(39,247)
Cash flows from investing activities:		
Acquisition of property, plant and equipment	(533)	(875)
Net cash used in investing activities	(533)	(875)
Cash flows from financing activities:		
Borrowings under credit facility, net	16,711	12,500
Proceeds from the sale of common stock	88,816	—
Payments of financing costs related to issuance of common stock	(283)	—
Proceeds from the exercise of stock options	397	1,322
Payment of debt issuance costs and other financing activities	(6)	121
Net cash provided by financing activities	105,635	13,943
Net increase (decrease) in cash and cash equivalents	73,693	(26,179)
Cash and cash equivalents, beginning of period	28,165	63,710
Cash and cash equivalents, end of period	$ 101,858	$ 37,531
Supplemental Disclosure of Cash Flow Information:		
Income taxes paid	$ 16	$ 9
Interest paid	2,086	1,579
Acquisition of property, plant and equipment accrued not paid	53	(8)
Financing costs related to the issuance of common stock accrued not paid	122	—

The accompanying notes are an integral part of these condensed consolidated financial statements.

NUVECTRA CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY — Unaudited
(in thousands)

	Common Stock		Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Amount				
At December 31, 2017	10,849	$ 11	$ 125,999	$ (77,836)	$ (1)	$ 48,173
Issuance of common stock, net of issuance costs of $6,617	6,498	6	88,404	-	-	88,410
Issuance of common stock warrants	-	-	621	-	-	621
Option exercises	53	-	397	-	-	397
Restricted stock issued, net of stock forfeited	174	1	-	-	-	1
Stock-based compensation	-	-	1,908	-	-	1,908
Unrealized holding period gain	-	-	-	-	1	1
Net loss	-	-	-	(35,278)	-	(35,278)
At September 30, 2018	17,574	$ 18	$ 217,329	$ (113,114)	$ -	$ 104,233

The accompanying notes are an integral part of these condensed consolidated financial statements.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations – Nuvectra Corporation, together with its wholly-owned subsidiaries (i) Algostim, LLC ("Algostim"), (ii) PelviStim LLC ("PelviStim"), and (iii) NeuroNexus Technologies, Inc. ("NeuroNexus") (collectively "Nuvectra" or the "Company"), is a neurostimulation company committed to helping physicians improve the lives of people with chronic conditions. The Algovita® Spinal Cord Stimulation ("SCS") System ("Algovita") is the Company's first commercial offering and is Conformité Européene ("CE") marked and United States Food & Drug Administration ("FDA") approved for the treatment of chronic pain of the trunk and/or limbs. Nuvectra's innovative technology platform also has capabilities under development to support other neurological indications such as sacral neuromodulation ("SNM") for the treatment of overactive bladder and deep brain stimulation ("DBS") for the treatment of Parkinson's disease and Essential Tremor. In addition, the Company's NeuroNexus subsidiary designs, manufactures and markets neural-interface technologies for the neuroscience clinical research market.

In March 2016, the Company was formed as a separate public company as a result of a spin-off (the "Spin-off") from Integer Holdings Corporation ("Integer").

Basis of Presentation – The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information (Accounting Standards Codification ("ASC") 270, *Interim Reporting*) and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information necessary for a full presentation of financial position, results of operations, and cash flows in conformity with accounting principles generally accepted in the United States of America. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole. In the opinion of management, the condensed consolidated financial statements reflect all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the results of Nuvectra for the periods presented.

Liquidity and Capital Resources – The Company has incurred significant net losses and negative cash flows from operations since inception and expects to incur additional net losses for the foreseeable future.

Based on its current plans and expectations, the Company estimates that its cash on hand, which includes proceeds from the Company's follow-on common stock offerings completed in the first and third quarters of 2018, credit facility draw-downs, and cash generated from sales, should meet its cash needs for at least the next twelve months.

On September 14, 2018, pursuant to a second underwritten shelf takedown, with Piper Jaffray & Co. serving as representative of the several underwriters, the Company sold 3,248,750 shares of its common stock and received net proceeds of approximately $64.6 million, after deducting underwriting discounts and commissions of approximately $4.1 million and other expenses of approximately $0.3 million.

The Company periodically evaluates its liquidity requirements, alternative uses of capital, capital needs and available resources. As a result of this process, the Company has in the past sought, and may in the future seek, to explore strategic alternatives to finance its business plan, including but not limited to, a public offering of its common stock, private equity or debt financings, sale of non-strategic assets, or other sources, such as strategic partnerships. The Company has elected and may continue to elect to make near-term decisions, including engaging in various capital generating initiatives, to provide additional liquidity. If the Company is unable to raise additional funds when needed, it may be required to delay, reduce, or terminate some or all of its development plans. The Company is also focusing on increasing the sales of its products to generate cash flow to fund its operations. However, there can be no assurance that the Company will be successful in its plans described above or in attracting alternative debt or equity financing.

Use of Estimates – The preparation of financial statements in conformity with U.S. GAAP 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 reported amounts of sales and expenses during the reporting period. Actual results could differ materially from those estimates. Significant items subject to such estimates and assumptions include inventories, tangible and intangible asset valuations, revenue, stock-based compensation, warrants, certain accruals, and income tax accounts.

Inventories – The value of inventories, comprised solely of finished goods, are stated at the lesser of net realizable value or cost, determined using the first-in, first-out ("FIFO") method. To value inventory, management must estimate excess or obsolete inventory, as well as inventory that is not of saleable quality. This valuation involves an inherent level of risk and uncertainty due to unpredictability of trends in the industry and customer demand for the Company's products. In assessing the ultimate realization of inventories, management must make judgments as to future demand requirements and compare that with the current or committed inventory levels. Reserve requirements generally increase as demand decreases due to market conditions and technological and product life-cycle changes.

Write-downs of excess and obsolete inventories were $0.4 million and $0.1 million in the third quarter of 2018 and 2017, respectively. Future events and variations in valuation methods or assumptions may cause significant fluctuations in this estimate and could have a material impact on the Company's results.

Goodwill Valuation – The Company tests its goodwill balances for impairment on December 31, or more frequently if certain indicators are present or changes in circumstances suggest that impairment may exist. When evaluating goodwill for impairment, the Company compares the fair value of a reporting unit with its carrying amount. The Company recognizes an impairment charge for the amount by which the carrying amount of a reporting unit, including goodwill, exceeds its fair value; however, the loss recognized would not exceed the total amount of goodwill allocated to the reporting unit. The Company first assesses qualitative factors to determine whether it is necessary to perform the quantitative goodwill impairment test. If determined to be necessary, the quantitative impairment test is used to identify goodwill impairment and measure the amount for a goodwill impairment to be recognized, if any. In addition, the Company also performs impairment tests of its other long-lived assets in accordance with ASC 360-10, *Impairment and Disposal of Long-Lived Assets*, when indicators of impairment exist. The Company completed its annual impairment test of goodwill as of December 31, 2017 and the Company determined that it was more likely than not that the fair value of both reporting units exceeded their carrying value. The Company did not identify any indicators of impairment that required an impairment test in the first nine months of 2018 for its Nuvectra reporting unit. The Company did not identify any indicators of impairment that required an impairment test in the second or third quarters of 2018 for its NeuroNexus reporting unit. In the first quarter of 2018, the Company evaluated strategic alternatives with respect to its NeuroNexus reporting unit which triggered an interim impairment test. Upon completing the goodwill impairment test for NeuroNexus, the Company determined that its fair value exceeded its carrying value.

Impairment of Long-Lived Assets – The Company assesses the impairment of definite-lived long-lived assets or asset groups when events or changes in circumstances indicate that the carrying value may not be recoverable. Factors that are considered in deciding when to perform an impairment review include: a significant decrease in the market price of the asset or asset group; a significant change in the extent or manner in which a long-lived asset or asset group is being used or in its physical condition; a significant change in legal factors or in the business climate that could affect the value of a long-lived asset or asset group, including an action or assessment by a regulator; an accumulation of costs significantly in excess of the amount originally expected for the acquisition or construction; a current-period operating or cash flow loss combined with a history of operating or cash flow losses or a projection or forecast that demonstrates continuing losses associated with the use of a long-lived asset or asset group; or a current expectation that, more likely than not, a long-lived asset or asset group will be sold or otherwise disposed of significantly before the end of its previously estimated useful life. The term more likely than not refers to a level of likelihood that is more than 50 percent.

Potential recoverability is measured by comparing the carrying amount of the asset or asset group to its related total future undiscounted cash flows. The projected cash flows for each asset or asset group considers multiple factors, including current revenue from existing customers, proceeds from the sale of the asset or asset group and expected profit margins giving consideration to historical and expected margins. If the carrying value is not recoverable, the asset or asset group is considered to be impaired. Impairment is measured by comparing the asset or asset group's carrying amount to its fair value. When it is determined that useful lives of assets are shorter than originally estimated, and no impairment is present, the rate of depreciation is accelerated in order to fully depreciate the assets over their new shorter useful lives. The Company did not identify any indicators of impairment in the first nine months of 2018 for the Nuvectra asset group or in the second or third quarters of 2018 for the NeuroNexus asset group; however, as noted above, the Company performed an interim impairment test in the first quarter of 2018 for the NeuroNexus asset group and determined the undiscounted cash flows exceeded the carrying amounts of long-lived assets.

Concentration of Credit Risk – Financial instruments that potentially subject the Company to concentration of credit risk consist principally of trade accounts receivable owed to the Company by its customers. The Company performs on-going credit evaluations of its customers. No customers individually accounted for more than 10% of the Company's consolidated revenues in the nine months ended September 30, 2018 or 2017. No customers individually accounted for more than 10% of the Company's accounts receivable at September 30, 2018 or December 31, 2017. Additionally, the Company maintains cash deposits with major banks, which from time to time may exceed insured limits. The Company performs on-going credit evaluations of its banks. See Note 11 "Business Segments, Geographic and Concentration Risk Information" for additional information.

Warranty Reserve – The Company offers a warranty on certain of its products and maintains a warranty reserve, as a component of other current liabilities, for any potential claims. The Company estimates its warranty reserve based upon an analysis of all identified or expected claims and an estimate of the cost to resolve those claims. Factors that affect the Company's warranty liability include the number of units sold, historical and anticipated rates of warranty claims, and differences between actual and expected warranty costs per claim. The Company periodically assesses the adequacy of its warranty liability and adjusts the amount as necessary.

Subsequent Events – The Company considers events or transactions that occur after the balance sheet date but prior to the issuance of the financial statements to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure.

2. REVENUE FROM CONTRACTS WITH CUSTOMERS

The Company adopted ASC 606, *Revenue From Contracts With Customers* ("ASC 606"), on January 1, 2018 using the modified retrospective method for all contracts not completed as of the date of adoption. The adoption of ASC 606 did not have a material impact on the Company's consolidated financial statements. The reported results for 2018 reflect the application of ASC 606 guidance while the reported results for 2017 were prepared under the guidance of ASC 605, *Revenue Recognition* ("ASC 605"), which is also referred to herein as "previous U.S. GAAP." The adoption of ASC 606 represents a change in accounting principle that will more closely align revenue recognition with the delivery of the Company's goods and services and will provide financial statement readers with enhanced disclosures. In accordance with ASC 606, revenue is recognized when a customer obtains control of promised goods or services. The amount of revenue recognized reflects the consideration to which the Company expects to be entitled to receive in exchange for these goods or services, and excludes any sales incentives or taxes collected from a customer which are subsequently remitted to government authorities. To achieve this core principle, the Company applies the following five steps:

1) *Identify the contract(s) with a customer* - A contract with a customer exists when (i) the Company enters into an enforceable contract with a customer that defines each party's rights regarding the goods or services to be transferred and identifies the payment terms related to those goods or services, (ii) the contract has commercial substance and, (iii) the Company determines that collection of substantially all consideration for goods or services that are transferred is probable based on the customer's intent and ability to pay the promised consideration.

2) *Identify the performance obligations in the contract* - Performance obligations promised in a contract are identified based on the goods or services that will be transferred to the customer that are both capable of being distinct, whereby the customer can benefit from the good or service either on its own or together with other resources that are readily available from third parties or from the Company, and are distinct in the context of the contract, whereby the transfer of the goods or services is separately identifiable from other promises in the contract. To the extent a contract includes multiple promised goods or services, the Company must apply judgment to determine whether promised goods or services are capable of being distinct and distinct in the context of the contract. If these criteria are not met the promised goods or services are accounted for as a combined performance obligation.

3) *Determine the transaction price* - The transaction price is determined based on the consideration to which the Company will be entitled in exchange for transferring goods or services to the customer. To the extent the transaction price includes variable consideration, the Company estimates the amount of variable consideration that should be included in the transaction price utilizing either the expected value method or the most likely amount method depending on the nature of the variable consideration. Variable consideration is included in the transaction price if, in the Company's judgment, it is probable that a significant future reversal of cumulative revenue under the contract will not occur. Determining the transaction price requires significant judgment, which is discussed by revenue category in further detail below.

4) *Allocate the transaction price to the performance obligations in the contract* - If the contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. Contracts that contain multiple performance obligations require an allocation of the transaction price to each performance obligation based on a relative standalone selling price ("SSP") basis unless the transaction price is variable and meets the criteria to be allocated entirely to a performance obligation or to a distinct good or service that forms part of a single performance obligation. The Company determines SSP based on the price at which the performance obligation is sold separately. If the SSP is not observable through past transactions, the Company estimates the SSP taking into account available information such as market conditions and internally approved pricing guidelines related to the performance obligations.

5) *Recognize revenue when (or as) the Company satisfies a performance obligation* - The Company satisfies performance obligations either over time or at a point in time as discussed in further detail below. Revenue is recognized at the time the related performance obligation is satisfied by transferring a promised good or service to a customer.

Disaggregated Revenue - Revenue Streams & Timing of Revenue Recognition

The Company's most significant revenue streams include (i) product sales, consisting of Nuvectra's Algovita and NeuroNexus's neural interface systems and (ii) development and engineering service revenue. Following is a description of the nature of the Company's disaggregated revenue streams. Also see Note 11, "Business Segments, Geographic and Concentration Risk Information" for further disaggregation of revenue by reportable segment.

Product Sales

The Company's product sales revenues include sales of Algovita and neural interface systems and components to the neuroscience and clinical markets. Contracts may include one or more systems or components, each is determined to be a distinct performance obligation. Product revenue was $36.7 million for the nine months ended September 30, 2018.

Algovita – Generally, Algovita product sales are made through the Company's trained personnel when the Company has the obligation to perform the initial programming and stimulation which occurs on the same day as the trial or permanent procedure. For these customers, the products and the programming and stimulation services are not separately distinct but rather are a combined performance obligation for which revenue is recognized upon completion of the procedure. In cases where the customer has a Clinician Programmer and has undergone the requisite training in order to perform the programming and stimulation services, the Company recognizes revenue upon shipment when control passes to the customer. Similarly, when the Company sells through distributors or ships product directly to the end user and has no additional obligations, revenue is recognized at the time of shipment when control passes to the customer. For the remaining sales that are sent from the Company's distribution center directly to hospitals and medical facilities, where product is ordered in advance of an implantation procedure and a valid purchase order has been received, the Company defers revenue until all programming and stimulation obligations are fulfilled.

Neural interface systems and components – Each component is a separate distinct performance obligation. The customer obtains control of the individual components upon shipment, and therefore revenue is recognized at that point in time.

Shipping and handling costs – Costs associated with outbound freight after control over a product has transferred to a customer are accounted for as a fulfillment cost and are included in cost of revenues.

Warranty – The Company provides a standard warranty against defects but does not provide a general right of return.

Significant judgments – The Company's contracts with customers often include promises to transfer multiple products to a customer. Determining whether the promises are considered distinct performance obligations that should be accounted for separately versus together may require significant judgment. Judgment is required to determine the SSP for each distinct performance obligation. The Company determines SSP based on the price at which the performance obligation is sold separately. If the SSP is not observable through past transactions, the Company estimates the SSP taking into account available information such as market conditions and internally approved pricing guidelines related to the performance obligations.

Development and Engineering Service Revenue

The Company's development services are typically provided on a fixed-fee basis. Service revenue is recognized over time as the services are performed using an input method, on a cost-to-cost basis. In 2017 and 2018, the Company had one contract that generated development and engineering services revenue with Aleva Neurotherapeutics S.A. ("Aleva"). Under this contract, the Company is leveraging its neurostimulation technology platform in its performance of services in the development of a DBS system for Aleva to treat Parkinson's disease and Essential Tremor. If successful, the Company will provide Aleva a royalty bearing distribution license for commercialization by Aleva. The Company concluded that the licenses and the development services were not separately distinct given the proprietary nature of the Company's technology. As such, the combined performance obligation will be recognized over time as costs are incurred. The transaction price includes a fixed fee, payable monthly based on the progress completion in satisfying the performance obligations in that month, royalties for intellectual property licenses on future sales of the licensed technology, and non-cash consideration for the customer commitment to issue the Company a common stock warrant upon CE Mark approval in Europe. When the Company receives consideration in the form of royalties, the Company will estimate the royalty revenue and recognize the royalty revenue when a sale by the customer occurs. The non-cash consideration is a form of variable consideration which must be estimated at contract inception and therefore requires significant judgment. See the "Significant Judgments" section below for further discussion. Services revenue recognized over time was $1.3 million for the first nine months of 2018. The Company is still performing services and the client has yet to receive CE Mark approval and therefore, the Company has not yet billed or recognized any royalty revenue to date.

Significant judgments – The Company's contracts with customers often include promises to transfer multiple products to a customer. Determining whether the promises are considered distinct performance obligations that should be accounted for separately versus together may require significant judgment, specifically for development and engineering service revenues. Once the performance obligations are identified, the Company determines the transaction price, which includes estimating the amount of variable consideration to be included in the transaction price, if any. The Company then allocates the transaction price to each performance obligation in the contract based on a relative stand-alone selling price method. The corresponding revenues are recognized as the related performance obligations are satisfied as discussed above. Judgment is required to determine the SSP for each distinct performance obligation. The Company determines SSP based on the price at which the performance obligation is sold separately. If the SSP is not observable through past transactions, the Company estimates the SSP taking into account available information such as market conditions and internally approved pricing guidelines related to the performance obligations.

The Company's service revenue is recognized over time using an input method based on costs incurred. As such, estimating the total costs to be incurred and progress to completion on the contract requires significant judgment. Management uses historical experience, project plans and an assessment of the risks and uncertainties inherent in the arrangements to establish these estimates. Various uncertainties may or may not be within the Company's control.

Transaction Price Allocated to Future Performance Obligations

ASC 606 requires disclosure of the aggregate amount of transaction price that is allocated to performance obligations that have not yet been satisfied or are partially satisfied as of the balance sheet date. The Company has elected to apply certain optional exemptions that limit this requirement to exclude contracts which are expected to be satisfied within one year as well as the potential royalty license revenue. After considering these exemptions, the Company's service revenue contract with Aleva is subject to this disclosure for the portion of the transaction price not subject to royalties. As of September 30, 2018, the estimated revenue expected to be recognized in the future related to this contract totals $1.1 million and is expected to be recognized over the following 6 to 12 months.

Contract Balances

Timing of revenue recognition may differ from the timing of invoicing to customers. The Company records a receivable when revenue is recognized prior to invoicing when it has an enforceable right to payment and a contract asset when the Company does not. If invoicing occurs prior to revenue recognition, the unearned revenue is presented on the condensed consolidated balance sheet as a contract liability, referred to as deferred revenue. When invoicing occurs after revenue recognition, earned revenue is presented on the condensed consolidated balance sheet as a contract asset, referred to as unbilled receivables. The Company's standard payment terms are 30 days.

Revenue recognized during the first nine months of 2018 from amounts included in deferred revenue at the beginning of the period was $0.1 million, which was related to product sales revenue. There was no revenue recognized during the first nine months of 2018 from performance obligations satisfied or partially satisfied in previous periods. During the nine months ended September 30, 2018, there were no contract assets reclassified to receivables as a result of the right to the transaction consideration becoming unconditional.

Costs to Obtain and Fulfill a Contract

The Company has elected to apply the practical expedient and recognize the incremental costs of obtaining contracts as an expense when incurred if the amortization period of the assets that the Company otherwise would have recognized is one year or less, and therefore, the Company recognizes an asset for the incremental costs of obtaining a contract with a customer if the expected period of benefit of those costs is longer than one year. As of January 1, 2018 and September 30, 2018, all contract acquisition costs have been expensed as incurred as the period of benefit is less than one year.

Certain NeuroNexus contracts may include pre-production activities, design work for custom products. The Company's policy is to capitalize incremental costs incurred to fulfill its contracts that (i) relate directly to the contract (ii) are expected to generate resources that will be used to satisfy the Company's performance obligation under the contract and (iii) are expected to be recovered through revenue generated under the contract. These costs have historically been immaterial. Accordingly, there are no capitalized fulfillment costs as of January 1, 2018 or September 30, 2018.

3. INTANGIBLE ASSETS

Intangible assets are comprised of the following (in thousands):

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
At September 30, 2018			
Technology and patents	$ 1,058	$ (729)	$ 329
Customer lists	1,869	(994)	875
Total intangible assets	$ 2,927	$ (1,723)	$ 1,204
At December 31, 2017			
Technology and patents	$ 1,058	$ (624)	$ 434
Customer lists	1,869	(875)	994
Total intangible assets	$ 2,927	$ (1,499)	$ 1,428

Aggregate intangible asset amortization expense is classified as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Cost of sales	$ 34	$ 32	$ 104	$ 95
Selling, general and administrative expenses	40	39	120	120
Total intangible asset amortization expense	$ 74	$ 71	$ 224	$ 215

Estimated future intangible asset amortization expense based on the current carrying value is as follows (in thousands):

	Estimated Amortization Expense
Remainder of 2018	$ 74
2019	293
2020	209
2021	194
2022	108
Thereafter	326
Total estimated amortization expense	$ 1,204

4. ACCRUED LIABILITIES

Accrued liabilities consisted of the following (in thousands):

	At	
	September 30, 2018	December 31, 2017
Inventory purchases	$ 6,418	$ 5,825
Research and development	575	164
Warranty reserve	454	195
Regulatory, clinical and quality	426	358
Sales and marketing	379	321
Interest	305	199
Legal	299	358
Deferred revenue	187	335
Sales and use tax	154	145
Information technology	-	114
Operations engagement fee	-	200
Insurance	-	127
Accrued other	780	486
Total accrued liabilities	$ 9,977	$ 8,827

5. EMPLOYEE BENEFIT PLANS

Nuvectra Corporation 2016 Equity Incentive Plan – The Nuvectra Corporation 2016 Equity Incentive Plan (the "2016 Equity Plan") provides that the Compensation and Organization Committee of the Company's Board of Directors (the "Compensation Committee") may award eligible participants, as it may determine from time to time, the following types of awards: stock options, stock appreciation rights, restricted stock, restricted stock units and stock bonuses. Subject to adjustment provisions in the 2016 Equity Plan, the total number of shares of Nuvectra common stock reserved for issuance under the 2016 Equity Plan is 1,975,018.

During the nine months ended September 30, 2018, the Compensation Committee granted equity awards aggregating 385,386 shares of common stock under the 2016 Equity Plan in the form of both restricted stock units and non-qualified stock options to its directors and certain officers and key employees. Compensation cost related to the 2016 Equity Plan for the three and nine months ended September 30, 2018 was approximately $0.7 million and $1.9 million, respectively.

During the nine months ended September 30, 2017, the Compensation Committee granted equity awards aggregating 546,146 shares of common stock under the 2016 Equity Plan in the form of both restricted stock units and non-qualified stock options to its directors and certain officers and key employees. Compensation cost related to the 2016 Equity Plan for the three and nine months ended September 30, 2017 was approximately $0.6 million and $1.5 million, respectively.

Stock-Based Compensation – Certain of the Company's employees participated in the stock-based compensation programs of Integer and prior to the Spin-off received awards of time-based stock options and time- and performance-based restricted stock units, which typically vest over a three-year period and are settled in shares of Integer common stock. The stock-based payment compensation expense includes the compensation expense directly attributable to Nuvectra employees from these Integer equity incentives. In addition, certain incentive awards that were originally granted under an Integer equity incentive award plan adjusted into an incentive award of Nuvectra common stock at the time of the Spin-off. There was no compensation cost related to these equity incentives for the three and nine months ended September 30, 2018. Compensation cost related to these Integer equity incentives was approximately $0.04 million and $0.2 million for the three and nine months ended September 30, 2017, respectively.

The components and classification of stock-based compensation expense were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Stock options	$ 263	$ 227	$ 764	$ 637
Restricted stock and restricted stock units	391	379	1,144	1,074
Total stock-based compensation expense	$ 654	$ 606	$ 1,908	$ 1,711

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Selling, general and administrative expenses	$ 591	$ 507	$ 1,652	$ 1,491
Research, development and engineering costs, net	63	99	256	220
Total stock-based compensation expense	$ 654	$ 606	$ 1,908	$ 1,711

The fair value of each stock option grant is estimated on the date of grant using the Black-Scholes option-pricing model with weighted-average assumptions based on the grant date. The weighted average fair value and assumptions used to value options granted under the 2016 Equity Plan were as follows:

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Weighted average fair value	$13.56	$7.85	$9.32	$3.63
Risk-free interest rate	2.81%	2.01%	2.67%	2.06%
Expected volatility	65%	65%	65%	55%
Holding period (in years)	6	6	6	6
Expected dividend yield	—%	—%	—%	—%

The following table summarizes the stock option activity during the first nine months of 2018:

	Number of Time-Vested Stock Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2017	870,820	$ 6.78		
Granted	238,146	15.40		
Exercised	(53,002)	7.51		
Forfeited or expired	(84,247)	9.17		
Outstanding at September 30, 2018	971,717	$ 8.64	7.18	$ 12,977
Exercisable at September 30, 2018	566,522	$ 6.59	5.94	$ 8,717

The Company received proceeds totaling approximately $0.4 million upon the exercise of 53,002 stock options during the first nine months of 2018.

The following table summarizes the restricted stock and restricted stock unit activity during the first nine months of 2018:

	Time-Vested Activity	Weighted Average Fair Value
Non-vested at December 31, 2017	429,005	$ 6.88
Granted	147,240	16.83
Vested	(174,959)	14.58
Forfeited	(76,756)	8.07
Non-vested at September 30, 2018	324,530	$ 11.04

Nuvectra Bonus Plan – The terms of the Nuvectra Corporation Bonus Plan (the "Bonus Plan") provide for both annual discretionary cash contribution-based bonuses and cash performance-based bonuses based upon Nuvectra's company-wide performance measures and, for certain employees, individual performance measures that are set by Nuvectra's executive management and, in some instances, members of the Board of Directors. Compensation cost related to the Bonus Plan for the three and nine months ended September 30, 2018 was approximately $0.7 million and $1.9 million, respectively. Compensation cost related to the Bonus Plan for the three and nine months ended September 30, 2017 was approximately $0.1 million and $1.4 million, respectively.

Defined Contribution Plans – The Company sponsors a defined contribution Section 401(k) plan for its employees. The plan provides for the deferral of employee compensation under Section 401(k) of the Internal Revenue Code of 1986, as amended ("Section 401(k)"), and a discretionary match by the Company. For each of the three and nine months ended September 30, 2018 this match was 25% per dollar of participant deferral, up to 6% of the total compensation for each participant. Direct costs related to this defined contribution plan were $0.1 million and $0.2 million for the three and nine months ended September 30, 2018, respectively. Direct costs related to this defined contribution plan were $0.07 million and $0.2 million for the three and nine months ended September 30, 2017, respectively.

6. DEBT

Long-term debt is comprised of the following (in thousands):

	At	
	September 30, 2018	December 31, 2017
Term loan	$ 48,488	$ 29,631
Deferred financing fees	(799)	(962)
Discount on debt	(3,865)	(1,994)
Total debt	43,824	26,675
Less current portion of long-term debt	-	789
Total long-term debt	$ 43,824	$ 25,886

Credit Facility – The Company has a credit facility, originally entered into and funded in March 2016 and subsequently amended in February 2017 and February 2018 (the "Credit Facility"), that consists of term loan facilities in an aggregate maximum principal amount of $45 million. The term loan facilities are comprised of (i) a $27.5 million Term Loan A Commitment, which replaced the previously-existing $27.5 million term loan, (ii) a $12.5 million Term Loan B Commitment, which was funded in February 2018, and (iii) a $5 million Term Loan C Commitment, which was funded in September 2018.

The Term Loans bear interest at a floating rate equal to the prime rate plus 4.15%, with a floor of 8.65%. At September 30, 2018 the interest rate on borrowings under the Term Loans was 9.15%. The Company pays monthly accrued interest only on the Term Loans through March 2020 and thereafter the Company will pay monthly accrued interest on the Term Loans plus equal payments of principal for 30 months. At the maturity of the Term Loans, on September 1, 2022, all principal on the Term Loans then outstanding, plus an additional 7.75% of the funded loan amounts (the "Final Payment"), will be due and payable. This Final Payment has been treated as an in-substance discount and is being amortized using the straight-line method over the life of the Term Loans.

In connection with the February 2018 amendment to the Credit Facility, Term Loan A and Term Loan B were funded for aggregate gross proceeds of $40 million, of which $27.5 million was applied to repay the outstanding principal balance of the previously-existing term loans. The Company determined that it met the criteria to be accounted for as a modification in which any unamortized debt discount is amortized over the remaining term of the exchanged or modified debt. The Company also paid a fee of approximately $0.8 million in connection with the February 2018 amendment, which was recorded as a discount on long-term debt to be amortized over the term of Term Loan B. If any Term Loans are prepaid prior to their scheduled maturity, the Company must pay, in addition to the Final Payment, a prepayment fee equal to $1.3 million plus 3% of the prepaid principal if paid prior to February 2019, 2% of the prepaid principal if paid prior to February 2020, and 1% of the prepaid principal if paid thereafter.

The Term Loans are secured by a first priority lien on substantially all of the assets of the Company, including, without limitation, all cash, deposit accounts, accounts receivable, equipment, inventory, contract rights, the ownership interests of its subsidiaries and the Company's real property located in Blaine, Minnesota, but excluding all intellectual property of the Company (other than accounts receivable and proceeds of intellectual property). The Company's intellectual property is subject to a negative pledge. The Company must maintain its primary operating and investment accounts with SVB Financial Group, one of the Company's lenders under the Credit Facility, which accounts are subject to customary control agreements.

The Credit Facility contains customary representations and warranties, reporting and other covenants for credit facilities of this kind including prohibitions on the payment of cash dividends on the Company's capital stock and restrictions on mergers, sales of assets, investments, incurrence of liens, incurrence of indebtedness and transactions with affiliates. The Company is subject to a quarterly financial covenant requiring the Company to achieve specified minimum consolidated product revenues. As of September 30, 2018, the Company was in compliance with the financial covenant. The events of default in the Credit Facility are customary for credit facilities of this kind, and include failure to pay interest or principal, breaches of affirmative and negative covenants, a material adverse change occurring, and cross defaults to other material agreements of the Company.

Warrants – As a condition to the lenders' initial funding of the initial Term Loan A Commitment on March 18, 2016 in the amount of $15 million, the Company issued to each of the two lenders, Oxford Finance LLC and SVB Financial Group (successor by assignment to Silicon Valley Bank), a warrant to purchase 56,533 shares of Nuvectra common stock (a total of 113,066 shares) at an exercise price of $5.97 per share, which warrants are exercisable until March 18, 2026. Additionally, the Company incurred $1.5 million in fees and other direct costs of the debt transaction in connection with the initial funding. The fair value of the warrants on the date of grant totaled approximately $0.2 million and was recorded as a discount on long-term debt along with the cash issuance costs and as additional paid-in capital in the consolidated balance sheet, as the warrants met the criteria under the relevant accounting standard for treatment as an equity instrument. The related debt discount was being amortized over the term of the Term Loan A Commitment.

As a condition to the lenders' funding the initial Term Loan B Commitment on September 28, 2017 in the amount of $12.5 million, the Company issued to each of the two lenders a warrant to purchase 22,844 shares of Nuvectra common stock (a total of 45,688 shares) at an exercise price of $12.31 per share, which warrants are exercisable until September 28, 2027. In connection with the February 2017 Credit Facility amendment, the Company paid fees of $0.04 million. The fair value of the warrants on the date of grant totaled approximately $0.4 million and was recorded as additional paid-in capital in the consolidated balance sheet, as the warrants met the criteria under the relevant accounting standard for treatment as an equity instrument. The related debt discount was being amortized over the term of the Term Loan B Commitment.

As a condition to the lenders' funding the new Term Loan B Commitment under the February 2018 amendment to the Credit Facility, the Company issued to the each of the two lenders a warrant to purchase 30,245 shares of Nuvectra common stock (a total of 60,490 shares) at an exercise price of $9.30 per share, which warrants are exercisable until February 18, 2028. The fair value of the warrants on the date of grant totaled approximately $0.5 million and was recorded as additional paid-in capital in the consolidated balance sheet in the first quarter of 2018, as the warrants met the criteria under the relevant accounting standard for treatment as an equity instrument. The related debt discount is being amortized over the term of the Term Loan B Commitment.

As a condition to the lenders' funding the new Term Loan C Commitment on September 28, 2018 in the amount of $5 million, the Company issued to the each of the two lenders a warrant to purchase 5,119 shares of Nuvectra common stock (a total of 10,238 shares) at an exercise price of $21.98 per share, which warrants are exercisable until September 28, 2028. The fair value of the warrants on the date of grant totaled approximately $0.2 million and was recorded as additional paid-in capital in the consolidated balance sheet in the third quarter of 2018, as the warrants met the criteria under the relevant accounting standard for treatment as an equity instrument. The related debt discount is being amortized over the term of the Term Loan C Commitment.

Deferred Financing Fees – The change in deferred financing fees is as follows (in thousands):

At December 31, 2017	$	962
Additions during the period		7
Amortization during the period		(170)
At September 30, 2018	$	799

In accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Update ("ASU") 2015-03, "Interest-Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs," the Company has presented debt issuance costs as a direct deduction from Long-Term Debt in the condensed consolidated balance sheet.

7. INCOME TAXES

The income tax provision for interim periods is determined using an estimate of the annual effective tax rate, adjusted for discrete items, if any, that are taken into account in the relevant period. Each quarter, the estimate of the annual effective tax rate is updated, and if the estimated effective tax rate changes, a cumulative adjustment is made. There is a potential for volatility of the effective tax rate due to several factors, including changes in the mix of the pre-tax income and the jurisdictions to which it relates, changes in tax laws, business reorganizations and settlements with taxing authorities.

The Company records a valuation allowance when it is "more likely than not" that all or a portion of a deferred tax asset will not be realized. Management reviews all available positive and negative evidence, including the Company's current and past performance, the market environment in which the Company operates, the utilization of past tax credits, length of carry back and carry forward periods, existing contracts or sales backlog that will result in future profits, as well as other factors. The Company maintains a full valuation allowance on all of the net deferred tax assets for the periods presented. Until an appropriate level of profitability is sustained, the Company expects to continue to record a full valuation allowance on future tax benefits.

Pursuant to the terms of the tax matters agreement entered into with Integer at the time of the Spin-off, until March 14, 2018, the Company was prohibited from (i) causing or permitting to occur any transaction or series of transactions, subject to certain exceptions provided under the U.S. federal income tax rules, in connection with which one or more persons would (directly or indirectly) acquire an interest in its capital stock that, when combined with any other acquisition of an interest in its capital stock that occurs after the Spin-off, comprises 30% or more of the value or the total combined voting power of all interests that are treated as outstanding equity of Nuvectra for U.S. federal income tax purposes immediately after such transaction or, in the case of a series of related transactions, immediately after any transaction in such series; (ii) transferring, selling or otherwise disposing of 35% or more of its gross assets if such transfer, sale or other disposition would violate the rules and regulations of the Internal Revenue Service; (iii) liquidating its business or (iv) ceasing to maintain its active business. The tax matters agreement terminated in full on March 14, 2018.

8. COMMITMENTS AND CONTINGENCIES

Litigation – Periodically the Company is a party to various legal actions, both threatened and filed, arising in the normal course of business. While the Company does not expect that the ultimate resolution of any ordinary course pending actions will have a material effect on its results of operations, financial position, or cash flows, litigation is subject to inherent uncertainties. As such, there can be no assurance that any pending or threatened ordinary course legal action, which the Company currently believes to be immaterial, does not become material in the future.

On September 19, 2017, Boston Scientific Corporation filed a lawsuit in district court in Suffolk County, Massachusetts, against the Company and three former Boston Scientific employees hired by the Company, alleging tortious interference of contract on the part of the Company and breaches of contract related to non-solicitation and confidentiality by Boston Scientific's former employees. The Company is currently engaging in confidential settlement discussions with Boston Scientific but does not expect any such settlement, if achieved, to have a material adverse impact to the Company. In the event the Company and Boston Scientific are unable to reach a mutually agreed upon settlement, the Company intends to vigorously defend against the allegations.

Purchase Commitments – Contractual obligations for purchase of goods or services are defined as agreements that are enforceable and legally binding on the Company and that specify all significant terms, including: fixed or minimum quantities to be purchased; fixed, minimum, or variable price provisions; and the approximate timing of the transaction. The Company's purchase orders are normally based on its current manufacturing or other operational needs. Inventory to be purchased by Nuvectra in 2018 under its supply agreements is subject to certain minimum order quantity requirements. As of September 30, 2018, the Company had no material commitments to purchase capital assets; however, planned capital expenditures for the remainder of 2018 are estimated at approximately $0.5 million and will primarily be financed by existing cash and cash equivalents. The Company also enters into contracts for outsourced services; however, the contracts generally contain provisions allowing for cancellation without significant penalty.

Operating Leases – The Company is party to various operating lease agreements for office and laboratory facilities. In the first quarter of 2018, the Company amended one of its office leases to extend the expiration date until March 2023.

Minimum future estimated annual operating lease payments as of September 30, 2018 were expected to be (in thousands):

2018 (remaining 3 months)	$	178
2019		720
2020		732
2021		745
2022		619
Thereafter		85
Total estimated operating lease payments	$	3,079

9. EARNINGS (LOSS) PER SHARE

Basic net loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the period. Diluted net loss per share is equal to basic net loss per share as the Company had no potentially dilutive securities outstanding for any of the periods presented.

The following table illustrates the calculation of basic and diluted net loss per share (in thousands, except per share amounts):

	Three Months Ended		Nine Months Ended	
	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Basic net loss per share:				
Net loss	$ (12,967)	$ (11,638)	$ (35,278)	$ (35,998)
Weighted average common shares outstanding	14,840	10,697	13,852	10,497
Basic net loss per share	$ (0.87)	$ (1.09)	$ (2.55)	$ (3.43)
Diluted net loss per share:				
Net loss	$ (12,967)	$ (11,638)	$ (35,278)	$ (35,998)
Weighted average common shares outstanding	14,840	10,697	13,852	10,497
Dilutive stock options, restricted stock and restricted stock units	—	—	—	—
Weighted average common shares outstanding – assuming dilution	14,840	10,697	13,852	10,497
Diluted net loss per share	$ (0.87)	$ (1.09)	$ (2.55)	$ (3.43)
Outstanding securities and warrants that were not included in the diluted calculation because their effect would be anti-dilutive	1,469	1,549	1,469	1,549

10. FAIR VALUE MEASUREMENTS

The carrying amounts of cash, accounts receivable, accounts payable, and accrued expenses approximate fair value because of the short-term nature of these items. As of September 30, 2018, the fair value of the Company's variable rate long-term debt approximates its carrying value and is categorized in Level 2 of the fair value hierarchy.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Fair value measurement standards apply to certain financial assets and liabilities that are measured at fair value on a recurring basis (each reporting period).

The Company categorizes its warrants measured at fair value on a recurring basis in Level 3 of the fair value hierarchy. The fair value of the warrants classified as liability awards was determined by utilizing a Monte Carlo simulation model, which projects the value of Nuvectra stock versus its peer group under numerous scenarios, and determines the value of the award based upon the present value of these projected outcomes. The estimated fair value of the warrants was presented as a long-term asset and a liability in the condensed consolidated balance sheet. The estimated fair value of the warrant liability was revalued on a periodic basis and any resulting increases or decreases in the estimated fair value was recorded as an adjustment to earnings. The table below presents a summary of changes in the fair value of the Company's Level 3 liability warrants during the first nine months of 2018 (in thousands):

Balance at December 31, 2017 – initial Term Loan C (new Term Loan B) Commitment warrant	$ 400
Loss on fair value of warrant liability – initial Term Loan C (new Term Loan B) Commitment warrant	55
Reclassification of warrant liability to equity upon issuance of warrants – initial Term Loan C (new Term Loan B) Commitment warrant	(455)
Fair value of warrant liability issued in first quarter 2018 – new Term Loan C Commitment warrant	109
Loss on fair value of warrant liability – new Term Loan C Commitment warrant	57
Reclassification of warrant liability to equity upon issuance of warrants in third quarter 2018 – new Term Loan C Commitment warrant	(166)
At September 30, 2018	$ -

As discussed in Note 6, "Debt," in connection with the issuance of warrants in February 2018, the fair value of the warrant liability was reclassified to equity. Additionally, in February 2018 the Company recognized a warrant liability of $0.1 million related to the new Term Loan C Commitment. In connection with the issuance of warrants in September 2018, the fair value of the warrant liability related to the new Term Loan C Commitment was reclassified to equity.

The Company's investments in marketable securities primarily consist of investments in debt securities, which are classified as Cash and Cash Equivalents on the consolidated balance sheet because of their original maturities of three months or less. Unrealized gains or losses for the periods presented are included in other comprehensive loss.

The fair values of marketable securities were estimated using the market approach using prices and other relevant information generated by market transactions involving identical or comparable assets. The Company uses quoted market prices in active markets or quoted market prices in markets that are not active to measure fair value. When developing fair value estimates, the Company maximizes the use of observable inputs and minimizes the use of unobservable inputs. As of September 30, 2018, the fair market value of marketable securities was approximately $93.8 million, all of which had original maturities of three months or less.

Marketable securities, measured at fair value, by level within the fair value hierarchy were as follows (in thousands):

		September 30, 2018		
	Fair Value Hierarchy	Cost	Unrealized Loss	Fair Value
Cash	Level 1	$ 78,828	$ -	$ 78,828
Government	Level 1	1,502	-	1,502
Financial	Level 2	8,654	-	8,654
Industrial	Level 2	4,800	-	4,800
Total		$ 93,784	$ -	$ 93,784

		December 31, 2017		
	Fair Value Hierarchy	Cost	Unrealized Loss	Fair Value
Cash	Level 1	$ 7,336	$ -	$ 7,336
Government	Level 1	1,499	-	1,499
Financial	Level 2	3,799	(1)	3,798
Industrial	Level 2	8,649	-	8,649
Total		$ 21,283	$ (1)	$ 21,282

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

Fair value standards also apply to certain assets and liabilities that are measured at fair value on a nonrecurring basis. A summary of the valuation methodologies for assets and liabilities measured on a nonrecurring basis is as follows:

Long-lived Assets – The Company reviews the carrying amount of its long-lived assets to be held and used, other than goodwill, for potential impairment whenever certain indicators are present as described in Note 1 "Summary of Significant Accounting Policies." During the first nine months of 2018 and 2017, no impairment charges were recorded related to the Company's long-lived assets.

Goodwill – Goodwill recorded is not amortized but is periodically tested for impairment. The Company assesses goodwill for impairment on December 31, or more frequently if certain events occur as described in Note 1 "Summary of Significant Accounting Policies." During the first nine months of 2018 and 2017, no impairment charges were recorded related to the Company's goodwill.

Warrants – In order to determine the fair value of the warrants classified as equity awards, the Company used a Monte Carlo simulation model. The risk-free interest rate represents the 10-Year U.S. Treasury rate as of the issuance date. The expected volatility assumption is based on historical volatilities for publicly traded stock of comparable companies.

11. BUSINESS SEGMENT, GEOGRAPHIC AND CONCENTRATION RISK INFORMATION

The Company has two reportable segments and two reporting units, consisting of Nuvectra and NeuroNexus.

Nuvectra is a neurostimulation company committed to helping physicians improve the lives of people with chronic conditions. Algovita is the Company's first commercial offering and is approved for the treatment of chronic pain of the trunk and/or limbs. Nuvectra's innovative technology platform also has capabilities under development to support other neurological indications such as SNM for the treatment of overactive bladder and DBS for the treatment of Parkinson's disease and Essential Tremor. Revenue includes development and engineering service fees and sales from the release of Algovita in the United States and Europe. Future revenues of Nuvectra are expected to come primarily from sales of Algovita, particularly after expansion of its launch commercially in the United States, and, subject to FDA approval, Virtis, the second application of the Company's neurostimulation technology platform and its first product for the SNM market.

NeuroNexus designs, manufactures and markets neural-interface technologies for the neuroscience clinical research market. Revenues include sales of neural interface technology, components and systems to the neuroscience and clinical markets.

An analysis and reconciliation of the Company's product lines, business segments and geographic information to the respective information in the consolidated financial statements follows (in thousands):

	Three Months Ended		Nine Months Ended	
Product line sales:	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Algovita	$ 12,460	$ 6,302	$ 33,050	$ 15,180
Neural interface components and systems	1,353	1,129	3,636	3,504
Development and engineering service	403	186	1,253	1,196
Total sales	$ 14,216	$ 7,617	$ 37,939	$ 19,880

	Three Months Ended		Nine Months Ended	
Business segment sales:	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Nuvectra	$ 12,863	$ 6,488	$ 34,303	$ 16,376
NeuroNexus	1,353	1,129	3,636	3,504
Total sales	$ 14,216	$ 7,617	$ 37,939	$ 19,880

	Three Months Ended		Nine Months Ended	
Segment (loss) income from operations:	September 30, 2018	September 30, 2017	September 30, 2018	September 30, 2017
Nuvectra	$ (12,164)	$ (11,092)	$ (32,851)	$ (34,510)
NeuroNexus	177	64	444	210
Total segment (loss) income from operations	(11,987)	(11,028)	(32,407)	(34,300)
Unallocated operating expenses	—	—	—	—
Operating loss	(11,987)	(11,028)	(32,407)	(34,300)
Unallocated other expense, net	(997)	(601)	(2,860)	(1,689)
Loss before provision for income taxes	$ (12,984)	$ (11,629)	$ (35,267)	$ (35,989)

All of the Company's long-lived tangible assets are located in the United States.

12. RELATED PARTY TRANSACTIONS

On March 14, 2016, Integer completed the Spin-off, at which time the Company became a separate public company. The Company entered into, or amended, various agreements with Integer to effect the Spin-off and to provide a framework for the Company's relationship with Integer after the Spin-off including a supply agreement, license agreements, a separation and distribution agreement, a tax matters agreement, a transition services agreement and an employee matters agreement, which provided for the allocation between Nuvectra and Integer of assets, employees, liabilities and obligations (including PP&E, employee benefits, and tax-related assets and liabilities) attributable to the Company's business for the period prior to, at, and after the Spin-off. The tax matters agreement, the transition services agreement and the employee matters agreement have expired and are no longer in effect.

Employee Benefit Plans – Prior to the Spin-off, certain of the Company's employees participated in various Integer stock-based compensation plans. Compensation expense allocated to Nuvectra for these plans from Integer was based upon the costs directly attributable to Nuvectra employees. See Note 5 "Employee Benefit Plans" for additional information.

Supply Agreement – The Company has a supply agreement with Integer pursuant to which Integer manufactures Algovita and certain of its components. Total charges incurred under this supply agreement are included in cost of sales.

13. RECENTLY ISSUED ACCOUNTING STANDARDS

In the normal course of business, management evaluates all new accounting pronouncements issued by the FASB to determine the potential impact they may have on the Company's condensed consolidated financial statements. Based upon this review, except as noted below, management does not expect any of the recently issued accounting pronouncements, which have not already been adopted, to have a material impact on the Company's condensed consolidated financial statements.

Recently Adopted in 2018

In May 2017, the FASB issued ASU 2017-09, *Compensation-Stock Compensation (Topic 718): Scope of Modification Accounting*. ASU 2017-09 clarifies when changes to the terms or conditions of a share-based payment award must be accounted for as modifications. Under ASU 2017-09, an entity will not apply modification accounting to a share-based payment award if the award's fair value, vesting conditions and classification as an equity or liability instrument are the same immediately before and after the change. ASU 2017-09 will be applied prospectively to awards modified on or after the adoption date. The adoption of ASU 2017-09 did not have a material impact on the Company's condensed consolidated financial statements.

In January 2017, the FASB issued ASU 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business*. ASU 2017-01 provides a screen to determine when an integrated set of assets and activities (collectively referred to as a "set") does not constitute a business. The screen requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. This screen reduces the number of transactions that need to be further evaluated. If the screen is not met, the amendments in ASU 2017-01 (i) require that to be considered a business, a set must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output and (ii) remove the evaluation of whether a market participant could replace missing elements. The adoption of ASU 2017-01 did not have a material impact on the Company's condensed consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This update provides clarification regarding how certain cash receipts and cash payments are presented and classified in the statement of cash flows. ASU 2016-15 addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. The adoption of ASU 2016-15 did not have a material impact on the Company's condensed consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, *Recognition and Measurement of Financial Assets and Financial Liabilities*, which updates certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The adoption of ASU 2016-01 did not have a material impact on the Company's condensed consolidated financial statements.

In May 2014, the FASB issued ASC Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which has been subsequently updated. ASU 2014-09 provides enhancements to the quality and consistency of how revenue is reported while also improving comparability in the financial statements of companies using U.S. GAAP and International Financial Reporting Standards. ASC 606 outlines a single comprehensive model for companies to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The core principle requires entities to recognize revenue in a manner that depicts the transfer of goods or services to customers in amounts that reflect the consideration an entity expects to be entitled to in exchange for those goods or services. The new standard also includes criteria for the capitalization and amortization of certain contract acquisition and fulfillment costs. The Company adopted ASU 2014-09 and its related amendments effective January 1, 2018 under the modified retrospective method and will only apply this method to contracts that are not completed as of the date of adoption. The modified retrospective method results in a cumulative effect of initially applying the standard as an adjustment to the opening balance of retained earnings at the date of initial application for the impact to changes in the timing and amount of revenue recognition as well as the timing of capitalization and amortization of certain contract costs. With the exception of the increased disclosure requirements, the adoption of ASU 2014-09 did not have a material impact on the Company's consolidated financial statements as of the date of adoption, January 1, 2018 and as of and for the nine months ended September 30, 2018. Please see Note 2, "Revenue from Contracts with Customers," for the Company's updated policies related to revenue recognition and accounting for costs to obtain and fulfill a customer contract.

Not Yet Adopted

In August 2018, the FASB issued ASU 2018-15, *Intangibles-Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract.* ASU 2018-15 aligns the requirements for capitalizing implementation costs incurred in a cloud computing arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The ASU is effective for fiscal years beginning after December 15, 2019, and interim periods within those fiscal years. Early adoption is permitted. The Company is currently in the process of evaluating the impact of adoption of the ASU on its condensed consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*, which modifies the disclosure requirements on fair value measurements. ASU 2018-13 is effective in the first quarter of fiscal 2020, and earlier adoption is permitted. The Company is currently in the process of evaluating the impact of adoption of the ASU on its condensed consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*. The purpose of ASU 2016-13 is to replace the current incurred loss impairment methodology, for financial assets measured at amortized cost, with a methodology that reflects expected credit losses. It also requires consideration of a broader range of reasonable and supportable information, including forecasted information, to develop credit loss estimates. The ASU affects trade receivables, debt securities, net investment in leases, and most other financial assets that represent a right to receive cash. Additional disclosures about significant estimates and credit quality are also required. ASU 2016-13 is effective for annual periods beginning after December 15, 2019, including interim periods within those annual periods. Early adoption is permitted for annual periods beginning after December 15, 2018. The Company is currently in the process of evaluating the impact of adoption of the ASU on its condensed consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842),* in order to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet for those leases classified as operating leases under previous U.S. GAAP. ASU 2016-02 requires that a lessee should recognize a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term on the balance sheet. In July 2018, the FASB issued ASU 2018-11, *Leases (Topic 842) Targeted Improvements*, which provides an additional transition method and practical expedient that allows entities to initially apply the new standard at the adoption date and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption without restating prior periods. ASU 2016-02 is effective for fiscal years beginning after December 15, 2018 (including interim periods within those periods), using a modified retrospective approach, and early adoption is permitted. The Company intends to adopt the requirements of the new standard effective January 1, 2019, via a cumulative-effect adjustment without restating prior periods.

The Company has preliminarily elected the package of practical expedients that permits the Company not to reassess: (i) whether expired or existing contracts contain a lease under the new standard; (ii) the lease classification for expired or existing leases; and (iii) whether previously-capitalized initial direct costs would qualify for capitalization under the new standard. The Company also preliminarily made the following policy elections: (i) to use the hindsight practical expedient to determine lease term and when assessing existing right of use assets for impairment; (ii) not to recognize right-of-use assets or lease liabilities for leases with a term of 12 months or less, as permitted by the short-term lease practical expedient in the standard; and (iii) not to apply the practical expedient that permits a lessee to account for lease and non-lease components in a contract as a single lease component (rather than separate lease and non-lease components) and, accordingly, the Company will account for these components separately.

The Company has established an implementation team to assist with its assessment of the impact that the new guidance will have on the Company's operations, consolidated financial statements and related disclosures. To date, this assessment has included surveying the Company's business units, assessing the Company's portfolio of leases, compiling information on active leases and assessing the potential impact of embedded leases from its manufacturing outsourcing, service arrangements and other agreements. The implementation team is in the process of evaluating and designing the necessary changes to its business processes, systems and controls to support recognition and disclosure under the new standard. The Company's primary operating leases are its real estate leases. See Note 8 "Commitments and Contingencies" for additional information.

The Company is currently in the process of evaluating the impact of adoption of the ASU on its condensed consolidated financial statements and has not yet determined the impact from adoption of this new accounting pronouncement on its condensed consolidated financial statements. However, adoption of this standard will result in the recognition of right-of-use assets and lease liabilities in the Company's condensed consolidated balance sheet for those leases classified as operating leases under current U.S. GAAP.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This report contains "forward-looking statements" within the meaning of the safe harbor provisions of the U.S. Private Securities Litigation Reform Act of 1995. Our actual results could differ materially from those discussed in the forward-looking statements. Forward-looking statements can be identified by the use of words such as, but not limited to: "anticipate," "intend," "plan," "goal," "seek," "believe," "project," "target," "estimate," "expect," "strategy," "future," "likely," "may," "can," "continue," "could," "should," "would," "will," and similar expressions or references to future periods. These statements are based on the beliefs and assumptions of our management based on information currently available to management. Such forward-looking statements are subject to risks, uncertainties and other important factors that could cause actual results and the timing of certain events to differ materially from future results expressed or implied by such forward-looking statements. Important factors that could cause our actual results to differ materially from those indicated in the forward-looking statements include: (i) our ability to successfully commercialize Algovita and to develop, complete and commercialize enhancements or improvements to Algovita; (ii) our ability to successfully compete with our current SCS competitors and the ability of our U.S. sales representatives to successfully establish market share and acceptance of Algovita; (iii) the uncertainty and timing of obtaining regulatory approvals in the United States and Europe for our Virtis SNM system; (iv) our ability to successfully launch and commercialize the Virtis SNM system if and when it receives regulatory approval; (v) our ability to demonstrate the features, perceived benefits and capabilities of Algovita to physicians and patients in competition with similar products already well-established and sold in the SCS market; (vi) our ability to anticipate and satisfy customer needs and preferences and to develop, introduce and commercialize new products or advancements and improvements to Algovita in order to successfully meet our customers' expectations; (vii) the outcome of our development plans for our neurostimulation technology platform, including our ability to identify additional indications or conditions for which we may develop neurostimulation medical devices or therapies and seek regulatory approval thereof; (viii) our ability to identify business development and growth opportunities and to successfully execute on our strategy, including our ability to seek and develop strategic partnerships with third parties to, among other things, fund clinical and development costs for new product offerings; (ix) the performance by our development partners, including Aleva Neurotherapeutics, S.A., of their obligations under their agreements with us; (x) the scope of protection for our intellectual property rights covering Algovita and other products using our neurostimulation technology platform, along with any product enhancements or improvements; (xi) our ability to successfully build, attract and maintain an effective commercial infrastructure and qualified sales force in the United States; (xii) our compliance with all regulatory and legal requirements regarding implantable medical devices and interactions with healthcare professionals; (xiii) our reliance on each of Integer, our exclusive and sole manufacturer and supplier of parts and components for Algovita, and Minnetronix, Inc., our sole-source supplier of external peripheral devices; (xiv) any supplier shortages related to Algovita or its components and any manufacturing disruptions which may impact our inventory supply as we expand our business; (xv) any product recalls, or the receipt of any warning letters, mandatory corrections or fines from any governmental or regulatory agency; (xvi) our ability to satisfy the conditions and covenants of our Credit Facility; and (xvii) our ability to raise capital should it become necessary to do so, through another public offering of our common stock, private equity or debt financings, strategic partnerships, or other sources. Factors that could cause or contribute to such differences include, but are not limited to, those included in the section entitled "Risk Factors" in Nuvectra's Annual Report on Form 10-K for the fiscal year ended December 31, 2017. Furthermore, such forward-looking statements speak only as of the date of this report. We undertake no obligation to publicly update any forward-looking statement, whether written or oral, that may be made from time to time, whether as a result of new information, future developments, or otherwise.

Our Business

Nuvectra is a neurostimulation medical device company focused on the development and commercialization of our neurostimulation technology platform for the treatment of various disorders through stimulation of tissues associated with the nervous system. Our neurostimulation technology platform has the capability to provide treatment to patients in several established neurostimulation markets, including SCS, SNM, DBS, and other emerging neurostimulation markets.

Our Algovita™ SCS system, or Algovita, is the first application of our neurostimulation technology platform and is indicated for the treatment of chronic pain of the trunk and limbs. Algovita received premarket approval from the FDA in November 2015, and we commercially launched Algovita in the United States during the first half of 2016. Outside of the United States, Algovita obtained CE Mark approval in June 2014 and is indicated for the treatment of chronic intractable pain of the trunk or limbs. Algovita is reimbursable under existing SCS codes in the United States, the European Union and Australia, and has been commercially available to patients in Germany and several other European countries since November 2014.

We have also developed our existing platform for use in the SNM market and have filed regulatory submissions with the FDA and CE Mark authorities in January 2017 and December 2016, respectively, for Virtis, the Company's SNM system for the treatment of chronic urinary retention and the symptoms of overactive bladder. We received requests from the FDA and CE Mark authorities for additional information and data regarding these submissions on July 2, 2018 and June 22, 2018, respectively, as further described below under "Strategic and Financial Overview."

In addition, in early 2016, we entered into a development agreement with Aleva, which was amended and restated on August 31, 2017. This agreement provides that we will leverage our neurostimulation technology platform to develop a DBS system for Aleva to treat Parkinson's disease. This platform is still under development and is subject to Aleva receiving sufficient financing, the outcome of which may impact our development of the DBS system during 2019.

Our results also include the operations of our subsidiary NeuroNexus. NeuroNexus works closely with researchers to develop and refine new tools that aid and advance neuroscience research. NeuroNexus designs, manufactures and sells neural interface systems including high quality, high density microelectrode arrays, custom designed probes, electrode instrumentation and accessories.

Our revenues include sales of Algovita, neural interface technology, components and systems to the neuroscience and clinical markets, and development and engineering service fees. We expect that our future revenues will come primarily from sales of neurostimulation medical device products, including Algovita, particularly as we continue our commercial expansion in the United States, and, pending regulatory approvals, from Virtis, the second application of our neurostimulation technology platform and our first product for the SNM market. From time to time, our future revenues may also include technology licensing fees, development and engineering service fees, and royalty fees.

Our Customers

Algovita was designed to provide pain management solutions to patients who have evolving requirements and needs. We are still developing our customer base for Algovita, which includes distributors in Europe and hospitals, surgery centers and medical facilities in the United States served through a direct sales force and third-party distributors; therefore, the nature and extent of our selling relationships with each customer is different in terms of breadth of products purchased, purchased product volumes, length of contractual commitment, ordering patterns, inventory management, and selling prices. Our NeuroNexus customers include institutions, scientists or universities throughout the world who perform research for the neuroscience and clinical markets. Additionally, in the DBS market, our customer is Aleva, whom we service through a strategic development agreement.

Strategic and Financial Overview

We are a neurostimulation medical device company formed in 2008 to design and develop a neurostimulation technology platform that could be utilized in multiple indications. Since our inception, the majority of our resources have been spent designing and developing Algovita. SCS was chosen as the first sector of the neurostimulation market to pursue, as we believe that it is a high growth existing market, there is an established regulatory and reimbursement pathway, and we believe that there are significant unmet needs in the SCS market. We currently have four significant competitors in the United States who may be better capitalized and who offer similar SCS devices that are already established and accepted in the market. While the competitive landscape for SCS remains challenging and we may face barriers to market acceptance of our product, we believe Algovita has certain differentiating features from other existing SCS systems that offer our patients and customers a broad set of capabilities and treatment options.

We have been leveraging our neurostimulation technology platform for other sectors of the neurostimulation market such as SNM and DBS, and are exploring other emerging indications.

We submitted a pre-market approval application for Virtis to TÜV SÜD, our notified body in Europe, and to the FDA in the United States, in December 2016 and January 2017, respectively. In July 2018, we received notice from the FDA requesting that the Company provide supplemental information related to modifications to the Virtis device, labeling and manufacturing, as well as clarifications of data related to magnetic resonance imaging ("MRI"). In early August 2018 we filed our response to the FDA's requests. The FDA has up to 180 days from that submission to review our response, after which the FDA could approve the device, reject the device, request additional information or request additional clinical study data.

On June 22, 2018, we also received notice from TÜV SÜD regarding our Virtis application for CE Mark. TÜV SÜD notified us that it was requesting additional clinical study data regarding the safety and efficacy of the device for the requested indication. We are currently evaluating the best path forward to determine whether a clinical studies plan can be effectuated in a timely and cost-effective manner. If we determine a strategy that meets our objectives, we may move forward with a clinical studies plan after obtaining FDA approval.

In early 2016, we entered into a development agreement with Aleva, which was amended and restated on August 31, 2017. This agreement provides that we will leverage our neurostimulation technology platform to develop a DBS system for Aleva to treat Parkinson's disease. This platform is still under development and is subject to Aleva receiving sufficient financing, the outcome of which may impact the ability to fund our development of the DBS system during 2019. We expect Aleva to raise additional capital funds in order to fully develop a DBS system. If we complete development of a DBS system to treat Parkinson's disease for Aleva, we expect that Aleva will commercialize the DBS system. If Aleva does so and is successful, we would receive royalties on the sale of these DBS systems and components.

We also intend to pursue other strategic partnerships to fund clinical and development costs of new products, expand our product distribution channels, supplement our product commercialization efforts, obtain assistance in designing and performing clinical studies and post market studies, add specialized clinical or regulatory expertise, or acquire or obtain access to complementary intellectual property.

Although we believe we have significant revenue growth opportunity in large, established markets, we have a history of significant net losses, and we expect to continue to incur net losses for the foreseeable future. We expect that future revenue growth will come largely from sales of Algovita in the United States market.

Our Financial Results

The discussion that follows should be read in conjunction with our condensed consolidated financial statements and related notes and with the Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. The following table presents certain selected financial information derived from our condensed consolidated financial statements for the periods presented (dollars in thousands, except per share data):

	Three Months Ended		Change		Nine Months Ended		Change	
	September 30, 2018	September 30, 2017	$	%	September 30, 2018	September 30, 2017	$	%
Sales:								
Algovita	$ 12,460	$ 6,302	$ 6,158	98%	$ 33,050	$ 15,180	$17,870	118%
Neural interface components and systems	1,353	1,129	224	20%	3,636	3,504	132	4%
Development and engineering services	403	186	217	117%	1,253	1,196	57	5%
Total sales	14,216	7,617	6,599	87%	37,939	19,880	18,059	91%
Cost of sales	6,597	4,151	2,446	59%	17,641	10,101	7,540	75%
Gross profit	7,619	3,466	4,153	120%	20,298	9,779	10,519	108%
Gross profit as a % of sales	*53.6%*	*45.5%*			*53.5%*	*49.2%*		
Selling, general and administrative expenses (SG&A)	15,221	11,358	3,863	34%	40,814	33,349	7,465	22%
SG&A as a % of total operating expenses	*77.6%*	*78.4%*			*77.4%*	*75.7%*		
Research, development and engineering costs, net (RD&E)	4,385	3,136	1,249	40%	11,891	10,730	1,161	11%
RD&E as a % of total operating expenses	*22.4%*	*21.6%*			*22.6%*	*24.3%*		
Operating loss	(11,987)	(11,028)	(959)	9%	(32,407)	(34,300)	1,893	(6)%
Interest expense, net	986	422	564	134%	2,772	1,190	1,582	133%
Other expense, net	11	179	(168)	(94)%	88	499	(411)	(82)%
Provision for income taxes	(17)	9	(26)	(289)%	11	9	2	22%
Effective tax rate	*0.0%*	*0.0%*			*0.0%*	*0.0%*		
Net loss	$ (12,967)	$ (11,638)	$(1,329)	11%	$ (35,278)	$ (35,998)	$ 720	(2)%
Diluted earnings per share	$ (0.87)	$ (1.09)	$ 0.22	(20)%	$ (2.55)	$ (3.43)	$ 0.88	(26)%

Sales

Algovita. The primary factor behind the 98% increase in sales from the third quarter of 2017 to the third quarter of 2018 and the 118% increase in sales from the first nine months of 2017 to the first nine months of 2018 was the continued growth in volume of sales from the Company's commercial launch of Algovita in the United States during 2016. We expect to continue to develop our worldwide sales organization for Algovita, consisting of direct sales representatives and independent sales agents in the United States and a network of distributors and independent sales agents outside of the United States, to support future growth.

We expect our revenue to fluctuate from quarter to quarter due to a variety of factors, including seasonality, as we have historically experienced lower sales in the first quarter and third quarter of the year, which we believe is due to weather-related events, holidays, the buying patterns and implant volumes of our distributors, hospitals and clinics and reimbursement related factors such as patient deductibles. We anticipate that our total revenue will increase as we continue our commercialization in the United States.

Neural Interface Components and Systems. Neural interface components and systems are related to our NeuroNexus segment and consist of sales of neural interface technology, components, and systems to the neuroscience and clinical markets. Sales increased 20% from the third quarter of 2017 to the third quarter of 2018 and increased 4% from the first nine months of 2017 to the first nine months of 2018.

Development and Engineering Service. We recognized $0.4 million and $1.3 million of development and engineering services revenue during the third quarter and first nine months of 2018, respectively, and $0.2 million and $1.2 million of revenue during the third quarter and first nine months of 2017, respectively, from our development agreement with Aleva. See the section entitled "Strategic and Financial Overview" above for more information related to our development agreement with Aleva.

Cost of Sales

Cost of sales consists of the costs of components and materials, labor costs, amortization of technology intangibles, and plant and equipment depreciation and overhead. The primary driver behind the 59% increase in cost of sales from the third quarter of 2017 to the third quarter of 2018 was the increase in sales of our Algovita systems. We expect that our cost of sales will continue to increase as our sales of our Algovita products continue to grow.

From the third quarter of 2017 to the third quarter of 2018 our gross profit increased $4.2 million, or 120%, and our gross profit as a percentage of sales, or gross margin, increased from 45.5% to 53.6%. These increases were primarily due to an increase in the volume and mix of Algovita sales in the United States.

Our gross margin has been and will continue to be affected by a variety of factors, including by our revenue mix as margins vary across each of our product lines, the costs to have our product manufactured for us, inventory-related charges and write-downs, the ratio of trial to permanent implants, and the average selling prices of our products. We expect our gross margin to be positively affected over time to the extent we are successful in reducing manufacturing costs. However, our gross margin may continue to fluctuate from period to period as our revenue mix continues to shift towards Algovita and, if and when approved for commercial sale, Virtis.

The primary factor behind the 75% increase in cost of sales from the first nine months of 2017 to the first nine months of 2018 was the increased sales of our Algovita systems. We expect that our cost of sales will continue to increase as our sales of our Algovita products continue to grow.

From the first nine months of 2017 to the first nine months of 2018 our gross profit increased $10.5 million or 108%, and our gross profit as a percentage of sales, or gross margin, increased from 49.2% to 53.5%. These increases were primarily due to an increase in the volume and mix of Algovita sales in the United States.

Selling, General and Administrative Expenses

Selling, general and administrative ("SG&A") expenses consist primarily of personnel costs, including salary and employee benefits for our sales and marketing personnel and for personnel that support our general operations, such as information technology, executive management, financial accounting, and human resources personnel. SG&A expenses increased $3.9 million, or 34%, from the third quarter of 2017 to the third quarter of 2018. This increase was primarily the result of an increase in personnel-related expenses as we have continued to increase our sales of our Algovita product.

SG&A expenses increased $7.5 million, or 22%, from the first nine months of 2017 to the first nine months of 2018. This increase was primarily the result of an increase in personnel-related expenses as we have continued to increase our sales of our Algovita product.

Our SG&A expenses may fluctuate from period to period due to the seasonality of our revenue and the timing and extent of our SG&A expense. Going forward, we expect SG&A expenses to continue to increase as we build our Virtis worldwide sales organization consisting of direct sales representatives and independent sales agents in the United States and a network of distributors and independent sales agents outside of the United States pending regulatory approvals. We expect that this will require recruiting appropriate and qualified direct sales representatives and independent sales agents, expanding our commercial infrastructure in the United States and training our direct sales representatives and independent sales agents. Thereafter, we expect that our sales representatives and independent sales agents will require lead time in the field to access and grow their network of accounts and produce sales results. We believe that successfully recruiting, training and retaining a sufficient number of productive sales representatives and independent sales agents is important in achieving our future growth objective.

Research, Development and Engineering Costs, Net

Research, development and engineering ("RD&E") costs primarily include salary and employee benefits for our specialists in software engineering, mechanical engineering, electrical engineering, and graphical user interface design. Many of these specialists have considerable experience in neurostimulation-related products. Additionally, RD&E costs include design verification testing expenses, which include salary and employee benefits for our engineers who test the design and materials used in our medical devices. RD&E costs also include salary, benefits and other personnel-related expenses for our regulatory, quality and clinical affairs employees.

RD&E costs increased $1.2 million, or 40%, from the third quarter of 2017 to the third quarter of 2018. The increase was primarily the result of an increase in personnel-related expenses and the timing of research project-related expenses.

RD&E costs increased $1.2 million, or 11%, for the first nine months of 2018 compared to the same period in 2017. The increase was primarily the result of an increase in personnel-related expenses.

As we must continually strive to anticipate and meet our customers' and patients' evolving needs and preferences, we expect to continue to invest in product development, product enhancements and improvements and future clinical studies to further develop and update our existing technologies and to expand the features offered in Algovita and Virtis. We also intend to continue to pursue strategic partnerships to fund clinical and development costs, in part or in full, of new products, expand our product distribution channels, improve our access to physicians and opinion leaders, supplement our product commercialization efforts, obtain assistance in performing clinical studies, add specialized clinical or regulatory expertise, or acquire or obtain access to complementary intellectual property.

Interest Expense, Net

Interest expense, net for the third quarter of 2018 and the third quarter of 2017 was $1.0 million and $0.4 million, respectively. Interest expense, including amortization of deferred financing fees and discounts on debt, related to our Credit Facility was $1.2 million and $0.5 million for the third quarter of 2018 and the third quarter of 2017, respectively. The increase was primarily a result of an increase in our outstanding borrowings under our Credit Facility in the third quarter of 2018 as compared to the third quarter of 2017. Interest income from investments was $0.2 million for the third quarter of 2018 and $0.1 million for the third quarter of 2017.

Interest expense, net for the first nine months of 2018 and the first nine months of 2017 was $2.8 million and $1.2 million, respectively. Interest expense, including amortization of deferred financing fees and discounts on debt, related to our Credit Facility was $3.4 million and $1.4 million for the first nine months of 2018 and the first nine months of 2017, respectively. Interest income from investments was $0.6 million for the first nine months of 2018 and $0.2 million for the first nine months of 2017.

For additional information, see Note 6 "Debt" of the notes to our Condensed Consolidated Financial Statements.

Other Expense, Net

Other expense, net for the third quarter and the first nine months of 2018 and 2017 primarily related to the revaluation of our previously existing warrant liability due to the change in the estimated fair value.

Provision for Income Taxes

During the third quarters of 2018 and 2017, we recorded a valuation allowance for the amount of the deferred tax asset that was generated from our net losses and federal research and development tax credit earned and Section 754 election to the extent they exceeded any deferred tax liability, as it was more likely than not that the deferred tax asset generated from those activities will not be realized. See Note 7 "Income Taxes" of the notes to our Condensed Consolidated Financial Statements for disclosures related to our income taxes.

Liquidity and Capital Resources

Background

We have incurred significant net losses and negative cash flows from operations since our inception and we expect to continue to incur additional net losses for the foreseeable future.

Immediately prior to the completion of the Spin-off, Integer made a cash capital contribution of $75.0 million to us, which we have used for the continued development and commercialization of Algovita, development of Virtis, and general corporate purposes. Based on our current plans and expectations, we estimate that our cash on hand, which includes proceeds from the Company's follow-on common stock offerings completed in February and September 2018, Credit Facility draw-downs, and cash generated from sales, should meet our cash needs for at least the next twelve months.

We periodically evaluate our liquidity requirements, alternative uses of capital, capital needs and available resources. As a result of this process, we have in the past sought, and may in the future seek, to explore strategic alternatives to finance our business plan, including but not limited to, a public offering of our common stock, private equity or debt financings, sale of non-strategic assets, or other sources, such as strategic partnerships. We have elected and may continue to elect to make near-term decisions, including engaging in various capital generating initiatives, to provide additional liquidity. However, if we are unable to raise additional funds when needed, we may be required to delay, reduce, or terminate some or all of our development plans. We are also focusing on increasing the sales of our products to generate cash flow to fund our operations. However, there can be no assurance that we will be successful in our plans described above or in attracting alternative debt or equity financing.

Currently, we expect our research and development expenditures for 2018 to be between approximately $15 million and $20 million. These expenditures are primarily to continue our research and development program to enhance and improve Algovita and Virtis and to continue to develop our neurostimulation technology platform for uses in indications outside of SCS and SNM. Costs are primarily related to development engineering, regulatory, quality and clinical affairs. We expect to finance these expenditures using cash on-hand and cash generated from sales. We may increase, decrease or re-allocate these anticipated expenditures during any period based on industry conditions, the availability of capital, or other factors. We believe that nearly all of our anticipated research and development expenditures are discretionary.

Consolidated Cash Flows

Net cash used in operating activities was $31.4 million compared to a net loss of $35.3 million for the first nine months of 2018. Net cash used in operating activities was $39.2 million compared to a net loss of $36.0 million for the first nine months of 2017. The primary components driving the decrease in cash used in operating activities from the first nine months of 2017 to the first nine months of 2018 was the $0.7 million decrease in our net loss (adjusted to exclude non-cash charges) and changes in working capital accounts, specifically, the significant payments in the first nine months of 2017 (totaling $5.9 million) related to large accounts payable and other current liabilities at the end of 2016 primarily for inventory purchases from Integer in accordance with certain minimum order quantity requirements under our supply agreement. Additionally, there was an increase in accounts receivable of $3.9 million in the nine months ended September 30, 2017 as compared to an increase in accounts receivable of $0.8 million in the nine months ended September 30, 2018. These changes in accounts receivable were due to the increased sales of our Algovita systems and timing of collections.

Net cash used in investing activities was $0.5 million for the first nine months of 2018 compared to $0.9 million for the first nine months of 2017. Cash used in investing activities related to the purchases of property, plant and equipment. As of September 30, 2018, we had no material commitments to purchase capital assets; however, planned capital expenditures for the remainder of 2018 are estimated at approximately $0.5 million.

Net cash provided by financing activities was $105.6 million for first nine months of 2018 compared to $13.9 million for the first nine months of 2017. Cash provided by financing activities in 2018 was primarily composed of $88.5 million net from the sale of common stock and $16.7 million in net borrowings under our amended Credit Facility. Cash provided by financing activities in the first nine months of 2017 was primarily composed of $12.5 million of borrowings under our Credit Facility and $1.3 million in proceeds from the exercise of stock options.

Credit Facility

The Credit Facility consists of term loan facilities in an aggregate maximum principal amount of $45 million, comprised of (i) a $27.5 million Term Loan A Commitment, which was funded in full in February 2018, (ii) a $12.5 million Term Loan B Commitment, which also was funded in full in February 2018, and (iii) a $5 million Term Loan C Commitment, which was funded in full in September 2018.

The Term Loans bear interest at the Wall Street Journal prime rate plus 4.15%, subject to an interest rate floor of 8.65%. At September 30, 2018 the interest rate on the term loans was 9.15%. The Credit Facility provides for interest-only payments on outstanding term loans for 24 months after the first borrowing in February 2018 followed by 30 months of principal payments in equal amounts on outstanding term loan borrowings plus accrued interest payments.

On March 18, 2016, in connection with arranging the Credit Facility, we paid Piper Jaffray an arrangement fee of $1.1 million, which equaled 2.50% of the aggregate principal amount of the then-existing Credit Facility. On March 18, 2016, under the terms of the Credit Facility, we paid a commitment fee in an amount equal to 0.50% of the aggregate principal amount of the then-existing $40 million term loan and $5 million revolving line of credit. We also paid a fee of $25,000 plus the expenses of the lenders when we amended the Credit Facility in February 2017 and a second amendment fee of approximately $0.8 million when we amended the Credit Facility in February 2018.

In addition, a final payment fee in an amount equal to 7.75% of the funded amount of the term loans will be due at the time of the final principal payment under the Credit Facility or upon early termination of the Credit Facility.

The Credit Facility includes affirmative and negative covenants, including an affirmative covenant regarding minimum revenue requirements, prohibitions on the payment of cash dividends on our capital stock, and restrictions on mergers, sales of assets, investments, incurrence of liens, incurrence of indebtedness and transactions with affiliates. The Credit Facility includes a prepayment fee for the prepayment of the outstanding term loans prior to the maturity date in an amount equal to $1.3 million plus 3.00% of the prepaid term loans for a prepayment made prior to February 2019, 2.00% of the prepaid term loans for a prepayment made prior to February 2020 and 1.00% of the prepaid term loans for a prepayment made thereafter. Our obligations under the Credit Facility are secured by substantially all of our assets, except for our intellectual property, which is subject to a negative pledge covenant.

For additional information regarding the Credit Facility, see Note 6, “Debt” of the notes to our condensed consolidated financial statements.

Contractual Obligations and Commitments

The following table summarizes our contractual obligations at September 30, 2018, and the effect such obligations are expected to have on our liquidity and cash flow in future periods:

	Payments Due by Period				
(in thousands)	Total	Less Than 1 Year	1 – 3 Years	3 – 5 Years	More than 5 Years
Term loans and interest	$ 60,110	$ 4,137	$ 33,583	$ 22,390	$ -
Operating lease commitments (1)	3,079	717	1,471	891	-
Purchasing commitments (2)	19,200	19,200	-	-	-
Total	$ 82,389	$ 24,054	$ 35,054	$ 23,281	$ -

(1) We lease office and laboratory facilities located in Texas, Colorado and Michigan. The lease, as amended, for our Plano, Texas headquarters, which is with Integer, expires in March 2023. The leases, as amended, for our Broomfield, Colorado and Ann Arbor, Michigan facilities expire in September 2022 and June 2022, respectively.

(2) Purchasing commitments represent contractual non-cancelable obligations to purchase goods and services to be used in our operations.

Off-Balance Sheet Arrangements

We have no off-balance sheet arrangements within the meaning of Item 303(a)(4) of Regulation S-K.

Recently Issued Accounting Standards

In the normal course of business, we evaluate all new accounting pronouncements issued by the FASB to determine the potential impact they may have on our Condensed Consolidated Financial Statements. See Note 13 “Recently Issued Accounting Standards” of the notes to the Condensed Consolidated Financial Statements contained in Item 1 of this report for additional information about these recently issued accounting standards and their potential impact on our financial condition or results of operations.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk – There have been no material changes from the Company's interest rate risk as previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Disclosure controls and procedures are designed to ensure that material information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's (the "SEC's") rules and forms and to ensure that such material information is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Based on this evaluation, our CEO and CFO concluded that as of the end of the period covered by this quarterly report, our disclosure controls and procedures were effective.

Changes in Internal Control Over Financial Reporting

We maintain a system of internal controls that are designed to provide reasonable assurance that our books and records accurately reflect, in all material respects, the transactions of the Company and that we meet and achieve our control objectives. From time to time, we may experience changes to our internal controls due to, for example, employee turnover, re-balancing of workloads, extended absences, and promotions of employees.

Beginning January 1, 2018, we implemented ASC 606, *Revenue from Contracts with Customers*. Although the new revenue standard did not have a material impact on our net loss, we did implement changes to our processes related to revenue recognition and the control activities within them. These included the development of new policies based on the five-step model provided in the new revenue standard, new training, ongoing contract review requirements, and gathering of information provided for disclosures.

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Periodically we are a party to various legal actions, both threatened and filed, arising in the normal course of business. While we do not expect that the ultimate resolution of any ordinary course pending actions will have a material effect on our results of operations, financial position, or cash flows, litigation is subject to inherent uncertainties. As such, there can be no assurance that any pending or threatened ordinary course legal action, which we currently believe to be immaterial, does not become material in the future.

On September 19, 2017, Boston Scientific Corporation filed a lawsuit in district court in Suffolk County, Massachusetts, against the Company and three former Boston Scientific employees hired by the Company, alleging tortious interference of contract on the part of the Company and breaches of contract related to non-solicitation and confidentiality by Boston Scientific's former employees. The Company is currently engaging in confidential settlement discussions with Boston Scientific but does not expect any such settlement, if achieved, to have a material adverse impact to the Company. In the event the Company and Boston Scientific are unable to reach a mutually agreed upon settlement, the Company intends to vigorously defend against the allegations.

ITEM 1A. RISK FACTORS

Other than as described below, there have been no material changes to the Company's risk factors as previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2017 and Quarterly Report on Form 10-Q for the quarter ended June 30, 2018.

The following risk factor was previously provided in the Company's Annual Report on Form 10-K for the year ended December 31, 2017. The risk factor has been updated to reference "disruptions caused by human error, malicious acts, earthquakes, hurricanes, tornados, floods, fires, war, terrorist attacks, power losses, hardware failures, systems failures, and similar events." The risk factor is otherwise unchanged.

We are dependent upon sole-source manufacturers and suppliers, including Integer and Minnetronix, making us vulnerable to supply shortages and disruptions, manufacturing problems and price fluctuations, which could harm our business.

In connection with the spin-off, we entered into an exclusive supply agreement with Integer under which we purchase fully assembled Algovita systems and most products, parts and components necessary for the production of Algovita. We also entered into a product component framework agreement that provides Integer with the exclusive right to supply us with products, parts and components necessary for production of future SNM or DBS neurostimulation devices that we may seek to commercialize. Subject to conditions specified in these agreements, Integer is our exclusive and sole source manufacturer and supplier for most products, parts and components of Algovita, while Minnetronix is the sole-source supplier of our external peripheral devices.

Effective December 9, 2016, we entered into a manufacturing and supply amendment with Minnetronix for the supply of our current platform of external peripheral devices used with our Algovita spinal cord stimulation system, including the clinician programmer, patient programmer, the patient charging paddle, the external pulse generator kit and the patient feedback tool. Minnetronix is our sole-source supplier for these items (although we retain the right to manufacture the products ourselves).

As a result, we are vulnerable to supply shortages, failure to maintain adequate safety stock and manufacturing problems encountered by Integer or Minnetronix, including, for example, failure to follow specific protocols and procedures, failure to comply with applicable legal and regulatory requirements, equipment malfunction and environmental factors, failure to properly conduct its own business affairs, and infringement of third-party intellectual property rights, any of which could delay or impede its ability to meet our requirements. Integer or Minnetronix may also be unwilling to supply components for Algovita or our other products or suffer from disruptions in their own supply chains. Even if Integer or Minnetronix were in material default under the supply agreements, as a practical matter, it would require time and investment to qualify new suppliers and comply with regulatory requirements regarding manufacture and supply. In addition, we may not be able to take advantage of price fluctuations or competitive pricing that may become available from alternative supply sources. Our reliance on each of Integer and Minnetronix as our sole source suppliers also subjects us to other risks that could harm our business, including:

- we are not the only customer of either supplier, and they may therefore give other customers' needs higher priority than ours;

- in the event our supply agreement or relationship is terminated, we may have difficulty locating and qualifying alternative suppliers on a timely basis or at all;

- in the event our supply agreement or relationship is terminated, switching suppliers would likely require product redesign and submission to FDA, or other foreign regulatory bodies, which would significantly impede or delay our commercial activities or even suspend them;

- Integer or Minnetronix, which are dependent upon certain sole-source suppliers themselves, could suffer from shortages or delays in their supply chains, including disruptions caused by human error, malicious acts, earthquakes, hurricanes, tornados, floods, fires, war, terrorist attacks, power losses, hardware failures, systems failures, and similar events, which could inhibit or delay their ability to fulfill our orders and meeting our requirements; and

- Integer or Minnetronix could encounter other financial or business hardships unrelated to our demand, which could inhibit their ability to fulfill our orders and meet our requirements.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Our Registration Statement on Form S-3 (File No. 333-220834) was declared effective by the SEC on October 24, 2017.

On February 5, 2018, pursuant to an underwritten shelf takedown, with Piper Jaffray & Co. serving as representative of the several underwriters, we sold 3,248,750 shares of our common stock and received net proceeds of approximately $23.8 million, after deducting underwriting discounts and commissions of approximately $1.8 million and other expenses of approximately $0.4 million. We have used, and continue to use, these proceeds for general corporate purposes, which include expansion of our employee base and sales force, research and development, capital expenditures and funding our operations and working capital needs, as further described in our prospectus supplement filed with the SEC pursuant to Rule 424(b)(5) on February 2, 2018.

On September 14, 2018, pursuant to a second underwritten shelf takedown, with Piper Jaffray & Co. serving as representative of the several underwriters, we sold 3,248,750 shares of our common stock and received net proceeds of approximately $64.6 million, after deducting underwriting discounts and commissions of approximately $4.1 million and other expenses of approximately $0.3 million. We intend to use these proceeds for general corporate purposes, which include expansion of our employee base and sales force, research and development, capital expenditures and funding our operations and working capital needs, as further described in our prospectus supplement filed with the SEC pursuant to Rule 424(b)(5) on September 13, 2018.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Exhibit No.	Description
3.1	Certificate of Incorporation (filed as Exhibit 3.1 to our Current Report on Form 8-K on March 18, 2016, and incorporated herein by reference)
3.2	Bylaws of Nuvectra Corporation (filed as Exhibit 3.2 to our Current Report on Form 8-K on March 18, 2016, and incorporated herein by reference)
4.1	Warrant to Purchase Common Stock, dated March 18, 2016, issued to Oxford Finance LLC (filed as Exhibit 4.1 to our current report on Form 8-K on March 18, 2016, and incorporated herein by reference)
4.2	Warrant to Purchase Common Stock, dated March 18, 2016, issued to Silicon Valley Bank (filed as Exhibit 4.2 to our current report on Form 8-K on March 18, 2016, and incorporated herein by reference)
4.2.2	First Amendment to Warrant to Purchase Common Stock, dated March 23, 2018, issued to SVB Financial Group (successor by assignment from Silicon Valley Bank) (filed as Exhibit 4.2.2 to our quarterly report on Form 10-Q on May 2, 2018, and incorporated herein by reference)
4.3	Warrant to Purchase Common Stock, dated September 28, 2017, issued to Oxford Finance LLC (filed as Exhibit 4.1 to our current report on Form 8-K on October 3, 2017, and incorporated herein by reference)
4.4	Warrant to Purchase Common Stock, dated February 16, 2018, issued to Oxford Finance LLC (filed as Exhibit 4.1 to our current report on Form 8-K on February 21, 2018, and incorporated herein by reference)
4.5	Warrant to Purchase Common Stock, dated September 28, 2018, issued to Oxford Finance LLC (filed as Exhibit 4.1 to our current report on Form 8-K on October 3, 2018, and incorporated herein by reference)
4.6	Warrant to Purchase Common Stock, dated September 28, 2018, issued to Silicon Valley Bank (filed as Exhibit 4.2 to our current report on Form 8-K on October 3, 2018, and incorporated herein by reference)
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended*
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended *
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
100.INS	XBRL Instance Document*
100.SCH	XBRL Extension Schema Document*
100.CAL	XBRL Extension Calculation Linkbase Document*
100.LAB	XBRL Extension Label Linkbase Document*
100.PRE	XBRL Extension Presentation Linkbase Document*
100.DEF	XBRL Extension Definition Linkbase Document*

* Filed herewith.
** Furnished herewith.

SIGNATURES

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

NUVECTRA CORPORATION

Date: October 29, 2018

/s/ Scott F. Drees
Scott F. Drees
Chief Executive Officer
(Principal Executive Officer)

Date: October 29, 2018

/s/ Walter Z. Berger
Walter Z. Berger
Chief Operating Officer and Chief Financial Officer
(Principal Financial Officer)

Date: October 29, 2018

/s/ Jennifer J. Kosharek
Jennifer J. Kosharek
Vice President, Controller and Principal Accounting Officer
(Principal Accounting Officer)

EXHIBIT INDEX

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100.DEF	XBRL Extension Definition Linkbase Document*

* Filed herewith.
** Furnished herewith.

Exhibit 31.1

CERTIFICATION

I, Scott F. Drees, certify that:

1 I have reviewed this quarterly report on Form 10-Q for the fiscal quarter ended September 30, 2018 of Nuvectra Corporation;

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

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

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

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

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

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

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

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

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

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

Date: October 29, 2018

/s/ Scott F. Drees
Scott F. Drees
Chief Executive Officer

Exhibit 31.2

CERTIFICATION

I, Walter Z. Berger, certify that:

1 I have reviewed this quarterly report on Form 10-Q for the fiscal quarter ended September 30, 2018 of Nuvectra Corporation;

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

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

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

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

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

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

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

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

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

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

Date: October 29, 2018

/s/ Walter Z. Berger
Walter Z. Berger
Chief Operating Officer and Chief Financial Officer

Exhibit 32.1

CERTIFICATION

Pursuant to 18 U.S.C. Section 1350 as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, each of the undersigned officers of Nuvectra Corporation (the "Company"), does hereby certify, to such officer's knowledge, that:

The Quarterly Report on Form 10-Q for the quarter ended September 30, 2018 (the "Form 10-Q") of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: October 29, 2018

/s/ Scott F. Drees
Scott F. Drees
Chief Executive Officer
(Principal Executive Officer)

Dated: October 29, 2018

/s/ Walter Z. Berger
Walter Z. Berger
Chief Operating Officer and Chief Financial Officer
(Principal Financial Officer)

This certification is being furnished solely to accompany this Form 10-Q pursuant to 18 U.S.C. Section 1350, and is not being filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, and is not to be deemed incorporated by reference into any filing of the Company except to the extent the Company specifically incorporates it by reference therein.