SeaSpine Holdings Corp
Form 10-Q
August 04, 2017
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2017
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to
COMMISSION FILE NO. 001-36905

SeaSpine Holdings Corporation
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE	47-3251758
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	(I.R.S. EMPLOYER IDENTIFICATION NO.)
5770 Armada Drive, Carlsbad, California	92008
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES)	(ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (760) 727-8399

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 x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a 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 o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o
	Emerging growth company x

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. o

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

The number of shares of the registrant's common stock, $0.01 par value, outstanding as of July 31, 2017 was 12,551,541.

SEASPINE HOLDINGS CORPORATION
INDEX

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SEASPINE HOLDINGS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Total revenue, net	$34,196	$33,201	$66,090	$64,600
Cost of goods sold	13,994	13,930	27,166	28,213
Gross profit	20,202	19,271	38,924	36,387
Operating expenses:				
Selling, general and administrative	24,249	26,989	48,219	52,363
Research and development	3,344	3,181	6,394	5,934
Intangible amortization	792	1,281	1,584	2,562
Total operating expenses	28,385	31,451	56,197	60,859
Operating loss	(8,183)	(12,180)	(17,273)	(24,472)
Other income (expense), net	185	(232)	172	26
Loss before income taxes	(7,998)	(12,412)	(17,101)	(24,446)
Provision (benefit) for income taxes	45	(429)	45	(456)
Net loss	$(8,043)	$(11,983)	$(17,146)	$(23,990)
Net loss per share, basic and diluted	$(0.68)	$(1.07)	$(1.46)	$(2.15)
Weighted average shares used to compute basic and diluted net loss per share	11,888	11,179	11,705	11,173

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

SEASPINE HOLDINGS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Unaudited)
(In thousands)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net loss	$(8,043)	$(11,983)	$(17,146)	$(23,990)
Other comprehensive income (loss)				
Foreign currency translation adjustments	320	(104)	401	86
Comprehensive loss	$(7,723)	$(12,087)	$(16,745)	$(23,904)

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

SEASPINE HOLDINGS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(In thousands, except par value data)

	June 30, 2017	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$12,287	$ 14,566
Trade accounts receivable, net of allowances of $522 and $483	21,689	20,982
Inventories	42,515	45,299
Prepaid expenses and other current assets	3,130	1,813
Total current assets	79,621	82,660
Property, plant and equipment, net	22,986	21,863
Intangible assets, net	38,568	41,785
Other assets	788	857
Total assets	$141,963	$ 147,165
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Short-term debt	$—	$ 445
Accounts payable, trade	10,413	8,537
Accrued compensation	3,862	4,393
Accrued commissions	4,801	4,398
Contingent consideration liabilities	1,860	2,855
Accrued expenses and other current liabilities	4,681	3,790
Total current liabilities	25,617	24,418
Long-term borrowings under credit facility	3,994	3,835
Contingent consideration liabilities	3,917	5,125
Other liabilities	2,969	2,810
Total liabilities	36,497	36,188
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $0.01 par value; 15,000 authorized; no shares issued and outstanding at June 30, 2017 and December 31, 2016	—	—
Common stock, $0.01 par value; 60,000 authorized; 12,407 and 11,258 shares issued and outstanding at June 30, 2017 and December 31, 2016, respectively	124	113
Additional paid-in capital	191,976	180,753
Accumulated other comprehensive income	1,673	1,272
Accumulated deficit	(88,307)	(71,161)
Total stockholders' equity	105,466	110,977
Total liabilities and stockholders' equity	$141,963	$ 147,165

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

5

SEASPINE HOLDINGS CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Six Months Ended June 30,	
	2017	2016
OPERATING ACTIVITIES:		
Net loss	$(17,146)	$(23,990)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	5,442	6,248
Instrument replacement expense	724	760
Impairment of spinal instruments	—	672
Provision for excess and obsolete inventories	2,797	3,652
Amortization of debt issuance costs	69	71
Deferred income tax provision (benefit)	51	(88)
Stock-based compensation	2,708	3,587
Loss from change in fair value of contingent consideration liabilities	345	—
Changes in assets and liabilities:		
Accounts receivable	(553)	2,524
Inventories	937	(9)
Prepaid expenses and other current assets	(1,310)	1,481
Other non-current assets	(10)	5
Accounts payable	177	(3,683)
Accrued commissions	403	239
Accrued expenses and other current liabilities	1,384	818
Other non-current liabilities	42	213
Net cash used in operating activities	(3,940)	(7,500)
INVESTING ACTIVITIES:		
Purchases of property and equipment	(2,973)	(3,446)
Additions to technology assets	(200)	—
Net cash used in investing activities	(3,173)	(3,446)
FINANCING ACTIVITIES:		
Repayments of short-term debt	(445)	—
Proceeds from issuance of common stock- employee stock purchase plan	453	356
Proceeds from issuance of common stock, net of offering costs- ATM transactions	4,566	—
Proceeds from exercise of stock options	35	—
Repurchases of common stock for income tax withheld upon vesting of restricted stock awards	(46)	(2)
Net cash provided by financing activities	4,563	354
Effect of exchange rate changes on cash and cash equivalents	271	150
Net change in cash and cash equivalents	(2,279)	(10,442)
Cash and cash equivalents at beginning of period	14,566	33,429
Cash and cash equivalents at end of period	$12,287	$22,987
Non-cash operating activities:		
Settlement of bonus in payment of restricted stock units	$970	$—
Non-cash investing activities:		
Property and equipment in liabilities	$2,275	$1,453
	$2,548	$—

Settlement of contingent closing consideration liabilities in connection with acquisition of business (see Note 8)

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

SEASPINE HOLDINGS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF EQUITY
(Unaudited)
(In thousands)

	Common Stock		Additional	Accumulated Other		Total
	Number of Shares	Amount	Paid-In Capital	Comprehensive Income	Accumulated Deficit	Stockholders' Equity
Balance December 31, 2016	11,258	$ 113	$ 180,753	$ 1,272	$ (71,161)	$ 110,977
Net loss	—	—	—	—	(17,146)	(17,146)
Foreign currency translation adjustment	—	—	—	401	—	401
Restricted stock awards/units issued	252	2	968	—	—	970
Issuance of common stock under employee stock purchase plan	71	1	452	—	—	453
Issuance of common stock- NLT Spine Ltd contingent closing consideration	350	3	2,545	—	—	2,548
Issuance of common stock, net of offering costs- ATM transactions	477	5	4,561	—	—	4,566
Issuance of common stock- exercise of stock options	5	—	35	—	—	35
Repurchases of common stock for income tax withheld upon vesting of restricted stock awards	(6)	—	(46)	—	—	(46)
Stock-based compensation	—	—	2,708	—	—	2,708
Balance June 30, 2017	12,407	124	191,976	1,673	(88,307)	105,466

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

SEASPINE HOLDINGS CORPORATION
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BUSINESS AND BASIS OF PRESENTATION

Business

SeaSpine Holdings Corporation was incorporated in Delaware on February 12, 2015 in connection with the spin-off of the orthobiologics and spinal instrumentation business of Integra LifeSciences Holdings Corporation, a diversified medical technology company. The spin-off occurred on July 1, 2015. Unless the context indicates otherwise, (i) references to "SeaSpine" or the "Company" refer to SeaSpine Holdings Corporation and its wholly-owned subsidiaries, and (ii) references to "Integra" refer to Integra LifeSciences Holdings Corporation and its subsidiaries other than SeaSpine.

Basis of Presentation and Principles of Consolidation

The Company prepared the unaudited interim condensed consolidated financial statements included in this report in accordance with accounting principles generally accepted in the U.S. (GAAP) for interim financial information and the rules and regulations of the Securities and Exchange Commission (SEC) related to quarterly reports on Form 10-Q.

The Company’s financial statements are presented on a consolidated basis. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Intercompany accounts and transactions have been eliminated in consolidation. The unaudited interim condensed consolidated financial statements do not include all information and disclosures required by GAAP for annual audited financial statements and should be read in conjunction with the Company’s consolidated financial statements and notes thereto for the year ended December 31, 2016 included in the Company’s Annual Report on Form 10-K filed with the SEC. In the opinion of management, the unaudited interim condensed consolidated financial statements included in this report have been prepared on the same basis as the Company's audited consolidated financial statements and include all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the financial position, results of operations, cash flows, and statement of equity for periods presented. The results for the three and six months ended June 30, 2017 are not necessarily indicative of the results expected for the full year. The condensed consolidated balance sheet as of December 31, 2016 was derived from the audited consolidated financial statements for the year ended December 31, 2016.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities, and the reported amounts of revenues and expenses. Significant estimates affecting amounts reported or disclosed in the consolidated financial statements include allowances for doubtful accounts receivable and sales returns and other credits, net realizable value of inventories, discount rates and estimated projected cash flows used to value and test impairments of identifiable intangible and long-lived assets, assumptions related to the timing and probability of the product launch dates, discount rates matched to the estimated timing of payments, and probability of success rates and discount adjustments on the related cash flows for contingent considerations in business combinations, depreciation and amortization periods for identifiable intangible and long-lived assets, computation of taxes, valuation allowances recorded against deferred tax assets, the valuation of stock-based compensation and loss

contingencies. These estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the current circumstances. Actual results could differ from these estimates.

Recent Accounting Standards Not Yet Adopted

The Company qualifies as an “emerging growth company” (EGC) pursuant to the provisions of the Jumpstart Our Business Startups (JOBS) Act and elected to take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act of 1933, as amended, which permits EGCs to defer compliance with new or revised accounting standards (the EGC extension) until non-issuers are required to comply with such standards. Accordingly, so long as the Company continues to qualify as an EGC, the Company will not have to adopt or comply with new or revised accounting standards until non-issuers are required to adopt or comply with such standards.

In May 2014, the Financial Accounting Standards Board (FASB) issued Update No. 2014-09, Revenue from Contracts with

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Customers (Topic 606). The new standard provides a five-step approach to be applied to all contracts with customers. The new standard also requires expanded disclosures about revenue recognition. The new standard as amended by ASU 2015-14 will be effective for the Company beginning on January 1, 2019, and for interim periods within annual periods beginning on January 1, 2020. The Company performed a preliminary assessment of the impact of this new standard on its consolidated financial statements. In assessing the impact, the Company has outlined all revenue streams, and considered the five steps outlined in the standard for product sales, from which substantially all the Company's revenue is generated. The Company will continue to evaluate the future impact of the new standard throughout 2017. Overall, the Company does not currently expect the adoption of the new guidance to have a material impact on the amounts reported in its consolidated financial statements, but will impact certain disclosures regarding revenue recognition.

In February 2016, the FASB issued Update No. 2016-02, Leases (Topic 842). The new standard requires lessees to recognize lease liabilities and corresponding right-of-use assets for all leases with lease terms of greater than twelve months. It also changes the definition of a lease and expands the disclosure requirements of lease arrangements. The new standard must be adopted using the modified retrospective approach. The standard will be effective for the Company beginning on January 1, 2020, and interim periods within annual periods beginning on January 1, 2021, with early adoption permitted. The Company does not plan to early adopt and expects to apply the transition practical expedients allowed by the standard. Note 11 to the Condensed Consolidated Financial Statements provides details on the Company’s current lease arrangements. While the Company continues to evaluate the impact of this new standard on its consolidated financial statements, the Company expects the primary impact will be to record right-of-use assets and lease liabilities for existing operating leases in the consolidated balance sheets. The Company does not expect the adoption of this new standard to have a material impact on its consolidated results of operations or cash flows.

In August 2016, the FASB issued Update No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash
Receipts and Cash Payments. This new standard addresses eight specific cash flow issues related to cash receipts and cash payments with the objective of reducing the existing diversity of presentation and classification in the statement of cash flows. The new standard will be effective for the Company beginning on January 1, 2019, and interim periods within annual periods beginning on January 1, 2020. Early adoption is permitted and should be applied using a retrospective transition method to each period presented. The Company is in the process of evaluating the impact of this standard on its consolidated financial statements.

In May 2017, the FASB issued Update No. 2017-09, Compensation- Stock Compensation (Topic 718): Scope of Modification Accounting. The new standard provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The new standard will be effective for the Company beginning on January 1, 2018, and interim periods within those annual periods, beginning on January 1, 2018. The new standard should be applied prospectively to an award modified on or after the adoption date. The Company is in the process of evaluating the impact of this standard on its consolidated financial statements.

Recently Adopted Accounting Standards

In August 2014, the FASB issued Update No. 2014-15, Presentation of Financial Statements - Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern. The amendment requires management to evaluate, for each annual and interim reporting period, whether there are conditions and events, considered in the aggregate, that raise substantial doubt about an entity’s ability to continue as a going concern within one year after the date the financial statements are issued or are available to be issued. If substantial doubt is raised, additional disclosures around management’s plan to alleviate these doubts are required. This update became effective for all annual periods and interim reporting periods ending after December 15, 2016. The

implementation of the amended guidance in 2016 did not have an impact on current disclosures in the Company's consolidated financial statements.

In March 2016, the FASB issued Update No. 2016-09, Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting. Under current accounting guidance an entity is required to report excess tax benefits and tax deficiencies to the extent of previous windfalls in equity when the tax benefit is realized. Excess settlements are currently reported as cash inflows from financing activities. The amendment requires that an entity present all excess tax benefits and all tax deficiencies as income tax expense or benefit in the statement of operations to be applied using a prospective transition method. Related tax settlements are to be presented as cash inflows from operating activities using either a prospective or retrospective transition method. The amendment removes the requirement to delay recognition of an excess tax benefit until the tax benefit is realized, which should be applied using a modified retrospective transition method.

The Company elected to early adopt ASU 2016-09 as of January 1, 2016, the beginning of the annual period that includes the interim period of adoption. Amendments related to accounting for excess tax benefits (deficiencies) have been adopted

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

prospectively, and recognition of excess tax benefits (deficiencies) against income tax expenses was immaterial for the year ended December 31, 2016. The Company elected to apply the change in classification for excess tax benefits in the statement of cash flows on a prospective basis, and elected to continue estimating stock-based compensation award forfeitures in determining the amount of compensation cost to be recognized each period.

In January 2017, the FASB issued Update No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business. The amendments in this update provide a screen to determine when a set of transferred assets and activities is not 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. If the screen is not met, the amendments in this update (1) 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 (2) remove the evaluation of whether a market participant could replace missing elements. The Company elected to early adopt this guidance as of December 31, 2016 and will apply the guidance on a prospective basis.

In July 2015, the FASB issued Update No. 2015-11, Simplifying the Measurement of Inventory (Topic 330). The new guidance
requires an entity to measure inventory within the scope of the amendment at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The guidance was effective for the Company beginning on January 1, 2017, and interim periods within annual periods beginning on January 1, 2018. Adoption of this new guidance has had no impact on the Company’s consolidated financial statements.

Net Loss Per Share

Basic and diluted net loss per share was calculated using the weighted-average number of shares of common stock outstanding during the period. The weighted average number of shares used to compute diluted net loss per share excludes any assumed exercise of stock options, and any assumed issuance of common stock under restricted stock awards and units as the effect would be antidilutive. Common stock equivalents of 3.4 million and 2.8 million shares for the three and six months ended June 30, 2017 and 2016, respectively, were excluded from the calculation because of their antidilutive effect.

3. DEBT AND INTEREST

Credit Agreement
On December 24, 2015, the Company entered into a three-year credit facility (the Credit Facility), with Wells Fargo Bank, National Association. The Credit Facility provides an asset-backed revolving line of credit of up to $30.0 million in borrowing capacity with a maturity date of December 24, 2018, which maturity date is subject to a one-time, one-year extension at the Company's election. In connection with the Credit Facility, the Company was required to become a guarantor and to provide a security interest in substantially all its assets for the benefit of the counterparty.

Borrowings under the Credit Facility accrue interest at the rate then applicable to base rate loans (as customarily defined), unless and until converted into LIBOR rate loans (as customarily defined) in accordance with the terms of the Credit Facility. Borrowings bear interest at a floating annual rate equal to (a) during any month for which the Company's average excess availability (as customarily defined) is greater than $20.0 million, base rate plus (i) 1.25 percentage points for base rate loans and (ii) LIBOR rate plus 2.25 percentage points for LIBOR rate loans, (b) during any month for which the Company's average excess availability is greater than $10.0 million but less than or equal to

$20.0 million, (i) base rate plus 1.50 percentage points for base rate loans and (ii) LIBOR rate plus 2.50 percentage points for LIBOR rate loans and (c) during any month for which the Company's average excess availability is less than or equal to $10.0 million, (i) base rate plus 1.75 percentage points for base rate loans and (ii) LIBOR rate plus 2.75 percentage points for LIBOR rate loans. The Company will also pay an unused line fee in an amount equal to 0.375% per annum of the unused Credit Facility amount. The unused line fee is due and payable on the first day of each month.

In September 2016, the Company borrowed $3.3 million from the revolving line of credit. The Company elected to have the LIBOR rate apply to the amount borrowed with an interest period of six months commencing on September 28, 2016, which was further extended for another interest period of six months commencing on March 28, 2017. At June 30, 2017, there was $4.0 million outstanding in total debt and $15.8 million borrowing capacity under the Credit Facility. Debt issuance costs and legal fees related to the Credit Facility totaling $0.4 million were recorded as a deferred asset and are being amortized ratably over the term of the arrangement.

The Credit Facility contains various customary affirmative and negative covenants, including prohibiting the Company from incurring indebtedness without the lender’s consent. The Credit Facility also includes a financial covenant that requires the Company

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

to maintain a minimum fixed charge coverage ratio of 1.10 to 1.00 for the applicable measurement period, if the Company's Total Liquidity (as defined in the Credit Facility) is less than $5.0 million. The Company was in compliance with all applicable covenants at June 30, 2017.

The Credit Facility also includes customary events of default, including events of default relating to non-payment of amounts due under the Credit Facility, material inaccuracy of representations and warranties, violation of covenants, bankruptcy and insolvency, failure to comply with health care laws, violation of certain of the Company’s existing agreements, and the occurrence of a change of control. Under the Credit Facility, if an event of default occurs, Wells Fargo Bank, National Association will have the right to terminate the commitments and accelerate the maturity of any loans outstanding.

Insurance Premium Finance Agreements

In July 2016, the Company entered into two insurance premium finance agreements (the Finance Agreements) with First Insurance Funding Corporation and AFCO Acceptance Corporation (the Lenders), under which the Lenders agreed to pay premiums, taxes and fees to insurance companies on the Company's behalf for various insurance policies. The Company financed an aggregate of $1.2 million under the Finance Agreements with annual interest rates between 2% and 4%. The Company recorded the total amounts due to the Lenders as short-term debt on the balance sheet. At June 30, 2017, the financed amount plus interest was paid off and no amounts were outstanding under the Finance Agreements.

4. TRANSACTIONS WITH INTEGRA

Prior to the spin-off, and pursuant to certain supply agreements subsequent to the spin-off, SeaSpine purchased a portion of raw materials and finished goods from Integra for SeaSpine's Mozaik family of products, and SeaSpine contract manufactured certain finished goods for Integra. The Company's purchases of raw materials and Mozaik product finished goods from Integra totaled $0.3 million and $0.5 million for the three months ended June 30, 2017 and 2016, respectively, and $0.3 million and $1.0 million for the six months ended June 30, 2017 and 2016, respectively. The Company's sale of finished goods sold to Integra under its contract manufacturing arrangement totaled $0.2 million and $0.4 million for the three and six months ended June 30, 2017, respectively, and $0.2 million for both the three and six months ended June 30, 2016.

Pursuant to a transition services agreement, Integra and SeaSpine provided certain services to one another following the spin-off, and Integra and SeaSpine will indemnify each other against certain liabilities arising from their respective businesses. Under this agreement, Integra provided the Company with certain support functions, including information technology, accounting and other financial functions, regulatory affairs and quality assurance, human resources and other administrative support. The Company incurred no costs under the agreement for the three and six months ended June 30, 2017 and approximately $0.1 million and $0.3 million of costs under the agreement for the three and six months ended June 30, 2016, respectively. Subsequent to the spin-off, Integra also collected trade receivables from customers on behalf of the Company. The outstanding amount owed by Integra to the Company was immaterial as of June 30, 2017 and December 31, 2016.

5. INVENTORIES

Inventories consisted of the following:

	June 30, 2017	December 31, 2016
	(In thousands)	
Finished goods	$30,965	$ 30,922

Work in process	8,345	10,554
Raw materials	3,205	3,823
	$42,515	$ 45,299

6. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at historical cost less accumulated depreciation and any impairment charges. The Company provides for depreciation using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the lesser of the lease term or the useful life. The cost of major additions and improvements is capitalized, while maintenance and repair costs that do not improve or extend the lives of the respective assets are charged to operations as incurred. The cost of computer software obtained for internal use is accounted for in accordance with the Accounting Standards Codification (ASC) 350-40, Internal-Use Software.

The cost of purchased spinal instruments which the Company consigns to hospitals and independent sales agents to support surgeries is initially capitalized as construction in progress. The amount is then reclassified to spinal instrument sets and

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

depreciation is initiated when instruments are put together in a newly built set with spinal implants, or directly expensed for the instruments that are used to replace damaged instruments in an existing set. The depreciation expense and direct expense for replacement instruments are recorded in selling, general and administrative expense.
Property, plant and equipment balances and corresponding useful lives were as follows:

	June 30, 2017	December 31, 2016	Useful Lives
	(In thousands)		
Leasehold improvement	$5,222	$ 5,003	Lease Term
Machinery and production equipment	7,016	6,826	3-10 years
Spinal instrument sets	22,544	26,618	5 years
Information systems and hardware	7,283	6,918	3-7 years
Furniture and fixtures	1,072	1,058	3-5 years
Construction in progress	8,627	7,828	
Total	51,764	54,251	
Less accumulated depreciation and amortization	(28,778)	(32,388)	
Property, plant and equipment, net	$22,986	$ 21,863	

Depreciation and amortization expenses totaled $1.0 million and $1.1 million for the three months ended June 30, 2017 and 2016, respectively, and $2.0 million and $2.3 million for the six months ended June 30, 2017 and 2016, respectively. The cost of purchased instruments used to replace damaged instruments in existing sets and recorded directly to the instrument replacement expense totaled $0.2 million for each of the three months ended June 30, 2017 and 2016, and $0.7 million and $0.8 million for the six months ended June 30, 2017 and 2016, respectively.

For the three and six months ended June 30, 2016, the Company recorded impairment charges totaling $0.6 million and $0.7 million, respectively, against spinal instruments that are no longer expected to place into service. No impairment charges against spinal instruments were recorded for the three or six months ended June 30, 2017.

7. IDENTIFIABLE INTANGIBLE ASSETS
Identifiable intangible assets are initially recorded at fair value at the time of acquisition, generally using an income or cost approach. The Company capitalizes costs incurred to renew or extend the term of recognized intangible assets and amortizes those costs over their expected useful lives.
The components of the Company's identifiable intangible assets were as follows:

	June 30, 2017			
	Weighted Average Life	Cost	Accumulated Amortization	Net
	(Dollars in thousands)			
Product technology	12 years	$40,769	$ (24,051)	$16,718
Customer relationships	12 years	56,830	(34,980)	21,850
Trademarks/brand names	—	300	(300)	—
		$97,899	$ (59,331)	$38,568

	December 31, 2016			
	Weighted Average Life	Cost	Accumulated Amortization	Net
	(Dollars in thousands)			
Product technology	12 years	$40,569	$ (22,218)	$18,351
Customer relationships	12 years	56,830	(33,396)	23,434

Trademarks/brand names —	300	(300	) —
	$97,699	$ (55,914	) $41,785

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Annual amortization expense (including amounts reported in cost of goods sold) is expected to be approximately $6.8 million in 2017, $6.5 million in 2018, $5.8 million in 2019, $4.9 million in 2020 and $4.9 million in 2021. Amortization expense totaled $1.7 million and $1.9 million for the three months ended June 30, 2017 and 2016, respectively, and included $0.9 million and $0.6 million, respectively, of amortization of product technology intangible assets that is presented within cost of goods sold. Amortization expense totaled $3.4 million and $3.9 million for the six months ended June 30, 2017 and 2016, respectively, and included $1.8 million and $1.3 million, respectively, of amortization of product technology intangible assets that is presented within cost of goods sold.

8. BUSINESS COMBINATIONS

In August 2016, the Company entered into an asset purchase agreement with N.L.T Spine Ltd. (NLT), and NLT Spine, Inc., a wholly owned subsidiary of NLT, pursuant to which the Company agreed to purchase certain of the assets of NLT’s medical device business, including substantially all of NLT’s medical device intellectual property related to the ownership, design, development, manufacture, marketing and commercial exploitation of certain expandable interbody devices. The acquisition was undertaken to increase the Company's product offering in expandable interbody devices.

Upon the terms and subject to the conditions of the acquisition agreement, at the initial closing (as defined in the agreement), the Company entered into (i) an exclusive license agreement with NLT, pursuant to which the Company received an exclusive, worldwide license to make, use, import, offer for sale, sell and otherwise commercially exploit NLT’s expandable interbody device products , (ii) a transition services agreement with NLT, pursuant to which NLT agreed to provide certain services with respect to the continued development of the acquired intellectual property and (iii) a non-competition and non-solicitation agreement with NLT, pursuant to which NLT and its affiliates agreed not to compete with the Company with respect to the acquired intellectual property, subject to certain exceptions.

The purchase price consisted of an initial cash payment to NLT of $1.0 million, which was paid on September 26, 2016 upon the initial closing, and the issuance of 350,000 shares of the Company’s common stock with the total fair value of $2.5 million at issuance in January 2017 as contingent closing consideration upon the satisfaction of certain conditions, including FDA 510(K) clearance of one of the acquired product technologies. In accordance with the terms of the asset purchase agreement, the number of shares issued was determined based on the volume weighted average closing price (VWAP) of the common stock during the 20 trading day period ending one trading day prior to the issuance date, subject to a minimum and maximum VWAP of $10.00 and $17.00, respectively. The VWAP over such 20-trading day period was $7.58 and therefore $10.00 was used.

The Company is also obligated to pay up to a maximum of $5.0 million in milestone payments, payable at the Company's election in cash or in shares of its common stock, which are contingent on the Company's achievement of four independent events related to the commercialization of the acquired product technologies. Additionally, the Company is required to pay royalty payments, in cash, to NLT equal to declining (over time) percentages of the Company’s future net sales of certain of the acquired product technologies not to exceed $43.0 million in the aggregate. The Company has the option to terminate any future obligation to make royalty payments by making a one-time cash payment to NLT of $18.0 million.

The Company accounted for this transaction as a business combination in accordance with ASC 805 Business Combinations, and as such, the assets acquired have been recorded at their respective fair values. There were no liabilities assumed. The determination of fair value for the identifiable intangible assets acquired requires extensive use of estimates and judgments. Significant estimates include, measurements estimating cash flows and determining the appropriate discount rate, which are considered Level 3 inputs, as defined using the fair value concepts defined in ASC 820. Intangible assets acquired were valued at $9.3 million as of the initial closing date and recorded as product

technology intangible assets, which are being amortized ratably over a useful life of 10 years from the initial closing. Acquisition costs of $0.5 million incurred were recorded as selling, marketing and administrative expenses.

The following table summarizes the estimated fair value of total consideration to be paid to NLT as of September 26, 2016, the date of the initial closing. The Company estimated the fair value of the contingent consideration, including contingent milestone payments and contingent royalty payments, using a probability weighted approach that considers the possible outcomes based on assumptions related to the timing and probability of the product launch dates, discount rates matched to the timing of payments, and probability of success rates and discount adjustments on the related cash flows. Subsequent to the acquisition date, at each reporting period, the contingent consideration liabilities will be remeasured at current fair value with changes to be recorded in the consolidated statements of operations. The total purchase price was allocated entirely to product technology intangible asset.

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(In thousands)	
Cash paid for purchase	$1,000
Contingent closing consideration	2,930
Contingent milestone payments	2,310
Contingent royalty payments	3,010
Total purchase price	$9,250

The unaudited pro forma financial information set forth below assumes that the NLT purchased assets had been acquired on January 1, 2016. The unaudited pro forma financial information includes the effect of estimated amortization charges for acquired intangible assets of $0.2 million and $0.4 million for the three and six months ended June 30, 2016, respectively, and the estimated research and development expenses for the purchased assets of $0.3 million and $0.6 million for the three and six months ended June 30, 2016, respectively. There was no adjustment to the total revenues. The unaudited pro forma information is presented for informational purposes only and is not indicative of the results of operations that would have been achieved if the acquisition had taken place at the beginning of the periods presented.

The actual amortization charges for acquired intangible assets and research and development expenses for the purchased assets are included in the consolidated statement of operations for the three and six months ended June 30, 2017, and therefore no adjustment was made to such statement.

(In thousands, except per share data)	Three Months Ended June 30, 2016	Six Months Ended June 30, 2016
Operating loss	$(12,685)	$(25,483)
Net loss	(12,488)	(25,001)
Net loss per share, basic and diluted	$(1.12)	$(2.24)
Weighted average shares used to compute basic and diluted net loss per share	11,179	11,173

9. FAIR VALUE MEASUREMENTS

The fair values of the Company's assets and liabilities, including contingent consideration liabilities, are measured at fair value on a recurring basis, and are determined under the fair value categories as follows (in thousands):

	Total	Quoted Price in Active Market (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2017:				
Contingent consideration liabilities- current	$1,860	$ —	$ —	$ 1,860
Contingent consideration liabilities- non-current	3,917	—	—	3,917
Total contingent consideration	$5,777	$ —	$ —	$ 5,777

Contingent consideration liabilities are classified within Level 3 of the fair value hierarchy because they use significant unobservable inputs. For those liabilities, fair value is determined using a probability-weighted discounted cash flow model, and the significant inputs which are not observable in the market. The significant inputs include

assumptions related to the timing and probability of the product launch dates, discount rates matched to the timing of payments, and probability of success rates.

The following table sets forth the changes in the estimated fair value of the Company's liabilities measured on a recurring basis using significant unobservable inputs (Level 3) for the three and six months ended June 30, 2017. The gain from change in fair value of contingent closing consideration is the difference between the fair value of shares expected to be issued to NLT based on assumptions as of December 31, 2016, including the forecasted issuance date and stock price and the fair value of the shares actually issued to NLT on January 31, 2017. The loss from change in fair value of contingent milestone and royalty payments resulted from the passage of time, updated discount rates matched to the estimated timing of payments, actual net sales of certain products for the three and six months ended June 30, 2017, and updated estimated net sales for the remaining of 2017.

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Three months ended June 30, 2017	(in thousands)
Balance as of March 31, 2017	5,617
Loss from change in fair value of contingent milestone and royalty payments recorded in selling, general and administrative expenses	160
Fair value at June 30, 2017	$ 5,777

Six months ended June 30, 2017	(in thousands)
Balance as of January 1, 2017	$ 7,980
Contingent consideration liabilities settled	(2,548)
Gain from change in fair value of contingent closing consideration recorded in other income	(112)
Loss from change in fair value of contingent milestone and royalty payments recorded in selling, general and administrative expenses	457
Fair value at June 30, 2017	$ 5,777

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

10. EQUITY AND STOCK-BASED COMPENSATION

Common Stock

On January 31, 2017, the Company issued 350,000 shares of common stock to NLT as the settlement of contingent closing consideration pursuant to the terms of the asset purchase agreement entered into with NLT in August 2016. The total fair value of such shares was $2.5 million at issuance. See Note 8, "Business Combinations" above.

In August 2016, the Company entered into an equity distribution agreement (Distribution Agreement) with Piper Jaffray & Co. (Piper Jaffray), pursuant to which the Company may offer and sell shares of its common stock in “at the market” (ATM) offerings (as defined in Rule 415 of the Securities Act of 1933, as amended) having an aggregate offering price up to $25.0 million in gross proceeds from time to time through Piper Jaffray acting as sales agent. The shares offered and sold under the Distribution Agreement are covered by a registration statement on Form S-3 that was declared effective on August 24, 2016. Under the Distribution Agreement, during the three months ended June 30, 2017, the Company sold 477,478 shares of common stock at an average price per share of $10.03 and received net proceeds of approximately $4.6 million, net of offering costs. The Company intends to use the net proceeds for general corporate purposes, including sales and marketing expenditures aimed at growing its business, and research and development expenditures focused on product development. The Company has the capacity to issue up to approximately $20.2 million of additional shares of common stock under the Distribution Agreement as of June 30, 2017. Future sales, if any, will depend on a variety of factors including, but not limited to, market conditions, the trading price of the Company’s common stock and the Company’s capital needs.

Subsequent to June 30, 2017, the Company sold an additional 522,522 shares of common stock at an average price per share of $12.18 and received net proceeds of approximately $6.0 million, net of offering costs.

Equity Award Plans

As of June 30, 2015, Integra had stock options, restricted stock awards, performance stock awards, contract stock awards and restricted stock units outstanding under three plans, the 2000 Equity Incentive Plan, the 2001 Equity Incentive Plan, and the 2003 Equity Incentive Plan. In connection with the spin-off, Integra equity awards granted to individuals who became employees of SeaSpine were converted to equity awards denominated in SeaSpine common stock. In general, each post-conversion award is subject to the same terms and conditions as were applicable to the pre-conversion award.
In May 2015, the Company adopted the 2015 Incentive Award Plan (the 2015 Plan), under which the Company can grant its employees and non-employee directors incentive stock options and non-qualified stock options, restricted stock, performance stock, dividend equivalent rights, stock appreciation rights, stock payment awards and other incentive awards. The Company may issue up to 2,000,000 shares of its common stock under the 2015 Plan. On January 27, 2016, the Company's board of directors approved an amendment and restatement of the 2015 Plan, pursuant to which the share reserve was increased by 300,000 shares over the original share reserve under the 2015 Plan, and on March 30, 2016, the board of directors approved a second amendment and restatement of the 2015 Plan, pursuant to which the share reserve was increased by an additional 1,209,500 shares of common stock. The Company's stockholders approved such amendments and restatements on June 7, 2016. An aggregate of 3,509,500 shares are reserved for issuance under the second amended and restated 2015 Plan. As of June 30, 2017, there were 307,634 shares available to grant under the second amended and restated 2015 Plan.

In 2016, the Company established the 2016 Employment Inducement Incentive Award Plan (the 2016 Plan). The plan is a broad-based incentive plan which allows for the issuance of stock-based awards, including non-qualified stock

options, restricted stock awards, performance awards, restricted stock unit awards and stock appreciation rights, to any prospective officer or other employee who has not previously been an employee or director of SeaSpine or an affiliate or who is commencing employment with SeaSpine or an affiliate following a bona-fide period of non-employment by SeaSpine or an affiliate. An aggregate of 1,000,000 shares are reserved for issuance under the 2016 Plan. The Company has not awarded any shares under the 2016 Plan as of June 30, 2017.

Restricted Stock Awards and Restricted Stock Units

The Company expenses the fair value of restricted stock awards and restricted stock units on an accelerated basis over the vesting period or requisite service period, whichever is shorter. Stock-based compensation expense related to restricted stock awards, and restricted stock units includes an estimate for forfeitures. The expected forfeiture rate of all equity-based compensation is based on historical experience of pre-vesting forfeitures on awards by each homogenous group of shareowners and is estimated to be 12% annually for all non-executive employees for the six months ended June 30, 2017 and 10% annually

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

for the six months ended June 30, 2016. There is no forfeiture rate applied for non-employee directors and executive employees as their pre-vesting forfeitures are anticipated to be highly unlikely. As individual grant awards become fully vested, stock-based compensation expense is adjusted to recognize actual forfeitures.
During the three and six months ended June 30, 2017, the Company granted 116,628 and 120,610 shares of restricted stock awards to non-employee directors, respectively, and 13,153 and 743,955 shares of restricted stock units to employees, respectively. Of the total restricted stock units granted to employees, 131,523 shares were issued for bonuses earned under the annual incentive program for corporate and individual performance in 2016. During the three and six months ended June 30, 2016, the Company granted 75,075 shares of restricted stock awards to non-employee directors. There were no restricted stock units granted during the three or six months ended June 30, 2016. As of June 30, 2017, there was approximately $4.2 million of total unrecognized compensation expense related to the unvested portions of restricted stock awards and units. This cost is expected to be recognized over a weighted-average period of approximately 1.3 years.

Stock Options

Stock option grants to employees generally have requisite service periods of four years, and stock option grants to non-employee directors generally have a requisite service period of one year. Both are subject to graded vesting. The Company records stock-based compensation expense associated with stock options on an accelerated basis over the various vesting periods within each grant and based on their fair value at the date of grant using the Black-Scholes-Merton option pricing model. There were zero and 156,492 stock options granted during the three months ended June 30, 2017 and 2016, respectively, and 21,500 and 857,024 stock options granted during the six months ended June 30, 2017 and 2016, respectively. The following weighted-average assumptions were used in the calculation of fair value for options grants for the three and six months ended June 30, 2017 and 2016, respectively.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016		2017	2016
Expected dividend yield	0	%	0 %	0 %
Risk-free interest rate	1.2	%	2.0 %	1.3 %
Expected volatility	38.2	%	35.7%	38.3%
Expected term (in years)	4.8		5.1	4.9

The Company considered that it has never paid cash dividends and does not currently intend to pay cash dividends. The risk-free interest rates are derived from the U.S. Treasury yield curve in effect on the date of grant for instruments with a remaining term similar to the expected term of the options. Due to the Company’s limited historical data, the expected volatility is calculated based upon the historical volatility of comparable companies in the medical device industry whose share prices are publicly available for a sufficient period of time. The expected term of "plain vanilla" options is calculated using the simplified method as prescribed by accounting guidance for stock-based compensation. A "plain vanilla" option is an option with the following characteristics: (1) the option is granted at-the-money; (2) exercisability is conditional only on satisfaction of a service condition through the vesting date; (3) employees who terminate their service prior to vesting forfeit the options; (4) employees who terminate their service after vesting are granted limited time to exercise their stock options; and (5) the options are nontransferable and non-hedgeable. The expected term of any other option is based on disclosures from similar companies with similar grants. In addition, the Company applies an expected forfeiture rate when amortizing stock-based compensation expense. The expected forfeiture rate of stock options is based on historical experience of pre-vesting forfeitures on awards by each homogenous group of shareowners and is estimated to be 12% annually for all non-executive employees for the six months ended June 30, 2017, and 10% annually for the six months ended June 30, 2016. There is no forfeiture rate

applied for non-employee directors and executive employees as their pre-vesting forfeitures are anticipated to be highly unlikely. As individual grant awards become fully vested, stock-based compensation expense is adjusted to recognize actual forfeitures.

As of June 30, 2017, there was approximately $1.6 million of total unrecognized compensation expense related to unvested stock options. This cost is expected to be recognized over a weighted-average period of approximately 1.2 years.

Employee Stock Purchase Plan

In May 2015, the Company adopted a 2015 Employee Stock Purchase Plan, which was amended in December 2015 (as amended, the ESPP). Under the ESPP, eligible employees may purchase shares of the Company’s common stock through payroll deductions of up to 15% of eligible compensation during an offering period. Generally, each offering will be for a period of twenty-four months as determined by the Company's board of directors. There are four six-month purchase periods in each offering period for contributions to be made and to be converted into shares at the end of the purchase period. In no event

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

may an employee purchase more than 2,500 shares per purchase period based on the closing price on the first trading date of an offering period or more than $25,000 worth of stock during each calendar year. The purchase price for shares to be purchased under the ESPP is 85% of the lesser of the market price of the Company's common stock on the first trading date of an offering period or any purchase date during an offering period (June 30 or December 31).

The ESPP authorizes the issuance of up to 400,000 shares of common stock pursuant to purchase rights granted to employees. The ESPP is intended to qualify as an “employee stock purchase plan” within the meaning of Section 423 of the Internal Revenue Code of 1986, as amended (the IRC). The first offering period under the ESPP commenced on January 1, 2016 and will end on December 31, 2017. However, the ESPP contains a restart feature, such that if the market price of the stock at the end of any six-month purchase period is lower than the stock price at the original grant date of an offering period, that offering period will terminate after that purchase date, and a new two-year offering period will commence on the January 1 or July 1 immediately following the date the original offering period terminated. This restart feature was first triggered on the purchase date that occurred on June 30, 2016, such that the offering period that commenced on January 1, 2016 was terminated, and a new two-year offering period commenced on July 1, 2016. This restart feature was triggered again on the purchase date that occurred on December 31, 2016, such that the offering period that commenced on July 1, 2016 was terminated, and a new two-year offering period commenced on January 1, 2017 and will end on December 31, 2018. The Company applied share-based payment modification accounting to the awards that were initially valued at the grant date to determine the amount of any incremental fair value associated with the modified awards. The impact to stock-based compensation expense for modifications during the three and six months ended June 30, 2017 was immaterial.

During the six months ended June 30, 2017 and 2016, there were 70,537 and 39,955 shares of common stock, respectively, purchased under the ESPP.

The Company estimates the fair value of shares issued to employees under the ESPP using the Black-Scholes-Merton option-pricing model. The following weighted average assumptions were used in the calculation of fair value of shares under the ESPP at the grant date for the three and six months ended June 30, 2017 and 2016, respectively:

	Three and Six Months Ended June 30,	
	2017	2016
Expected dividend yield	0 %	0 %
Risk-free interest rate	1.0 %	0.7 %
Expected volatility	28.5%	32.4%
Expected term (in years)	1.3	1.3

11. LEASES

The Company leases administrative, manufacturing, research, and distribution facilities and various manufacturing, office and transportation equipment through operating lease agreements. During the six months ended June 30, 2017, the Company entered into two lease agreements: one for an office located in Wayne, Pennsylvania, where the Company designs spinal implants and which facilitates the Company's interactions with customers on the East Coast, and another for an office located in Lyon, France, which serves as the Company's international sales and marketing office. The terms of these two new lease agreements are through July 2022 and February 2026, respectively, and both have an average annual cost of less than $0.1 million.

Future minimum lease payments under the Company's operating leases at June 30, 2017 are as follows:

	Payments Due by Calendar Year (In thousands)
2017	$ 954
2018	2,052
2019	2,100
2020	2,156
2021	2,212
Thereafter	8,474
Total minimum lease payments	$ 17,948

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

Total rental expense for the three months ended June 30, 2017 and 2016 was $0.6 million and $0.8 million, respectively, and $1.1 million and $1.6 million for the six months ended June 30, 2017 and 2016, respectively.

12. INCOME TAXES

The following table provides a summary of the Company's effective tax rate for the three and six months ended June 30, 2017 and 2016:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Reported tax rate	(0.6)%	3.5%	(0.3)%	1.9%

The Company reported an income tax expense for the three and six months ended June 30, 2017 primarily related to foreign and state operations.

The Company reported an income tax benefit for the three and six months ended June 30, 2016 which was primarily the result of a refund of tax initially paid toward the income tax return for our U.S. subsidiary which was not part of the U.S consolidated tax group for the tax period January 1, 2015 through August 31, 2015.

In addition, for all periods presented, the pretax losses incurred by the consolidated U.S. tax group received no corresponding tax benefit because the Company has concluded that it is more likely than not that the Company will be unable to realize the value of any resulting deferred tax assets. The Company will continue to assess its position in future periods to determine if it is appropriate to reduce a portion of its valuation allowance in the future.

13. COMMITMENTS AND CONTINGENCIES

In consideration for certain technology, manufacturing, distribution, and selling rights and licenses granted to the Company, the Company has agreed to pay royalties on sales of certain products sold by the Company. The royalty payments that the Company made under these agreements were included in the consolidated statements of operations as a component of cost of goods sold.

The Company is subject to various claims, lawsuits and proceedings in the ordinary course of its business with respect to its products, its current or former employees, and involving commercial disputes, some of which have been settled by the Company. In the opinion of management, such claims are either adequately covered by insurance or otherwise indemnified, or are not expected, individually or in the aggregate, to result in a material adverse effect on the Company's financial condition. However, it is possible that the Company's results of operations, financial position and cash flows in a particular period could be materially affected by these contingencies.

The Company accrues for loss contingencies when it is deemed probable that a loss has been incurred and that loss is estimable. The amounts accrued are based on the full amount of the estimated loss before considering insurance proceeds, and do not include an estimate for legal fees expected to be incurred in connection with the loss contingency. The Company does not believe there are any pending legal proceedings that would have a material impact on the Company's financial position, cash flows or results of operations.

SEASPINE HOLDINGS CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

14. SEGMENT AND GEOGRAPHIC INFORMATION

Management assessed its segment reporting based on how it internally manages and reports the results of its business to its chief operating decision maker. The Company's management reviews financial results, manages the business and allocates resources on an aggregate basis. Therefore, financial results are reported in a single operating segment: the development, manufacture and marketing of orthobiologics and spinal instrumentation. The Company reports revenue in two product categories: orthobiologics and spinal instrumentation. Orthobiologics products consist of a broad range of advanced and traditional bone graft substitutes that are designed to improve bone fusion rates following surgery. The spinal instrumentation portfolio consists of an extensive line of products for minimally invasive surgery, complex spine, deformity and degenerative procedures.

Revenue, net consisted of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Orthobiologics	$17,615	$16,805	$34,740	$33,463
Spinal instrumentation	16,581	16,396	31,350	31,137
Total revenue, net	$34,196	$33,201	$66,090	$64,600

The Company attributes revenues to geographic areas based on the location of the customer. Total revenue by major geographic area consisted of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
United States	$30,353	$30,012	$58,964	$58,556
International	3,843	3,189	7,126	6,044
Total revenue, net	$34,196	$33,201	$66,090	$64,600

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

The terms "we," "us," "our," "SeaSpine" or the "Company" refer collectively to SeaSpine Holdings Corporation and its wholly-owned subsidiaries, unless otherwise stated. All information presented in this report is based on our fiscal year. Unless otherwise stated, references to particular years, quarters, months or periods refer to our fiscal years ending December 31 and the associated quarters, months and periods of those fiscal years.

This Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). The matters discussed in these forward-looking statements are subject to risk and uncertainties that could cause actual results to differ materially from those made, projected or implied in the forward-looking statements. Such risks and uncertainties may also give rise to future claims and increase exposure to contingent liabilities. Please see the "Risk Factors" section included in our Annual Report on Form 10-K for the year ended December 31, 2016 (the 2016 10-K) for a discussion of the uncertainties, risks and assumptions associated with these statements. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

You can identify these forward-looking statements by forward-looking words such as "believe," "may," "could," "will," "estimate," "continue," "anticipate," "intend," "seek," "plan," "expect," "should," "would" and similar expressions. These risks and uncertainties arise from (among other factors) the following:

- general economic and business conditions, in both domestic and international markets;
- our expectations and estimates concerning future financial performance, financing plans and the impact of competition;
- anticipated trends in our business, including healthcare reform in the United States, increased pricing pressure from our competitors or hospitals, exclusion from major healthcare systems, whether as a result of unwillingness to provide required pricing or otherwise, and changes in third-party payment systems;
- physicians' willingness to adopt our recently launched and planned products, customers' continued willingness to pay for our products and third-party payors' willingness to provide or continue coverage and appropriate reimbursement for any of our products and our ability to secure regulatory approval for products in development;
- existing and future regulations affecting our business, both in the United States and internationally, and enforcement of those regulations;
- anticipated demand for our products and our ability to purchase or produce our products in sufficient quantities to meet customer demand;
- our ability to manage timelines and costs related to manufacturing our products;
- our ability to attract and retain new, high-quality distributors, whether as a result of inability to reach agreement on financial or other contractual terms or otherwise, disruption to our existing distribution network as new distributors are added, and the ability of new distributors to generate growth or offset disruption to existing distributors;
- our ability to successfully develop new and next-generation products and the costs associated with designing and developing those new and next-generation products;

- our ability to support the safety and efficacy of our products with long-term clinical data;
- our ability to obtain additional debt and equity financing to fund capital expenditures and working capital requirements and acquisitions;
- the risk of supply shortages, including our dependence on a limited number of third-party suppliers for components and raw materials;
- our ability to protect our intellectual property, including unpatented trade secrets, and to operate without infringing or misappropriating the proprietary rights of others;

- our ability to complete acquisitions, integrate operations post-acquisition and maintain relationships with customers of acquired entities; and

- other risk factors described in the section entitled “Risk Factors” of the 2016 10-K.

These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements that are included in this report.

Overview

We are a global medical technology company focused on the design, development and commercialization of surgical solutions for the treatment of patients suffering from spinal disorders. We have a comprehensive portfolio of orthobiologics and spinal instrumentation solutions to meet the varying combinations of products that neurosurgeons and orthopedic spine surgeons need to perform fusion procedures in the lumbar, thoracic and cervical spine. We believe this broad combined portfolio of orthobiologics and spinal instrumentation products is essential to meet the “complete solution” requirements of neurosurgeons and orthopedic spine surgeons.

We report revenue in two product categories: orthobiologics and spinal instrumentation. Our orthobiologics products consist of a broad range of advanced and traditional bone graft substitutes that are designed to improve bone fusion rates following a wide range of orthopedic surgeries, including spine, hip, and extremities procedures. Our spinal instrumentation portfolio consists of an extensive line of products to facilitate spinal fusion in MIS, complex spine, deformity and degenerative procedures.

Our U.S. sales organization consists of regional and territory managers who oversee a broad network of independent orthobiologics and spinal instrumentation sales agents to whom we pay commissions based on the sales of our products. Our international sales organization consists of a sales management team that oversees a network of independent orthobiologics and spinal instrumentation stocking distributors that purchase products directly from us and independently sell them. For the six months ended June 30, 2017 and 2016, international sales accounted for approximately 11% and 9% of our revenue, respectively. Our policy is not to sell our products through or participate in physician-owned distributorships.

For the six months ended June 30, 2017, our total revenue, net was $66.1 million and our net loss was $17.1 million. For the same period, revenue from sales of orthobiologics and spinal instrumentation totaled $34.7 million and $31.4 million, respectively. We expect to continue to incur losses as we further invest in the expansion of our business, primarily in sales, marketing and research and development, and from the general and administrative expenses we expect to incur due to our operation as an independent, publicly-traded company. As of June 30, 2017, our cash and cash equivalents totaled $12.3 million.

SeaSpine was incorporated in Delaware on February 12, 2015 in connection with the spin-off of the orthobiologics and spinal instrumentation business of Integra. The spin-off occurred on July 1, 2015.

Components of Our Results of Operations

Revenue

Our net revenue is derived primarily from the sale of orthobiologics and spinal instrumentation products across North America, Europe, Asia Pacific and Latin America. Sales are reported net of returns, rebates, group purchasing organization fees and other customer allowances.

In the United States, we generate most of our revenue by consigning our orthobiologics products and by consigning or loaning our spinal instrumentation sets to hospitals and independent sales agents, who in turn either deliver them to hospitals for a single surgical procedure, after which they are returned to us, or leave them with hospitals that are high volume users for multiple procedures. The spinal instrumentation sets typically contain the instruments, disposables, and spinal implants required to complete a surgery. We ship replacement inventory to independent sales agents to replace the consigned inventory used in surgeries. We maintain and replenish loaned sets at our kitting and

distribution centers and return replenished sets to a hospital or independent sales agent for the next procedure. We recognize revenue on these consigned or loaned products when they have been used or implanted in a surgical procedure.

For all other sales transactions, including sales to international stocking distributors and private label partners, we recognize revenue when the products are shipped to the customer or stocking distributor and the transfer of title and risk of loss occurs.

There is generally no customer acceptance or other condition that prevents us from recognizing revenue in accordance with the delivery terms for these sales transactions.

Cost of Goods Sold

Cost of goods sold primarily consists of the costs of finished goods purchased directly from third parties and raw materials used in the manufacture of our products, plant and equipment overhead, labor costs, packaging costs, amortization of product technology intangible assets and freight. The majority of our orthobiologics products are designed and manufactured internally. The cost of human tissue and fixed manufacturing overhead costs are significant drivers of the costs of goods sold and consequently our orthobiologics products, at current production volumes, generate lower gross margin than our spinal instrumentation products. We rely on third-party suppliers to manufacture our spinal instrumentation products, and we assemble them into surgical sets at our kitting and distribution centers. Beginning in the fourth quarter of 2016, we began outsourcing a portion of that assembly function to a third party logistics provider. Other costs included in cost of goods sold include amortization of product technology intangible assets, royalties, shipping, inspection and charges for expired, excess and obsolete inventory. We expect our cost of goods sold to continue to increase in absolute dollars as our sales volume increases over time.

Selling, General and Administrative Expense

Our selling, general and administrative (SG&A) expenses consist primarily of sales commissions to independent sales agents, cost of medical education and training, payroll and other headcount related expenses, depreciation of instrument sets, instrument replacement expense, stock-based compensation, marketing expenses, supply chain and distribution expenses, and expenses for information technology, legal, human resources, insurance, finance, facilities, and management.

Research and Development Expense

Our research and development (R&D) expenses primarily consist of expenses related to the headcount for engineering, product development, clinical affairs and regulatory functions as well as consulting services, third-party prototyping services, outside research and clinical studies activities, and materials, production and other costs associated with development of our products. We expense R&D costs as they are incurred.

While our R&D expenses fluctuate from period to period based on the timing of specific initiatives, we expect that these costs will increase over time as we continue to design and commercialize new products and expand our product portfolio, add related personnel and conduct additional clinical activities.

Intangible Amortization

Our intangible amortization, including the amounts reported in cost of goods sold, consists of acquisition-related amortization and impairments related to product discontinuations. We expect total annual amortization expense (including amounts reported in cost of goods sold) to be approximately $6.8 million in 2017, $6.5 million in 2018, $5.8 million in 2019, $4.9 million in 2020 and $4.9 million in 2021.

RESULTS OF OPERATIONS

(In thousands, except percentages)	Three Months Ended June 30, 2017	2016	2017 vs. 2016 % Change	Six Months Ended June 30, 2017	2016	2017 vs. 2016 % Change
Total revenue, net	$34,196	$33,201	3.0 %	$66,090	$64,600	2.3 %
Cost of goods sold	13,994	13,930	0.5 %	27,166	28,213	(3.7)%
Gross profit	20,202	19,271	4.8 %	38,924	36,387	7.0 %
Gross margin	59.1 %	58.0 %		58.9 %	56.3 %	
Operating expenses:						
Selling, general and administrative	24,249	26,989	(10.2)%	48,219	52,363	(7.9)%
Research and development	3,344	3,181	5.1 %	6,394	5,934	7.8 %
Intangible amortization	792	1,281	(38.2)%	1,584	2,562	(38.2)%
Total operating expenses	28,385	31,451	(9.7)%	56,197	60,859	(7.7)%
Operating loss	(8,183)	(12,180)	(32.8)%	(17,273)	(24,472)	(29.4)%
Other income (expense), net	185	(232)	(179.7)%	172	26	561.5 %
Loss before income taxes	(7,998)	(12,412)	(35.6)%	(17,101)	(24,446)	(30.0)%
Provision (benefit) for income taxes	45	(429)	(110.5)%	45	(456)	(109.9)%
Net loss	$(8,043)	$(11,983)	(32.9)%	$(17,146)	$(23,990)	(28.5)%

Three Months Ended June 30, 2017 Compared to Three Months Ended June 30, 2016

Revenue

Total revenue, net increased for the three months ended June 30, 2017 by $1.0 million, to $34.2 million compared to $33.2 million for the same period in 2016.

	Three Months Ended June 30, 2017	2016	2017 vs. 2016 % Change
	(In thousands)		
Orthobiologics	$17,615	$16,805	4.8 %
United States	15,975	14,894	7.3 %
International	1,640	1,911	(14.2)%
% of total revenue, net	52 %	51 %	
Spinal instrumentation	$16,581	$16,396	1.1 %
United States	14,378	15,118	(4.9)%
International	2,203	1,278	72.4 %
% of total revenue, net	48 %	49 %	
Total revenue, net	$34,196	$33,201	3.0 %

	Three Months Ended June 30, 2017	2016	2017 vs. 2016 % Change
	(In thousands)		
United States	$30,353	$30,012	1.1 %
International	3,843	3,189	20.5 %

Total revenue, net	$34,196	$33,201	3.0 %

Revenue from sales of orthobiologics totaled $17.6 million for the three months ended June 30, 2017, an increase of $0.8 million or 4.8%, from the same period in 2016. Revenue from sales of our orthobiologics products in the United States increased $1.1 million to $16.0 million for the three months ended June 30, 2017 compared to the same period in 2016 and was driven by growth generated from recently added distributors. Revenue from international sales of our orthobiologics products,

which can be volatile from quarter to quarter because of irregular ordering patterns from our stocking distributors, decreased $0.3 million for the three months ended June 30, 2017 compared to the same period in 2016, which was primarily attributable to decreased sales in Latin America.

Revenue from sales of spinal instrumentation totaled $16.6 million for the three months ended June 30, 2017, an increase of $0.2 million or 1.1%, from the same period in 2016. Revenue from sales in the United States decreased $0.7 million to $14.4 million for the three months ended June 30, 2017 compared to the same period in 2016, primarily due to lower prices and decreased demand for our legacy systems, which outpaced the revenue growth contributed by recently launched products. Revenue from international sales of our spinal instrumentation products, which can be volatile from quarter to quarter because of irregular ordering patterns from our stocking distributors, increased $0.9 million for the three months ended June 30, 2017 compared to the same period in 2016, mainly due to stocking orders from a recently added distributor in Latin America.

Cost of Goods Sold and Gross Margin

Cost of goods sold increased $0.1 million, to $14.0 million for the three months ended June 30, 2017, compared to the same period in 2016. Gross margin was 59.1% for the three months ended June 30, 2017 and 58.0% for the same period in 2016. The increase in gross margin was mainly driven by lower manufacturing costs for orthobiologics products manufactured at our Irvine, California facility. This was partially offset by a $0.2 million increase in non-cash amortization of technology intangible assets acquired in September 2016 from NLT and by lower gross margins associated with international sales, which were slightly higher as a percentage of total revenue compared to the same period of the prior year.

Cost of goods sold included $0.9 million and $0.6 million of amortization for product technology intangible assets for the three months ended June 30, 2017 and 2016, respectively.

Selling, General and Administrative

SG&A expenses decreased $2.7 million to $24.2 million for the three months ended June 30, 2017 compared to the same period in 2016. The decrease was mainly driven by a $1.5 million decrease in expenses for consulting services and other fees primarily related to the completion in late 2016 of the project to outsource a large portion of our spinal instrumentation kitting and distribution to a third party, lower legal fees, the absence of a $0.6 million instrument impairment recorded in the second quarter of 2016, and a $0.6 million decrease in compensation expenses primarily due to decreased temporary labor costs and stock compensation expenses. These decreases were partially offset by fees paid in 2017 to the new third party logistics provider, a $0.5 million increase in selling commissions and a $0.2 million non-cash charge related to an increase in the fair value of contingent consideration liabilities related to the NLT acquisition (see Note 8, "Business Combinations" to the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report). While we expect total SG&A expenses for the full year 2017 to decrease as a percentage of revenue compared to the full year 2016, components within SG&A expenses, specifically, selling commissions, are expected to increase relative to 2016, both in absolute terms and as percentage of revenue.

Research and Development

R&D expenses increased $0.2 million to $3.3 million, or 9.8% of revenue, for the three months ended June 30, 2017 compared to the same period in 2016. The increase was primarily driven by higher external costs related to product development and clinical studies related to our orthobiologics products, and by $0.1 million of fees incurred under the transition services agreement with NLT. For the full year 2017, we expect our investment in R&D to be between 8% and 10% of revenue, as we continue to accelerate the design and commercialization of new and next generation products to expand our product portfolio and conduct additional clinical activities.

Intangible Amortization

Intangible amortization expense, excluding the amounts reported in cost of goods sold for product technology intangible assets, decreased $0.5 million to $0.8 million for the three months ended June 30, 2017 compared to the same period in 2016. The decrease was primarily due to a customer relationships intangible that was fully amortized by the third quarter of 2016.

Income Taxes

	Three Months Ended June 30,	
	2017	2016
	(In thousands)	
Loss before income taxes	$(7,998)	$(12,412)
Provision (benefit) for income taxes	45	(429)
Effective tax rate	(0.6)%	3.5 %

We reported an income tax expense for the three months ended June 30, 2017 primarily related to our foreign and state operations.

We reported an income tax benefit for the three months ended June 30, 2016 which was primarily the result of a refund of tax initially paid toward the income tax return for our U.S. subsidiary which was not part of the U.S consolidated tax group for the tax period January 1, 2015 through August 31, 2015.

In addition, for all periods presented, the pretax losses incurred by the consolidated U.S. tax group received no corresponding tax benefit because we have concluded that it is more likely than not that we will be unable to realize the value of any resulting deferred tax assets.

Six Months Ended June 30, 2017 Compared to Six Months Ended June 30, 2016

Revenue

Total revenue, net increased for the six months ended June 30, 2017 by $1.5 million, to $66.1 million compared to $64.6 million for the same period in 2016.

	Six Months Ended June 30,		2017 vs. 2016
	2017	2016	% Change
	(In thousands)		
Orthobiologics	$34,740	$33,463	3.8 %
United States	31,077	29,818	4.2 %
International	3,663	3,645	0.5 %
% of total revenue, net	53 %	52 %	
Spinal instrumentation	$31,350	$31,137	0.7 %
United States	27,887	28,738	(3.0)%
International	3,463	2,399	44.4 %
% of total revenue, net	47 %	48 %	
Total revenue, net	$66,090	$64,600	2.3 %

	Six Months Ended June 30,		2017 vs. 2016
	2017	2016	% Change
	(In thousands)		
United States	$58,964	$58,556	0.7 %
International	7,126	6,044	17.9 %

Total revenue, net	$66,090	$64,600	2.3 %

Revenue from sales of orthobiologics totaled $34.7 million for the six months ended June 30, 2017, an increase of $1.3 million or 3.8%, from the same period in 2016. Revenue from sales of our orthobiologics products in the United States increased $1.3 million to $31.1 million for the six months ended June 30, 2017 compared to the same period in 2016 due primarily to growth generated by recently added distributors during the current year period. Revenue from international sales of orthobiologics was relatively flat for the six months ended June 30, 2017 as compared to the same period in 2016.

Revenue from sales of spinal instrumentation totaled $31.4 million for the six months ended June 30, 2017, an increase of $0.2 million or 0.7%, from the same period in 2016. Revenue from sales in the United States decreased $0.9 million to $27.9 million for the six months ended June 30, 2017 compared to the same period in 2016, primarily due to lower prices and decreased demand for our legacy systems, which outpaced the revenue growth contributed by recently launched products. Revenue from international sales of spinal instrumentation increased $1.1 million for the six months ended June 30, 2017 compared to the same period in 2016 due to stocking orders from a recently added distributor in Latin America.

Cost of Goods Sold and Gross Margin

Cost of goods sold decreased $1.0 million, to $27.2 million for the six months ended June 30, 2017, compared to the same period in 2016. Gross margin was 58.9% for the six months ended June 30, 2017, compared to 56.3% for the same period in 2016. The increase in gross margin was mainly driven by lower manufacturing costs for orthobiologics products manufactured at our Irvine, California facility, and by a $1.7 million provision for excess orthobiologics raw material inventory recorded in the first quarter of 2016. This provision related to management's decision to repurpose a portion of our matched-donor bone raw material for other production uses and that rendered a large portion of the remaining and now unmatched-donor bone as excess quantities that were unlikely to be consumed in future production. This was partially offset by a $0.5 million increase in non-cash amortization of technology intangible assets acquired in September 2016 from NLT, and by lower gross margins associated with international sales, which were slightly higher as a percentage of total revenue compared to the same period of the prior year.

Cost of goods sold included $1.8 million and $1.3 million of amortization for product technology intangible assets, for the six months ended June 30, 2017 and 2016, respectively.

Selling, General and Administrative

SG&A expenses decreased $4.1 million to $48.2 million for the six months ended June 30, 2017 compared to the same period in 2016. The decrease was mainly driven by a $2.1 million decrease in expenses for consulting services as a result of the completion in late 2016 of various significant information system related projects and the project to outsource a large portion of our spinal instrumentation kitting and distribution to a third party logistics provider, a $1.5 million decrease in compensation expenses primarily due to decreased temporary labor costs and stock compensation expenses, the absence of a $0.7 million instrument impairment recorded in 2016, and decreased legal fees. These decreases were partially offset by fees paid in 2017 to the new third party logistics provider, a $1.0 million increase in selling commissions and a $0.5 million non-cash charge related to an increase in the fair value of contingent consideration liabilities related to the NLT acquisition. While we expect total SG&A expenses for the full year 2017 to decrease as a percentage of revenue compared to the full year 2016, components within SG&A expenses, specifically, selling commissions, are expected to increase relative to 2016, both in absolute terms and as percentage of revenue.

Research and Development

R&D expenses increased $0.5 million to $6.4 million, or 9.7% of revenue, for the six months ended June 30, 2017 compared to the same period in 2016. The increase was primarily driven by higher external costs related to product development and clinical studies related to our orthobiologics products, and by $0.3 million of fees incurred under the transition services agreement with NLT, partially offset by a $0.3 million reduction in facility costs. For the full year 2017, we expect our investment in R&D to be between 8% and 10% of revenue, as we continue to accelerate the design and commercialization of new and next generation products to expand our product portfolio and conduct additional clinical activities.

Intangible Amortization

Intangible amortization expense, excluding the amounts reported in cost of goods sold for product technology intangible assets, decreased $1.0 million to $1.6 million for the six months ended June 30, 2017 compared to the same period in 2016. The decrease was primarily due to a customer relationships intangible that was fully amortized by the third quarter of 2016.

Income Taxes

	Six Months Ended June 30,	
	2017	2016
	(In thousands)	
Loss before income taxes	$(17,101)	$(24,446)
Provision (benefit) for income taxes	45	(456)
Effective tax rate	(0.3)%	1.9 %

We reported an income tax expense for the six months ended June 30, 2017 primarily related to the result of our foreign and state operations.

We reported an income tax benefit for the six months ended June 30, 2016 which was primarily the result of a refund of tax initially paid toward the income tax return for our U.S. subsidiary which was not part of the U.S consolidated tax group for the tax period January 1, 2015 through August 31, 2015.

In addition, for all periods presented, the pretax losses incurred by the consolidated U.S. tax group received no corresponding tax benefit because we have concluded that it is more likely than not that we will be unable to realize the value of any resulting deferred tax assets.

Liquidity and Capital Resources

Overview

As of June 30, 2017, we had cash and cash equivalents totaling approximately $12.3 million, and $15.8 million of current borrowing capacity was available under our credit facility. We believe that our cash and cash equivalents on hand and the amount currently available to us under our credit facility will be sufficient to fund our operations for at least the next twelve months.

Credit Facility

We have a $30.0 million credit facility with Wells Fargo Bank, National Association which expires in December 2018, subject to a one-time, one-year extension at our election. At June 30, 2017, there was $4.0 million of outstanding borrowings under our credit facility. The borrowing capacity under our credit facility is determined monthly and is based on the amount of our eligible accounts receivable and inventory balances and qualified cash (as defined in the credit facility). Depending on the extent to which our eligible accounts receivable and inventory balances increase, our borrowing capacity could increase by as much as an additional $6.7 million from the $15.8 million available as of June 30, 2017 before we are required to maintain the minimum fixed charge coverage ratio as discussed below. Our credit facility contains various customary affirmative and negative covenants, including prohibiting us from incurring indebtedness without the lender’s consent. Under the terms of our credit facility, if our Total Liquidity (as defined in the credit facility) is less than $5.0 million, we are required to maintain a minimum fixed charge coverage ratio of 1.10 to 1.00 for the applicable measurement period. Our Total Liquidity was $24.0 million at June 30, 2017, and therefore that financial covenant was not applicable at that time.

Business Combinations

In August 2016, we entered into an asset purchase agreement with NLT to acquire certain of the assets of NLT’s medical device business related to the expandable interbody medical devices. We made an upfront cash payment of

$1.0 million in connection with the initial closing in September 2016 and issued 350,000 shares of our common stock in January 2017 as contingent closing consideration. At June 30, 2017, we recorded a $2.3 million liability representing the estimated fair value of future contingent milestone payments related to the achievement of certain commercial milestones, which we anticipate will become payable at varying times between 2018 and 2022, and a $3.5 million liability representing the estimated fair value of future contingent royalty payments based on percentages of our future net sales of certain of the products and technology we acquired, which we anticipate will become payable at varying times between 2017 and 2027. The contingent milestone payments, if any, are payable in cash or in shares of our common stock, at our election. The contingent royalty payments, if any, are payable in cash.

At The Market Program

In August 2016, we entered into an equity distribution agreement with Piper Jaffray & Co. (Piper Jaffray), pursuant to which we may offer and sell shares of our common stock in “at the market” (ATM) offerings (as defined in Rule 415 of the Securities Act of 1933, as amended) having an aggregate offering price up to $25.0 million in gross proceeds from time to time of through Piper Jaffray acting as sales agent. During the three and six months ended June 30, 2017, we received net proceeds of approximately $4.6 million, net of offering costs, from the sale of approximately 477,000 shares of our common stock. We have the capacity to issue additional shares of our common stock for up to $20.2 million of gross proceeds under the equity distribution agreement as of June 30, 2017. Future sales, if any, will depend on a variety of factors including, but not limited to, market conditions, the trading price of our common stock and our capital needs.

Subsequent to June 30, 2017, we sold an additional approximately 522,000 shares of common stock at an average price per share of $12.18 and received net proceeds of approximately $6.0 million, net of offering costs.

Cash and Cash Equivalents

We had cash and cash equivalents totaling approximately $12.3 million and $14.6 million at June 30, 2017 and December 31, 2016, respectively.

Cash Flows

	Six Months Ended June 30,		2017 vs. 2016
	2017	2016	% Change
	(In thousands)		
Net cash used in operating activities	$(3,940)	$(7,500)	(47.5)%
Net cash used in investing activities	(3,173)	(3,446)	(7.9)%
Net cash provided by financing activities	4,563	354	1,189.0 %
Effect of exchange rate changes on cash and cash equivalents	271	150	80.7 %
Net decrease in cash and cash equivalents	$(2,279)	$(10,442)	(78.2)%

Net Cash Used in Operating Activities

Cash used in operating activities for the six months ended June 30, 2017 decreased by $3.6 million compared to the same period in 2016 primarily due to lower cash-based operating expenses incurred and lower purchases of inventory in the six months ended June 30, 2017 compared to the same period in 2016, partially offset by lower cash collections in the six months ended June 30, 2017 compared to the same period in 2016.

Net Cash Used in Investing Activities

Net cash used in investing activities was $3.2 million for the six months ended June 30, 2017 compared to $3.4 million for the same period in 2016. The decrease was primarily due to larger investments in leasehold improvements in our Carlsbad facility in the first half of 2016, offset by more instrument purchases in 2017 to support recent spinal instrumentation product launches and by a milestone payment under a license agreement.

Net Cash Provided by Financing Activities

Net cash provided by financing activities was $4.6 million for the six months ended June 30, 2017 and was comprised primarily of $4.6 million of net proceeds through the sale of shares of our common stock under the ATM equity offering program, $0.5 million of proceeds from sale of shares of our common stock under our 2015 Employee Stock Purchase Plan, somewhat offset by $0.4 million in repayments of short-term debt related to our insurance premium finance agreements (see Note 3, "Debt and Interest" to the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report).

Off-Balance Sheet Arrangements

There were no off-balance sheet arrangements as of June 30, 2017 that have or are reasonably likely to have, a current or future effect on our financial condition, revenues or expenses, results of operations, cash flows, liquidity, capital

expenditures or capital resources that is material to our business.

Contractual Obligations and Commitments

There have been no material changes outside the ordinary course of our business to the contractual obligations disclosed in the 2016 10-K.

Other Matters
Critical Accounting Policies and the Use of Estimates

Our discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities, and the reported amounts of revenues and expenses. Significant estimates affecting amounts reported or disclosed in the consolidated financial statements include revenue recognition, allowances for doubtful accounts receivable and sales return and other credits, net realizable value of inventories, amortization periods for acquired intangible assets, estimates of projected cash flows and discount rates used to value intangible assets and test them for impairment, estimates of projected cash flows and assumptions related to the timing and probability of the product launch dates, discount rates matched to the estimated timing of payments, and probability of success rates used to value contingent consideration liabilities from business combinations, estimates of projected cash flows and depreciation and amortization periods for long-lived assets, valuation of stock-based compensation, computation of taxes and valuation allowances recorded against deferred tax assets, and loss contingencies. These estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the current circumstances. Actual results could differ from these estimates.

Note 2, “Summary of Significant Accounting Policies” to the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this report and included in Part II, Item 8 of the 2016 10-K describe the significant accounting policies and estimates used in the preparation of our condensed consolidated financial statements. Those policies and estimates disclosed in the 2016 10-K have not materially changed.
Recently Issued Accounting Pronouncements
Information regarding new accounting pronouncements is included in Note 2, "Summary of Significant Accounting Policies," to the Notes to Unaudited Condensed Consolidated Financial Statements included in Part I, Item 1 of this report.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK
The market risk exposures described in Part II, Item 7A of the 2016 10-K have not materially changed during the six months ended June 30, 2017.

ITEM 4. CONTROLS AND PROCEDURES
Evaluation of Disclosure Controls and Procedures
Based on an evaluation under the supervision and with the participation of our management, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act were effective as of the end of the period covered by this report to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.
Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting identified in connection with the evaluation required by Rules 13a-15(d) and 15d-15(d) under the Exchange Act that occurred during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations of Internal Controls

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent or detect all error and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

From time to time, we are subject to legal proceedings and claims in the ordinary course of business. While management presently believes that the ultimate outcome of these proceedings, individually and in the aggregate, will not materially harm our financial position, cash flows, or overall trends in results of operations, legal proceedings are subject to inherent uncertainties, and unfavorable rulings or outcomes could occur that have individually or in aggregate, a material adverse effect on our business, financial condition or operating results. We are not currently subject to any pending material litigation, other than ordinary routine litigation incidental to our business, as described above.

ITEM 1A. RISK FACTORS
The risk factors described in the 2016 10-K have not materially changed.

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

Recent Sales of Unregistered Securities

None.

Purchases of Equity Securities by the Issuer

The table below is a summary of purchases of our common stock we made during the quarter covered by this report. Other than as indicated in the table below, no such purchases were made in any other month during the quarter. We do not have any publicly announced repurchase plans or programs.

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs
June 1-June 30	113	$ 10.00	—	—

(1) These shares were surrendered to the Company to satisfy tax withholdings obligations in connection with the vesting of restricted stock awards.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS

The information required by this Item 6 is set forth on the exhibit index that follows the signature page at the end of this report.

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.

SEASPINE HOLDINGS CORPORATION

Date: August 4, 2017 /s/ Keith C. Valentine
Keith C. Valentine
President and Chief Executive Officer

Date: August 4, 2017 /s/ John J. Bostjancic
John J. Bostjancic
Chief Financial Officer

EXHIBIT INDEX

Exhibit No.	Description
*31.1	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
*31.2	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
**32.1	Certification of Principal Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
**32.2	Certification of Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
*†101.INS	XBRL Instance Document
*†101.SCH	XBRL Taxonomy Extension Schema Document
*†101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
*†101.DEF	XBRL Definition Linkbase Document
*†101.LAB	XBRL Taxonomy Extension Labels Linkbase Document
*†101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

* Filed herewith

** These certifications are being furnished solely to accompany this report pursuant to 18 U.S.C. 1350, and are not being filed for purposes of Section 18 of the Securities Exchange Act of 1934 and are not to be incorporated by reference into any filing of the registrant, whether made before or after the date hereof, regardless of any general incorporation by reference language in such filing.

† The financial information of SeaSpine Holdings Corporation Quarterly Report on Form 10-Q for the quarter ended June 30, 2017 filed on August 4, 2017 formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statements of Operations, (ii) Condensed Consolidated Statements of Comprehensive Loss, (iii) the Condensed Consolidated Balance Sheets, (iv) Parenthetical Data to the Condensed Consolidated Balance Sheets, (v) the Condensed Consolidated Statements of Cash Flows, (vi) the Condensed Consolidated Statement of Equity, and (vii) Notes to Unaudited Condensed Consolidated Financial Statements, is furnished electronically herewith.