

TRANSGENOMIC INC
Form 10-K/A
October 21, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A
AMENDMENT NO. 1

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2010

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number 000-30975

TRANSGENOMIC, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

91-1789357
(IRS Employer
Identification Number)

12325 Emmet Street
Omaha, NE 68164
(Address of Principal Executive Offices)

68164
(Zip Code)

(402) 452-5400
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
None	N/A

Securities registered pursuant to Section 12(g) of the Act:

Common Stock, par value \$.01 per share
(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.
Yes No

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K/A or any amendment to this Form 10-K/A

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "accelerated filer", "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer Smaller Reporting Company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Act Rule 12b-2).

Yes No

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant based on the last reported closing price per share of Common Stock as reported on the OTC Bulletin Board on the last business day of the registrant's most recently completed second quarter was approximately \$10.0 million.

At March 14, 2011, the registrant had 49,289,672 of Common Stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant Proxy Statement relating to its 2011 Annual Meeting of Stockholders (the "Proxy Statement") have been incorporated into Part III of this Report on Form 10-K/A.

EXPLANATORY NOTE

We are filing this Amendment No. 1 (“Form 10-K/A”) to our Annual Report on Form 10-K for the period ended December 31, 2010, originally filed with the Securities and Exchange Commission (“SEC”) on March 14, 2011 (the “Form 10-K”) for the purpose of adding the signature of our independent registered public accounting firm to the Report of Independent Registered Public Accounting Firm contained in Item 8 of Part II of the Form 10-K. In accordance with Rule 12b-15 under the Securities Exchange Act of 1934, as amended, each item of the Form 10-K that is amended by this Form 10-K/A is restated in its entirety, and this Form 10-K/A is accompanied by currently dated certifications on Exhibits 31 and 32 by our Chief Executive Officer and Chief Financial Officer.

Except as expressly set forth in this Form 10-K/A, we are not amending any other part of the Form 10-K. This Form 10-K/A does not reflect events occurring after the filing of the Form 10-K or modify or update any related or other disclosures, including forward-looking statements, unless expressly noted otherwise. Accordingly, this Form 10-K/A should be read in conjunction with the Form 10-K and with our other filings with the SEC subsequent to the filing of the Form 10-K, including any amendments to those filings.

The Report of the Independent Registered Public Accounting Firm dated March 14, 2011, as amended, is set forth below.

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders
Transgenomic, Inc.

We have audited the accompanying consolidated balance sheets of Transgenomic, Inc. and Subsidiary as of December 31, 2010 and 2009, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Transgenomic, Inc. and Subsidiary as of December 31, 2010 and 2009, and the results of their operations and their cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

/s/ McGladrey & Pullen, LLP

Omaha, Nebraska
March 14, 2011

TRANSGENOMIC, INC. AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS
As of December 31, 2010 and 2009
(Dollars in thousands except per share data)

	2010	2009
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$3,454	\$5,642
Accounts receivable (net of allowances for bad debts of \$334 and \$310, respectively)	7,601	4,522
Inventories (net of allowances for obsolescence of \$518 and \$507, respectively)	3,344	3,552
Other current assets	635	738
Total current assets	15,034	14,454
PROPERTY AND EQUIPMENT:		
Equipment	9,820	9,972
Furniture, fixtures and leasehold improvements	3,479	3,834
	13,299	13,806
Less: accumulated depreciation	(11,697)	(12,839)
	1,602	967
OTHER ASSETS:		
Goodwill	6,275	—
Intangibles (net of accumulated amortization of \$519 and \$525, respectively)	8,962	383
Other assets	154	200
	\$32,027	\$16,004
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$1,360	\$1,013
Accrued compensation	875	573
Short term debt	989	—
Accrued expenses	3,231	2,517
Contractual obligation	1,628	—
Current portion of lease obligations	170	—
Total current liabilities	8,253	4,103
Long term debt less current maturities	8,640	—
Redeemable Series A convertible preferred stock, \$.01 par value, 3,879,307 shares authorized, 2,586,205 shares issued and outstanding	1,457	—
Preferred stock conversion feature	1,983	—
Warrant liability	2,351	—
Other long term liabilities	843	239
Total liabilities	23,527	4,342
STOCKHOLDERS' EQUITY:		
Preferred stock, \$.01 par value, 15,000,000 shares authorized, 2,586,205 shares issued and outstanding	—	—
Common stock, \$.01 par value, 100,000,000 shares authorized, 49,289,672 shares issued and outstanding	498	497
Additional paid-in capital	139,730	139,703
Accumulated other comprehensive income	1,589	1,645
Accumulated deficit	(133,317)	(130,183)
Total stockholders' equity	8,500	11,662

	\$32,027	\$16,004
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See notes to consolidated financial statements.

TRANSGENOMIC, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS
Years Ended December 31, 2010 and 2009
(Dollars in thousands except per share data)

	2010	2009
NET SALES	\$20,048	\$22,023
COST OF GOODS SOLD	10,284	10,418
Gross profit	9,764	11,605
OPERATING EXPENSES:		
Selling, general and administrative	10,933	10,319
Research and development	2,305	3,182
Restructuring charges	138	—
	13,376	13,501
LOSS FROM OPERATIONS	(3,612)	(1,896)
OTHER INCOME:		
Interest income (expense)	(4)	15
Other, net	632	3
	628	18
LOSS BEFORE INCOME TAXES	(2,984)	(1,878)
INCOME TAX EXPENSE	150	42
NET LOSS	\$(3,134)	\$(1,920)
BASIC AND DILUTED LOSS PER SHARE	\$(0.06)	\$(0.04)
BASIC AND DILUTED WEIGHTED AVERAGE SHARES OUTSTANDING	49,243,839	49,189,672

See notes to consolidated financial statements.

TRANSGENOMIC, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years Ended December 31, 2010 and 2009
(Dollars in thousands except share data)

	Common Stock		Additional		Accumulated Other Comprehensive		Total
	Outstanding Shares	Par Value	Paid in Capital	Accumulated Deficit	Income (Loss)		
Balance, January 1, 2009	49,189,672	\$ 497	\$ 139,501	\$ (128,263)	\$ 1,470	\$ 13,205	
Other comprehensive income (loss):							
Net loss	—	—	—	(1,920)	(1,920)	(1,920)	
Foreign currency translation adjustment	—	—	—	—	175	175	
Comprehensive loss					(1,745)		
Non-cash stock based compensation	—	—	202	—	—	202	
Balance, December 31, 2009	49,189,672	\$ 497	\$ 139,703	\$ (130,183)	\$ 1,645	\$ 11,662	
Other comprehensive income (loss):							
Net loss				(3,134)	(3,134)	(3,134)	
Foreign currency translation adjustment					(56)	(56)	
Comprehensive loss					(3,190)		
Non-cash stock based compensation	—	—	(14)	—	—	(14)	
Issuance of shares for employee stock options	100,000	1	41	—	—	42	
Balance, December 31, 2010	49,289,672	\$ 498	\$ 139,730	\$ (133,317)	\$ 1,589	\$ 8,500	

See notes to consolidated financial statements.

TRANSGENOMIC, INC. AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010 and 2009
(Dollars in thousands except share data)

	2010	2009
CASH FLOWS PROVIDED BY (USED IN) OPERATING ACTIVITIES:		
Net loss	\$(3,134)	\$(1,920)
Adjustments to reconcile net loss to net cash flows provided by (used in) operating activities:		
Depreciation, amortization and disposals	708	852
Non-cash stock based compensation	(14)	202
Changes in operating assets and liabilities, net of effects of acquisition:		
Accounts receivable	72	1,113
Inventories	97	1,290
Prepaid expenses and other current assets	95	(60)
Accounts payable	364	60
Accrued expenses and accrued compensation	92	(401)
Other long term liabilities	(24)	109
Deferred income taxes	26	22
Net cash flows provided by (used) in operating activities	(1,718)	1,267
CASH FLOWS USED IN INVESTING ACTIVITIES:		
Acquisition	(6,000)	—
Purchase of property and equipment	(192)	(351)
Change in other assets	(34)	(26)
Net cash flows used in investing activities	(6,226)	(377)
CASH FLOWS PROVIDED BY FINANCING ACTIVITIES:		
Issuance of preferred stock and related warrants	6,000	—
Stock issuance costs	(209)	—
Issuance of common stock	42	—
Principal payments on capital lease obligations	(72)	—
Net cash flows provided by financing activities	5,761	—
EFFECT OF FOREIGN CURRENCY EXCHANGE RATE CHANGES ON CASH	(5)	(19)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(2,188)	871
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	5,642	4,771
CASH AND CASH EQUIVALENTS AT END OF YEAR	\$3,454	\$5,642
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid during the year for:		
Interest	\$7	\$—
Income taxes	29	163
SUPPLEMENTAL DISCLOSURE OF NON-CASH INFORMATION		
Acquisition of equipment through capital leases	\$394	\$—

See notes to consolidated financial statements.

TRANSGENOMIC, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Years Ended December 31, 2010 and 2009

A. BUSINESS DESCRIPTION

Business Description.

Transgenomic, Inc. provides innovative products for the purification and analysis of nucleic acids used in the life sciences industry for research focused on molecular genetics and diagnostics. We also provide genetic variation analytical services to the medical research, clinical and pharmaceutical markets. Net sales are categorized as Laboratory Services and Instrument Related Business.

Laboratory Services:

Molecular Clinical Reference Laboratory. The molecular clinical reference laboratory specializes in genetic testing for oncology, hematology and inherited disorders. Located in New Haven, Connecticut and Omaha, Nebraska the molecular clinical reference laboratories are certified under the Clinical Laboratory Improvement Amendment (CLIA) as high complexity labs and our Omaha facility is accredited by CAP (College of American Pathologists).

Pharmacogenomics Research Services. Pharmacogenomics research services are provided by our Contract Research Organization located in Omaha, Nebraska. This lab specializes in pharmacogenomic, biomarker and mutation discovery research serving the pharmaceutical and biomedical industries world-wide for disease research, drug and diagnostic development and clinical trial support.

Instrument Related Business:

Bioinstruments. Our proprietary product is the WAVE® System which has broad applicability to genetic variation detection in both molecular genetic research and molecular diagnostics. There is a worldwide installed base of over 1,500 WAVE Systems as of December 31, 2010. We also distribute bioinstruments produced by other manufacturers (“OEM Equipment”) through our sales and distribution network. Service contracts to maintain installed systems are sold and supported by our technical support personnel.

Bioconsumables. The installed WAVE base and some OEM platforms generate a demand for consumables that are required for the continued operation of the bioinstruments. We develop, manufacture and sell these consumable products. In addition, we manufacture and sell consumable products that can be used on multiple, independent platforms. These products include SURVEYOR® Nuclease and a range of chromatography columns.

Although we have experienced declining sales and recurring net losses (resulting in an accumulated deficit of \$133.3 million at December 31, 2010), management believes existing sources of liquidity, including cash and cash equivalents of \$3.5 million, are sufficient to meet expected cash needs during 2011. Our business consolidation efforts have helped control our operating costs, however we will need to increase net sales in order to meet our liquidity needs on a long-term basis. If we cannot increase net sales, further reductions to operating expenses will be needed. In future periods, there is no assurance that we will be able to increase net sales or further reduce expenses and, accordingly, we may not have sufficient sources of liquidity to continue operations indefinitely.

B. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation.

The consolidated financial statements include the accounts of Transgenomic, Inc. and its wholly-owned subsidiary. All intercompany balances and transactions have been eliminated in consolidation.

TRANSGENOMIC, INC. AND SUBSIDIARY
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 Years Ended December 31, 2010 and 2009

Risks and Uncertainties.

Certain risks and uncertainties are inherent in our day-to-day operations and to the process of preparing our financial statements. The more significant of those risks are presented below and throughout the notes to the financial statements.

1. Use of Estimates.

The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of net sales and expenses during the reporting period. In addition, estimates and assumptions associated with the determination of the fair value of certain assets and related impairments require considerable judgment by management. Actual results could differ from the estimates and assumptions used in preparing these financial statements.

2. Concentration of Revenue Risk.

No customer accounted for more than 10% of consolidated net sales during the years ended December 31, 2010 and 2009. For the year ended December 31, 2010 one customer made up 15% of the Laboratory Services net sales. For the year ended December 31, 2009 one customer made up more than 20% of the Laboratory Services net sales.

Fair Value.

Unless otherwise specified, book value approximates fair market value.

Cash and Cash Equivalents.

Cash and cash equivalents include cash and investments with original maturities at acquisition of three months or less. Such investments presently consist of only temporary overnight investments.

Concentrations of Cash.

From time to time, we may maintain a cash position with financial institutions in amounts that exceed federally insured limits. We have not experienced any losses on such accounts as of December 31, 2010.

Accounts Receivable.

The following is a summary of activity for the allowance for doubtful accounts during the years ended December 31, 2010 and 2009:

	Beginning Balance	Dollars in Thousands		Ending Balance
		Provision	Write Offs	
Year Ended December 31, 2010	\$310	\$28	\$(4)	\$334
Year Ended December 31, 2009	\$388	\$(8)	\$(70)	\$310

While payment terms are generally 30 days, we have also provided extended payment terms of up to 90 days in certain cases. We operate globally and some of the international payment terms may be greater than 90 days. Accounts receivable are carried at original invoice and shown net of allowance for doubtful accounts and contractual allowances. The estimate made for doubtful accounts is based on a review of all outstanding amounts on a quarterly basis. We determine the allowance for doubtful accounts and contractual allowances by regularly evaluating individual customer receivables and considering a customer's financial condition, credit history and current economic conditions. Account receivables are written off when deemed uncollectible. Recoveries of account receivables previously written off are recorded when received. Management also evaluates contract terms and history of collections with third party payors. We do not charge interest on past due accounts.

TRANSGENOMIC, INC. AND SUBSIDIARY
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 Years Ended December 31, 2010 and 2009

Inventories.

Inventories are stated at the lower of cost or market net of allowance for obsolete inventory. Cost is computed using standard costs for finished goods and average or latest actual cost for raw materials and work in process, which approximates the first-in, first-out (FIFO) method.

The following is a summary of activity for the allowance for obsolete inventory during the twelve months ended December 31, 2010 and 2009:

	Dollars in Thousands			Ending Balance
	Beginning Balance	Provision	Write Offs	
Year Ended December 31, 2010	\$507	\$100	\$(89)	\$518
Year Ended December 31, 2009	\$108	\$482	\$(83)	\$507

We determine the allowance for obsolete inventory by quarterly evaluating the inventory for items deemed to be slow moving or obsolete.

Property and Equipment.

Property and equipment are carried at cost less accumulated depreciation. Depreciation is computed by the straight-line method over the estimated useful lives of the related assets as follows:

Leasehold improvements	1 to 10 years
Furniture and fixtures	3 to 7 years
Production equipment	3 to 7 years
Computer equipment	3 to 7 years
Research and development equipment	2 to 7 years

Depreciation of property and equipment totaled \$0.4 million in the year ended 2010 and \$0.6 million in the year ended 2009. Included in depreciation for the year ended December 31, 2010 is less than \$0.1 million related to capital leases. We did not have any capital leases during 2009.

Goodwill.

Goodwill is the excess of the purchase price over fair value of assets acquired and is not amortized. Goodwill is tested for impairment annually. We perform this impairment analysis during the fourth quarter of each year or when a significant event occurs which may impact goodwill. Impairment occurs when the carrying value is determined to be not recoverable thereby causing the carrying value of the goodwill to exceed its fair value. If impaired, the asset's carrying value is reduced to its fair value. No impairment existed at December 31, 2010.

Intangibles.

Intangibles include intellectual property, patents and acquired products.

1. Intellectual Property. Initial costs paid to license intellectual property from independent third parties are capitalized and amortized using the straight-line method over the license period. Ongoing royalties related to such licenses are expensed as incurred.

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TRANSGENOMIC, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Years Ended December 31, 2010 and 2009

2. Patents. We capitalize legal costs, filing fees and other expenses associated with obtaining patents on new discoveries and amortize these costs using the straight-line method over the shorter of the legal life of the patent or its economic life beginning on the date the patent is issued.

3. Intangibles. As a part of the FAMILION acquisition we acquired technology, in process technology, trademarks/tradenames and third party relationships. These costs will be amortized straight line over their estimated economic life of seven to eight years. See Footnote F.

These assets are treated as long-lived assets. Long-lived assets will be tested for impairment on an annual basis or when a significant event occurs, which may impact impairment. We quarterly review the carrying value of our long-lived assets to assess recoverability and impairment. We recorded no impairments during 2010. In 2009 we recorded less than \$0.1 million related to accelerated amortization on two license agreements that we terminated in the first quarter of 2010.

Other Long Term Assets.

Other long term assets include US security deposits and deferred tax assets.

Stock Based Compensation.

All stock options awarded to date have exercise prices equal to the market price of our common stock on the date of grant and have ten-year contractual terms. Unvested options as of December 31, 2010 had vesting periods of three years from date of grant. None of the stock options outstanding at December 31, 2010 are subject to performance or market-based vesting conditions.

We measure and recognize compensation expense for all stock-based awards made to employees and directors, including stock options. Compensation expense is based on the calculated fair value of the awards as measured at the grant date and is expensed ratably over the service period of the awards (generally the vesting period).

For the year ended December 31, 2010, we recorded compensation expense recovery of less than \$0.1 million within selling, general and administrative expense. Two executive officers departed during the second quarter of 2010. All stock options that were unvested were forfeited at the time of their departure as their requisite services period was not completed. The vesting of options exercisable for the purchase of 1.3 million shares was offset by the expense recovery for stock options that were forfeited due to the requisite service not being rendered. For the year ended December 31, 2009, we recorded compensation expense of \$0.2 million within selling, general and administrative expense as a result of the vesting of options exercisable for the purchase of 1.7 million shares during the year. As of December 31, 2010, there was \$0.1 million of unrecognized compensation expense related to unvested stock options, which is expected to be recognized over a weighted average period of nearly three years.

The fair value of the options granted during 2010 was estimated on their respective grant dates using the Black-Scholes option pricing model. The Black-Scholes model was used with the following assumptions: risk-free interest rates of 1.17% to 1.98%, based on the U.S. Treasury yield in effect at the time of grant; dividend yields of zero percent; expected lives of 5 years, based on historical exercise activity; and volatility of 103% to 105% for grants made during the year ended December 31, 2010 based on the historical volatility of our stock over a time that is consistent with the expected life of the option. A small group of senior executives hold the majority of the stock

options and are expected to hold the options until they are vested. Forfeitures of 2.2% to 2.5% have been assumed in the calculation due to the turnover of senior executives in 2010.

The fair value of the options granted during 2009 was estimated on their respective grant dates using the Black-Scholes option pricing model. The Black-Scholes model was used with the following assumptions: risk-free interest rates of 2.12% to 3.99%, based on the U.S. Treasury yield in effect at the time of grant; dividend yields of zero percent; expected lives of 5 to 10 years, based on historical exercise activity; and volatility of 80.03% to 106.00% for grants made during the year ended December 31, 2009 based on the historical volatility of our stock over a time that is consistent with the expected life of the option. A small group of senior executives held the majority of the stock options and are expected to hold the options until they are vested therefore no forfeitures were assumed in 2009.

TRANSGENOMIC, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Years Ended December 31, 2010 and 2009

Income Taxes.

Deferred tax assets and liabilities are determined based on the differences between the financial reporting and tax basis of assets and liabilities at each balance sheet date using tax rates expected to be in effect in the year the differences are expected to reverse. Deferred tax assets are reduced by a valuation allowance to the extent that it is more likely than not that they will not be realized. We had no material unrecognized tax benefits, interest, or penalties during fiscal 2010 or fiscal 2009, and we do not anticipate any such items during the next twelve months. Our policy is to record interest and penalties directly related to income taxes as income tax expense in the Consolidated Statements of Operations.

Net Sales Recognition.

Revenue is realized and earned when all of the following criteria are met:

- Persuasive evidence of an arrangement exists
- Delivery has occurred or services have been rendered
- The seller's price to the buyer is fixed or determinable, and
- Collectability is reasonably assured.

Net sales on the sales of products are recognized in accordance with the terms of the sales arrangement. Such recognition is based on receipt of an unconditional customer order and transfer of title and risk of ownership to the customer, typically upon shipment of the product under a purchase order. Our normal sales terms do not provide for the right of return unless the product is damaged or defective. Net sales from certain services associated with the analytical instruments, to be performed subsequent to shipment of the products, is deferred and recognized when the services are provided. Such services, mainly limited to installation and training services that are not essential to the functionality of the instruments, typically are performed in a timely manner subsequent to shipment of the instrument. We also enter into various service contracts that cover installed instruments. These contracts cover specific time periods and net sales associated with these contracts are deferred and ratably recognized over the service period. Deferred net sales mainly associated with our service contracts, included in the balance sheet in other accrued expenses, was approximately \$1.4 million for each of the years ended December 31, 2010 and 2009.

Net Sales from our Molecular Clinical Reference Laboratory Services are recognized on an individual test basis and takes place when the test report is completed, reviewed and sent to the client and is recorded net of the allowance for insurance, Medicare and Medicaid contractual adjustments. There are no deferred net sales associated with our Molecular Clinical Reference Laboratory. Adjustments to the allowances, based on actual receipts from the third party payers, are recorded upon settlement.

In our Pharmacogenomics Research Services Group, we perform services on a project by project basis. When payment is received in advance, revenue is recognized upon delivery of the service. These projects typically do not extend beyond one year. At December 31, 2010 and 2009, deferred net sales associated with the pharmacogenomics research projects included in the balance sheet in other accrued expenses, was less than \$0.1 million for each period.

Taxes collected from customers and remitted to government agencies for specific net sales producing transactions are recorded net with no effect on the income statement.

Research and Development.

Research and development and various collaboration costs are charged to expense when incurred.

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TRANSGENOMIC, INC. AND SUBSIDIARY
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Years Ended December 31, 2010 and 2009

Preferred Stock.

We entered into a Series A Convertible Preferred Stock Purchase Agreement on December 29, 2010, as discussed in Note L, selling shares of preferred stock and issuing warrants to purchase a certain number of shares of Series A Preferred Stock. The Series A Preferred Stock meets the definition of mandatorily redeemable stock as it is preferred capital stock which is redeemable at the option of the holder and should be reported outside of equity. Preferred stock is accreted to its redemption value. The warrants do not qualify to be treated as equity, and accordingly, are recorded as a liability. A preferred stock conversion feature is embedded within the Series A Preferred Stock that meets the definition of a derivative. The preferred stock, warrant liability and preferred stock conversion feature are all recorded separately and were initially recorded at fair value using the Black Scholes model. We are required to record these instruments at fair value at each reporting date and changes will be recorded as an adjustment to earnings. The warrant liability and preferred stock conversion feature are considered level three financial instruments.

Translation of Foreign Currency.

Our foreign subsidiary uses the local currency of the country in which they are located as their functional currency. Its assets and liabilities are translated into U.S. dollars at the exchange rates in effect at the balance sheet date. Cumulative translation losses of less than \$0.1 are reported as accumulated other comprehensive loss on the accompanying consolidated balance sheets for the year ended December 31, 2010. Cumulative translation gains of \$0.2 million were reported as accumulated other comprehensive income for the year ended December 31, 2009. Revenues and expenses are translated at the average rates during the period. For transactions that are not denominated in the functional currency, we recognized net losses of \$0.3 million as foreign currency transaction losses in the determination of net loss for each of the years ending December 31, 2010 and 2009.

Other Income.

Other income consists primarily of interest income from cash and cash equivalents invested in overnight instruments. Other income in the year ended December 31, 2010 includes an award of a federal grant under the Qualifying Therapeutic Discovery Project related to COLD-PCR, Surveyor Scan kit development for key cancer pathway gene mutations and mtDNA damage assays. Other income related to this federal grant was \$0.6 million net of consulting fees. Other income for the year ended December 31, 2009 was less than \$0.1 million.

Comprehensive Income.

Accumulated other comprehensive income at December 31, 2010 and 2009 consisted of foreign currency translation adjustments, net of applicable tax of zero. We deem our foreign investments to be permanent in nature and do not provide for taxes on currency translation adjustments arising from converting investments in a foreign currency to U.S. dollars.

Earnings Per Share.

Basic earnings per share is calculated based on the weighted average number of common shares outstanding during each period. Diluted earnings per share include shares issuable upon exercise of outstanding stock options, warrants or conversion rights that have exercise or conversion prices below the market value of our common stock. Options, warrants and conversion rights pertaining to 18,607,229 and 11,309,887 shares of our common stock have been

excluded from the computation of diluted earnings per share at December 31, 2010 and 2009, respectively. The options, warrants and conversion rights that were exercisable in 2010 and 2009 were not included because the effect would be anti-dilutive due to the net loss. As a result, none of our outstanding options, warrants or conversion rights affect the calculation of diluted earnings per share.

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Recently Issued Accounting Pronouncements.

In October 2009, the FASB issued ASU No. 2009-13, Revenue Recognition (ASC 605): Multiple-Deliverable Revenue Arrangements (a consensus of the FASB Emerging Issues Task Force); effective for years beginning after June 15, 2010. This standard update became effective for us on January 1, 2011. Vendors often provide multiple products and/or services to their customers as part of a single arrangement. These deliverables may be provided at different points in time or over different time periods. The existing guidance regarding how and whether to separate these deliverables and how to allocate the overall arrangement consideration to each was originally captured in EITF Issue 00-21, Revenue Arrangements with Multiple Deliverables, which is now codified at ASC 605-25, Revenue Recognition – Multiple-Element Arrangements. The issuance of ASU 2009-13 amends ASC 605-25 and represents a significant shift from the existing guidance that was considered abuse-preventative and heavily geared toward ensuring that revenue recognition was not accelerated. The application of this new guidance is expected to result in accounting for multiple-deliverable revenue arrangements that better reflects their economics as more arrangements will be separated into individual units of accounting. We are in the final stages of analyzing the impact of ASU 2009-13.

In October 2009, the FASB issued ASU No. 2009-14, Software (ASC 985): Certain Revenue Arrangements That Include Software Elements (a consensus of the FASB Emerging Issues Task Force); effective for years beginning after June 15, 2010. This standard update became effective for us on January 1, 2011. ASU 2009-14 modifies the existing scope guidance in ASC 985-605, Software Revenue Recognition, for revenue arrangements with tangible products that include software elements. This modification was made primarily due to the changes in ASC 605-25 noted previously, which further differentiated the separation and allocation guidance applicable to non-software arrangements as compared to software arrangements. Prior to the modification of ASC 605-25, the separation and allocation guidance for software and non-software arrangements was more similar. Under ASC 985-605, which was originally issued as AICPA Statement of position 97-2, Software Revenue Recognition, an arrangement to sell a tangible product along with software was considered to be in its scope if the software was more than incidental to the product as a whole. We are in the final stages of analyzing the impact of ASU 2009-14.

C. ACQUISITION

We acquired the FAMILION family of genetic tests from PGxHealth. PGxHealth is a subsidiary of Clinical Data, Inc. (NasdaqGM:CLDA) with a sales price of \$18.8 million. We secured \$6.0 million of financing from entities affiliated with Third Security, LLC, a leading life sciences investment firm, to fund the cash portion of our acquisition of Clinical Data's diagnostic business. This strategic acquisition provides us with proprietary genetic commercial tests that have an established revenue base, proprietary biomarker assays, an additional CLIA-certified laboratory operation and established test reimbursement and coverage policies that offer access to testing. The acquired assets and liabilities assumed are reported as a component of our laboratory services segment.

Under the terms of the financing with entities affiliated with Third Security, we issued an aggregate of 2,586,205 shares of the Company's newly created Series A convertible preferred stock to certain affiliates of Third Security. Additionally we issued such affiliates of Third Security warrants to purchase an aggregate of up to 1,293,102 shares of Series A preferred stock at an exercise price of \$2.32 per share. The Series A preferred shares issuable pursuant to the purchase agreement and upon exercise of the warrants are convertible into shares of our common stock at a conversion price of \$0.58 per share, for an aggregate of 15,517,228 million shares of common stock. Upon full exercise of the warrants, we will receive approximately \$3.0 million. These securities were issued

for an aggregate purchase price of \$6.0 million.

We entered into two notes payable with PGxHealth as a part of the acquisition. The first note is a three year secured promissory note in the amount of \$8.6 million with interest accruing at 10%. The second note is a one year secured promissory note for facility improvements of \$1.0 million with interest payable at 6.5%. See further information in Note G to the financial statements. Certain liabilities were assumed and various contingent liabilities recorded. The contingent liabilities include payments owed upon the collection of certain accounts receivable, retention bonuses for certain employees and royalties due to vendors based on milestone considerations.

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The following table summarizes the consideration paid for the acquired assets and liabilities assumed at the acquisition date.

Consideration	Dollars in Thousands
Cash	\$ 6,000
Notes payable	9,628
Assumed liabilities	452
Contingent liabilities	2,736
Fair value of consideration transferred	\$ 18,816

Acquisition related costs included in selling, general and administrative expenses in our Statement of Operations for the year ended December 31, 2010 were \$0.8 million. We incurred \$0.2 million in acquisition related costs to issue preferred stock which were recorded against the proceeds received upon the issuance of such preferred stock.

Recognized Amounts of Identifiable Assets Acquired and Liabilities Assumed	Dollars in Thousands
Working capital, net	\$ 3,222
Property and Equipment	639
Identifiable intangible assets	8,680
Total identifiable net assets	12,541
Goodwill	6,275
Total purchase price	18,816

The fair value of the financial assets acquired includes accounts receivable with a fair value of \$3.1 million. The gross amount due is \$7.0 million, of which \$3.9 million is expected to be uncollectible.

The goodwill arising from the acquisition primarily relates to synergies of the combined companies. The goodwill has been assigned to our Laboratory Services segment and is expected to be deductible for tax purposes.

The fair value of the preferred stock and related securities issued as a part of the consideration paid was determined on the basis of the closing market price of our common stock on the acquisition date, December 29, 2010.

The following table sets forth the pro forma revenue and earnings of the combined entity if the acquisition had occurred as of the beginning of our prior fiscal year. No revenue or net income was included in our actual results for the year ended December 31, 2010 or 2009. These pro forma amounts do not purport to be indicative of the actual results that would have been obtained had the acquisition occurred at that time.

	Dollars in Thousands	
	Year Ended December 31,	
	2010	2009
Revenue – Supplemental pro forma results	\$ 33,733	\$ 35,112
Net loss – Supplemental pro forma results	(7,716)	(13,071)

D. RESTRUCTURING CHARGES

In the third quarter of 2010 we made a decision to consolidate our research and development activities in Omaha, Nebraska. We substantially completed the transition at December 31, 2010. We have recognized expenses for restructuring, including but not limited to, severance, facility costs and costs to move equipment from Gaithersburg, Maryland to Omaha, Nebraska. These restructuring charges are attributable to our lab services and instrument segments.

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Restructuring charges include:

	Dollars in Thousands		
	Costs Incurred in the Three Months Ended December 31, 2010	Cumulative Costs Incurred at December 31, 2010	Total Expected Costs
	Severance and related costs	\$ 12	\$ 53
Facility closure costs	22	45	63
Other	32	40	66
Restructuring charges	\$ 66	\$ 138	\$ 182

In the fourth quarter of 2010 we had a reduction in workforce of five employees with severance payments of less than \$0.1 million which was attributable to our instrument segment.

E. INVENTORIES

Inventories (net of allowances for obsolescence) consisted of the following:

	Dollars in Thousands	
	December 31, 2010	December 31, 2009
Finished goods	\$ 2,119	\$ 2,322
Raw materials and work in process	1,531	1,588
Demonstration inventory	212	149
	\$ 3,862	\$ 4,059
Less allowance for obsolescence	(518)	(507)
Total	\$ 3,344	\$ 3,552

F. INTANGIBLES AND OTHER ASSETS

Finite lived intangible assets and other assets consisted of the following:

	Dollars in Thousands					
	December 31, 2010			December 31, 2009		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Intellectual property	\$ 290	\$ 274	\$ 16	\$ 310	\$ 284	\$ 26
Patents	511	245	266	598	241	357
Intangibles – acquired technology	6,535	—	6,535	—	—	—
Intangibles – third party payor relationships	367	—	367	—	—	—
Intangibles – assay royalties	1,434	—	1,434	—	—	—
Intangibles – tradenames and trademarks	344	—	344	—	—	—
Total	9,481	519	8,962	908	525	383

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Other assets	154	—	154	200	—	200
Total	\$ 9,635	\$ 519	\$ 9,116	\$ 1,108	\$ 525	\$ 583

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	Estimated Useful Life
Intellectual property	10 years
Patents	7 years
Intangibles – acquired technology	7 – 8 years
Intangibles – third party payor relationships	N/A
Intangibles – assay royalties	7 years
Intangibles – tradenames and trademarks	7 years

During 2009 we accelerated amortization on two intellectual property license agreements that we terminated in the first quarter of 2010. In addition we accelerated amortization on another license agreement, however; we are not terminating that agreement. In total the change to the net book value of intellectual property was less than \$0.1 million. We wrote off less than \$0.1 million in patents that we are no longer using.

Other assets include US security deposits and deferred tax assets.

Amortization expense for intangible assets was less than \$0.1 million during both years ended December 31, 2010 and 2009. Amortization expense for intangible assets is expected to be \$1.2 million in each of years 2011 through 2017.

G. DEBT

	Dollars in Thousands	
	Year Ended December 31,	
	2010	2009
PGxHealth note payable(1)	\$ 8,640	\$ —
PGxHealth note payable(2)	989	—
	\$ 9,629	\$ —

(1) The First Note is a three year senior secured promissory note to PGxHealth, LLC entered into on December 29, 2010 in conjunction with our acquisition of the FAMILION family of genetic tests from PGxHealth. Interest is payable at 10% per year with quarterly interest payments through March 29, 2012. Thereafter, quarterly installments will include both principal and interest through December 30, 2013.

(2) The Second Note is a one year senior secured promissory note to PGxHealth, LLC entered into on December 31, 2010 for facility improvements made to the CLIA certified laboratory in New Haven, Connecticut. Interest is payable at 6.5% per year with the principal and interest payable in twelve monthly installments with the final payment due on December 31, 2011.

The entire unpaid balance of the Notes will become immediately due and payable if: (i) we fail to make timely payments under the Notes; (ii) we make an assignment for the benefit of creditors; (iii) we file for bankruptcy; or (iv) upon any event of default under the Security Agreement. Additionally, under the terms of the First Note, if we consummate an equity financing that involves the receipt by us of net proceeds of not less than \$6,000,000, then we shall, upon the consummation of such equity financing, pay to PGxHealth the lesser of: (i) 25% of the gross proceeds received from such financing; and (ii) the then-outstanding balance under the First Note. Under the terms of the Second Note, in the event of a sale of all or substantially all of the assets of the Company, we shall pay PGxHealth the lesser of: (i) 100% of the proceeds, less certain fees, received pursuant to such sale; and (ii) the then-outstanding

balance under the Second Note.

The notes are secured by the assets of Transgenomic.

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The aggregate minimum principal maturities of the debt for each of the three fiscal years following December 31, 2010 are as follows:

2011	\$989
2012	3,703
2013	4,937
	\$9,629

H. CAPITAL LEASES

The following is an analysis of the leased property under capital leases.

Classes of Property	Dollars in Thousands	
	Asset Balances at December 31	
	2010	2009
Equipment	\$ 394	\$ —
Less: Accumulated amortization	13	—
Total	\$ 381	\$ —

The following is a schedule by years of future minimum lease payments under capital leases together with the present value of the net minimum lease payments as of December 31, 2010.

Year ending December 31:

	Dollars in Thousands
2011	\$ 190
2012	92
2013	76
Total minimum lease payments	\$ 358
Less: Amount representing interest	(32)
Present value of net minimum lease payments	\$ 326

I. COMMITMENTS AND CONTINGENCIES

We are subject to a number of claims of various amounts, which arise out of the normal course of business. In the opinion of management, the disposition of pending claims will not have a material adverse effect on our financial position, results of operations or cash flows.

We lease certain equipment, vehicles and operating facilities under non-cancellable operating leases that expire on various dates through 2016. The future minimum lease payments required under these leases are approximately \$1.2 million in 2011, \$0.8 million in 2012, \$0.2 million in 2013, \$0.1 million in 2014, \$0.1 million in 2015 and less than \$0.1 million in 2016. Rent expense for each of the years ended December 31, 2010 and 2009 was \$0.8 million.

We have entered into an employment agreement with Craig J. Tuttle, our President and Chief Executive Officer. The current term of Mr. Tuttle's employment agreement ends on July 12, 2011. The employment agreement provides that

Mr. Tuttle will be entitled to receive severance payment from the Company if his employment is terminated involuntarily except if such termination is based on “just cause”, as that term is defined in his employment agreement. The severance payment payable in the event of involuntary termination without just cause is equal to his annual base salary at the time of termination and will be paid over a twelve-month period. The employment agreement provides that the severance payment provision will be honored if the Company is acquired by, or merged into, another company and his position is eliminated as a result of such acquisition or merger. In addition we have one employee who is entitled to a severance payment of less than \$0.1 million if the employee’s position is eliminated prior to July 2012.

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At December 31, 2010, firm commitments to vendors to purchase components used in WAVE Systems and instruments manufactured by others totaled \$0.1 million.

J. INCOME TAXES

The Company's provision for income taxes for the years ended December 31, 2010 and 2009 relates to income taxes in states, foreign countries and other local jurisdictions and differs from the amounts determined by applying the statutory Federal income tax rate to loss before income taxes for the following reasons:

	Dollars in Thousands	
	2010	2009
Benefit at federal rate	\$(1,015)	\$(639)
Increase (decrease) resulting from:		
State income taxes—net of federal benefit	20	(10)
Foreign subsidiary tax rate difference	(27)	(50)
Tax contingency	45	48
Net operating loss expiration	—	1,258
Earnings repatriation	1,479	—
Miscellaneous permanent differences	60	93
Other—net	86	(33)
Valuation allowance	(498)	(625)
Current income tax expense	\$150	\$42

	Dollars in Thousands	
	2010	2009
Federal:		
Current	\$ 4	\$ (58)
Deferred	—	—
Total Federal	\$ 3	\$ (58)
State:		
Current	\$ 29	\$ (16)
Deferred	—	—
Total State	\$ 29	\$ (16)
Foreign:		
Current	\$ 111	\$ (60)
Deferred	6	176
Total Foreign	\$ 117	\$ 116
Total Tax Provision	\$ 150	\$ 42

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The Company's deferred income tax asset from continuing and discontinued operations at December 31, 2010 and 2009 is comprised of the following temporary differences:

	Dollars in Thousands	
	2010	2009
Deferred Tax Asset:		
Net operating loss carryforward	\$38,201	\$38,688
Research and development credit carryforwards	1,232	1,355
Deferred net sales	151	194
Inventory	188	186
Other	473	350
	40,245	40,773
Less valuation allowance	(40,141)	(40,639)
Deferred Tax Asset	\$ 104	\$ 134
Deferred Tax Liability:		
Uninstalled instruments	\$ 159	\$ 183
Deferred Tax Liability	\$ 159	\$ 183
Net Deferred Liability	\$(55)	\$(49)

At December 31, 2010, we had total unused federal tax net operating loss carryforwards from continuing and discontinued operations of \$104.3 million of which \$2.8 million expires in 2012, \$1.8 million expires in 2018, \$8.2 million expires in 2019, \$9.7 million expires in 2020, \$8.2 million expires in 2021, \$16.9 million expires in 2022, \$16.2 million expires in 2023, \$17.4 million expires in 2024, \$8.2 million expires in 2025, \$6.8 million expires in 2026, \$3.2 million expires in 2027, \$1.3 million expires in 2028, \$2.1 million expires in 2029, and \$1.5 million expires in 2030. Of these federal net operating loss carryforwards, \$6.4 million were obtained in the acquisition of Annovis, Inc. and may be subject to certain restrictions. At December 31, 2010, we had unused state tax net operating loss carryforwards from continuing and discontinued operations of approximately \$36.0 million that expire at various times beginning in 2011. At December 31, 2010, we had unused research and development credit carryforwards from continuing and discontinued operations of \$1.2 million that expire at various times between 2011 and 2024. A net deferred tax liability was recorded during 2010 related to the UK income taxes for \$0.1 million. A valuation allowance has been provided for the remaining deferred tax assets, due to the cumulative losses in recent years and an inability to utilize any additional losses as carrybacks. We will continue to assess the recoverability of deferred tax assets and the related valuation allowance. To the extent we begin to generate income in future years and it is determined that such valuation allowance is no longer required, the tax benefit of the remaining deferred tax assets will be recognized at such time.

We had no material unrecognized tax benefits, interest, or penalties during fiscal 2009 or fiscal 2008, and we do not anticipate any such items during the next twelve months. Our policy is to record interest and penalties directly related to income taxes as income tax expense in the Consolidated Statements of Operations. We file income tax returns in the U.S. federal jurisdiction, various U.S. state jurisdictions and various foreign jurisdictions. We have statutes of limitation open for Federal income tax returns related to tax years 2007 and 2008. We have state income tax returns subject to examination primarily for tax years 2006 through 2008. Open tax years related to foreign jurisdictions remain subject to examination. Our primary foreign jurisdiction is the United Kingdom which has open tax years for

2006 through 2008.

During the years ended December 31, 2010 and 2009, there were no material changes to the liability for uncertain tax positions. The liability for uncertain tax positions relates to potential uncertain tax positions in foreign jurisdictions.

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K. EMPLOYEE BENEFIT PLAN

We maintain an employee 401(k) retirement savings plan that allows for voluntary contributions into designated investment funds by eligible employees. Prior to October 1, 2010 we matched the employee's contributions at the rate of 50% on the first 6% of contributions. Effective October 1, 2010, Transgenomic discontinued matching employee 401(k) contributions. We may, at the discretion of our Board of Directors, make additional contributions on behalf of the Plan's participants. Contributions to the 401(k) plan were \$0.1 million for the year ended December 31, 2010. Contributions to the 401(k) plan were less than \$0.1 million for the year ended December 31, 2009.

L. STOCKHOLDERS' EQUITY

Common Stock.

The Company's Board of Directors is authorized to issue up to 100,000,000 shares of common stock, from time to time, as provided in a resolution or resolutions adopted by the Board of Directors.

Common Stock Warrants.

Warrants covering 5,172,408 shares of common stock were issued during 2010. No common stock warrants were exercised during 2010. No common stock warrants were issued or exercised during 2009. At December 31, 2010, there were warrants outstanding that were exercisable to purchase 5,697,408 shares of common stock.

Warrant Holder	Issue Year	Expiration Year	Underlying Shares	Exercise Price
Laurus Master Fund, Ltd. (1)	2004	2011	125,000	\$ 2.39
Laurus Master Fund, Ltd. (1)	2004	2011	400,000	\$ 1.13
Affiliates of Third Security, LLC(2)	2010	2015	5,172,408	\$.58
Total			5,697,408	

(1) These warrants were issued in conjunction with two loans that had been made to us by Laurus Master Fund, Ltd. (the "Laurus Loans"), and subsequent modifications of these loans. In conjunction with the 2005 private placement, the exercise prices of these warrants were adjusted according to repricing provisions contained in the original warrant agreements. While the Laurus Loans have been terminated, the warrants remain outstanding. Due to the repricing provision, these warrants are considered liabilities for financial reporting purposes.

(2) These warrants were issued in conjunction with the Series A stock financing with certain entities affiliated with Third Security. The number of shares shown reflects the post conversion shares.

Preferred Stock.

The Company's Board of Directors is authorized to issue up to 15,000,000 shares of preferred stock in one or more series, from time to time, with such designations, powers, preferences and rights and such qualifications, limitations and restrictions as may be provided in a resolution or resolutions adopted by the Board of Directors. The authority of the Board of Directors includes, but is not limited to, the determination or fixing of the following with respect to shares of such class or any series thereof: (i) the number of shares; (ii) the dividend rate, whether dividends shall be

cumulative and, if so, from which date; (iii) whether shares are to be redeemable and, if so, the terms and amount of any sinking fund providing for the purchase or redemption of such shares; (iv) whether shares shall be convertible and, if so, the terms and provisions thereof; (v) what restrictions are to apply, if any, on the issue or reissue of any additional preferred stock; and (vi) whether shares have voting rights. The preferred stock may be issued with a preference over the common stock as to the payment of dividends. Classes of stock such as the preferred stock may be used, in certain circumstances, to create voting impediments on extraordinary corporate transactions or to frustrate persons seeking to effect a merger or otherwise to gain control of the Company. For the foregoing reasons, any preferred stock issued by the Company could have an adverse effect on the rights of the holders of the common stock.

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On December 29, 2010, we entered into a Series A Convertible Preferred Stock Purchase Agreement with Third Security pursuant to which we: (i) sold an aggregate of 2,586,205 shares of Series A Convertible Preferred Stock; and (ii) issued warrants to purchase up to an aggregate of 1,293,102 shares of Series A Preferred Stock with an exercise price of \$2.32 per share. The Warrants may be exercised at any time from December 29, 2010 until December 28, 2015 and contain a “cashless exercise” feature. The shares of Series A Preferred Stock issuable pursuant to the Series A Purchase Agreement and upon exercise of the Warrants are initially convertible into shares of our common stock at a rate of 4-for-1, which conversion rate is subject to further adjustment as set forth in the Certificate of Designation. The aggregate gross proceeds from the issuance was \$6.0 million.

The Series A Preferred Stock meets the definition of mandatorily redeemable stock as it is preferred capital stock which is redeemable at the option of the holder and should be reported outside of equity. Preferred stock is accreted to its redemption value. The warrants do not qualify to be treated as equity, and accordingly, are recorded as a liability. A preferred stock conversion feature is embedded within the Series A Preferred Stock that meets the definition of a derivative. The preferred stock, warrant liability and preferred stock conversion feature are all recorded separately and were initially recorded at fair value using the Black Scholes model. We are required to record these instruments at fair value at each reporting date and changes will be recorded as an adjustment to earnings. The warrant liability and preferred liability are considered level three financial instruments.

The analysis produced a valuation for the three components of the instrument:

Redeemable Preferred Stock	\$1,666
Preferred Stock Conversion Feature	1,983
Warrants	2,351
	\$6,000

The costs to secure the Preferred Stock were taken against the preferred stock. For the year ended December 31, 2010 these costs were \$0.2 million.

We used the net proceeds from the financing to acquire the FAMILION family of genetic tests from PGxHealth, a subsidiary of Clinical Data.

In connection with the Financing, we filed a Certificate of Designation of Series A Convertible Preferred Stock with the Secretary of State of the State of Delaware, designating 3,879,307 shares of our Preferred Stock as Series A Preferred Stock. Certain rights of the holders of the Series A Preferred Stock are senior to the rights of the holders of Common Stock. The Series A Preferred Stock has a liquidation preference equal to its original price per share, plus any accrued and unpaid dividends thereon. The Series A Preferred Stock accrues cumulative dividends at the rate of 10.0% of the original price per share per annum.

Generally, the holders of the Series A Preferred Stock are entitled to vote together as a single group with the holders of Common Stock on an as-converted basis. However, the Certificate of Designation provides that we shall not perform some activities, subject to certain exceptions, without the affirmative vote of a majority of the holders of the outstanding shares of Series A Preferred Stock.

In connection with the Financing, we also entered into a registration rights agreement with the Investors (the “Registration Rights Agreement”). Pursuant to the terms of the Registration Rights Agreement, the Company has

granted the Investors certain demand, “piggyback” and S-3 registration rights covering the resale of the shares of Common Stock underlying the Series A Preferred Stock issued pursuant to the Series A Purchase Agreement and issuable upon exercise of the Warrants and all shares of Common Stock issuable upon any dividend or other distribution with respect thereto. The holders of the Series A Preferred Stock are entitled to receive quarterly dividends which will accrue whether or not declared, shall compound annually and shall be cumulative. In any calendar quarter we shall be required to pay from funds legally available a cash dividend in the amount of 50% of the distributable cash flow or aggregate amount of dividends accrued on the Series A Preferred Stock.

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M. EQUITY INCENTIVE PLAN

The Company's 2006 Equity Incentive Plan (the "Plan") allows the Company to make awards of various types of equity-based compensation, including stock options, dividend equivalent rights ("DERs"), stock appreciation rights ("SARs"), restricted stock, restricted stock units, performance units, performance shares and other awards, to employees and directors of the Company. The Plan was adopted in 2006 as a modification of the Company's 1997 Stock Option Plan (the "Prior Plan"). In addition to providing for additional types of equity-based awards, the Plan increased the total number of shares of common stock that the Company may issue from 7,000,000 under the Prior Plan to 10,000,000 shares under the Plan; provided, that no more than 5,000,000 of such shares may be used for grants of restricted stock, restricted stock units, performance units, performance shares and other awards.

The Plan is administered by the Compensation Committee of the Board of Directors (the "Committee") which has the authority to set the number, exercise price, term and vesting provisions of the awards granted under the Plan, subject to the terms thereof. Either incentive or non-qualified stock options may be granted to employees of the Company, but only nonqualified stock options may be granted to nonemployee directors and advisors. However, in either case, the Plan requires that stock options must be granted at exercise prices not less than the fair market value of the common stock on the date of the grant. Options issued under the plan vest over periods as determined by the Compensation Committee and expire 10 years after the date the option was granted. To date, the only awards made under the Plan (and the Prior Plan) have been non-incentive stock options.

For the year ended December 31, 2010, we recorded compensation expense recovery of less than \$0.1 million within selling, general and administrative expense. Two executive officers departed during the second quarter of 2010. All stock options that were unvested were forfeited at the time of their departure as their requisite services periods were not completed. The vesting of options exercisable for the purchase of 1.3 million shares was offset by the expense recovery for stock options that were forfeited due to the requisite service not being rendered. For the year ended December 31, 2009, we recorded compensation expense of \$0.2 million within selling, general and administrative expense as a result of the vesting of options exercisable for the purchase of 1.7 million shares. As of December 31, 2010, there was less than \$0.1 million of unrecognized compensation expense related to unvested stock options, which is expected to be recognized over a weighted average period of nearly three years.

The fair value of the options granted during 2010 was estimated on their respective grant dates using the Black-Scholes option-pricing model. The Black-Scholes model was used with the following assumptions: risk-free interest rates of 1.17% to 1.98%, based on the U.S. Treasury yield in effect at the time of grant; dividend yields of zero percent; expected lives of five years, based on historical exercise activity; and volatility of 103% to 105% for grants made during the year ended December 31, 2010 based on the historical volatility of our stock over a time that is consistent with the expected life of the option. A small group of senior executives hold the majority of the stock options and are expected to hold the options until they are vested. Forfeitures of 2.2% to 2.5% have been assumed in the calculation.

The fair value of the options granted during 2009 was estimated on their respective grant dates using the Black-Scholes option pricing model. The Black-Scholes model was used with the following assumptions: risk-free interest rates of 2.12% to 3.99%, based on the U.S. Treasury yield in effect at the time of grant; dividend yields of zero percent; expected lives of 5 to 10 years, based on historical exercise activity; and volatility of 106.08% to 80.03% for grants made during the year ended December 31, 2009 based on the historical volatility of our stock over a time that is consistent with the expected life of the option. A small group of senior executives hold the majority of the

stock options and are expected to hold the options until they are vested therefore minimal forfeitures were assumed in 2009.

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The following table summarizes activity under the Plan (and the Prior Plan) during the year ended December 31, 2010:

	Number of Options	Weighted Average Exercise Price
Balance at January 1, 2010:	3,331,731	\$ 2.39
Granted	125,000	.50
Exercised	(100,000)	(.42)
Forfeited	(593,499)	(.73)
Expired	(198,231)	(11.07)
Balance at December 31, 2010:	2,565,001	\$ 2.08
Exercisable at December 31, 2010	2,358,334	\$ 2.22

The following table summarizes activity under the Plan (and the Prior Plan) during the year ended December 31, 2009:

	Number of Options	Weighted Average Exercise Price
Balance at January 1, 2009:	3,531,064	\$ 2.54
Granted	70,000	.42
Exercised	—	—
Forfeited	(72,833)	(1.39)
Expired	(196,500)	(4.85)
Balance at December 31, 2009:	3,331,731	\$ 2.39
Exercisable at December 31, 2009	2,518,671	\$ 2.96

The following table summarizes the stock options that were issued during the year ended December 31, 2010:

	Number of Options	Exercise Price
June 7, 2010	75,000	\$ 0.58
October 29, 2010	50,000	\$ 0.39
	125,000	

The weighted average grant date fair value per share of options granted during the years ended December 31, 2010 and 2009 was \$0.38 and \$0.33 respectively.

The following summarizes all stock options outstanding at December 31, 2010:

Exercise Price Range	Number of Options Outstanding	Remaining Weighted-Average Contractual Life	Weighted-Average Exercise Price	Number of Options Exercisable
\$0.00 - \$1.30	1,755,668	5.8 years	\$ 0.80	1,549,001

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\$1.31 - \$2.60	308,333	1.9 years	\$ 1.94	308,333
\$2.61 - \$3.90	10,000	0.0 years	\$ 2.90	10,000
\$5.21 - \$6.50	401,500	.4 years	\$ 6.07	401,500
\$7.81 - \$9.10	10,000	.4 years	\$ 9.00	10,000
\$9.11 - \$10.00	79,500	.5 years	\$ 9.90	79,500
	2,565,001			2,358,334

All stock options outstanding were issued to employees or outside directors.

TRANSGENOMIC, INC. AND SUBSIDIARY
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The aggregate intrinsic value of stock options exercisable was less than \$0.1 million at December 31, 2010. The aggregate intrinsic value of stock options outstanding was less than \$0.1 million at December 31, 2010. During the year ended December 31, 2010, 100,000 stock options were exercised. No stock options were exercised in the year ended December 31, 2009.

N. OPERATING SEGMENT AND GEOGRAPHIC INFORMATION

Our chief decision-maker is the Chief Executive Officer, who regularly evaluates our performance based on net sales and gross profit. The preparation of this segment analysis required management to make estimates and assumptions around expense below the gross profit level. While we believe the segment information to be directionally correct, actual results could differ from the estimates and assumptions used in preparing this information.

The accounting policies of the segments are the same as the policies discussed in Footnote B – Summary of Significant Accounting Policies.

Segment information for the years ended December 31, 2010 and 2009 is as follows:

	Dollars in Thousands					
	2010			2009		
	Lab Services	Instrument Business	Total	Lab Services	Instrument Business	Total
Net Sales	\$4,979	\$15,069	\$20,048	\$4,566	\$17,457	\$22,023
Gross Profit	1,438	8,326	9,764	1,728	9,877	11,605
Net Income/(Loss) before Taxes	(2,526)	(459)	(2,984)	(2,273)	395	(1,878)
Income Taxes	—	150	150	—	42	42
Net Income/(Loss)	\$(2,526)	\$(608)	\$(3,134)	\$(2,273)	\$353	\$(1,920)
Depreciation/Amortization	304	190	495	296	450	746
Restructure	65	73	138	—	—	—
Interest Income (Expense)	(1)	(3)	(4)	4	11	15
Net Assets	\$24,631	\$7,396	\$32,027	\$7,457	\$8,547	\$16,004

We have two reportable operating segments. Net sales by product were as follows:

	Dollars in Thousands	
	Years Ended December 31, 2010	2009
Laboratory Services:		
Molecular Clinical Reference Laboratory	\$ 3,606	\$ 3,541
Pharmacogenomics Research Services	1,373	1,025
	4,979	4,566
Instrument Related Business:		
Bioinstruments	8,320	10,175

Bioconsumables	6,749	7,282
	15,069	17,457
Total Net Sales	\$ 20,048	\$ 22,023

TRANSGENOMIC, INC. AND SUBSIDIARY
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Net cost of goods sold were as follows:

	Dollars in Thousands	
	Years Ended December 31,	
	2010	2009
Laboratory Services:		
Molecular Clinical Reference Laboratory	\$ 2,125	\$ 2,018
Pharmacogenomics Research Services	1,416	820
	3,541	2,838
Instrument Related Business:		
Bioinstruments	3,560	3,801
Bioconsumables	3,183	3,779
	6,743	7,580
Total Cost of Goods Sold	\$ 10,284	\$ 10,418

Net sales for the year ended December 31, 2010 and 2009 by country were as follows:

	Dollars in Thousands	
	Years Ended December 31,	
	2010	2009
United States	\$ 8,729	\$ 8,777
Italy	3,294	3,683
United Kingdom	1,412	842
Germany	1,366	1,383
France	1,160	1,545
Netherlands	56	1,464
All Other Countries	4,031	4,329
Total	\$ 20,048	\$ 22,023

No other country accounted for more than 5% of total net sales.

No customer accounted for more than 10% of consolidated net sales during the years ended December 31, 2010 and 2009. For the year ended December 31, 2010 one customer made up 15% of the Laboratory Services net sales. For the year ended December 31, 2009 one customer made up 20% of the Laboratory Services net sales.

More than 95% of our long-lived assets are within the United States. Substantially all of the remaining long-lived assets are within Europe.

O. SUBSEQUENT EVENTS

Events or transactions that occur after the balance sheet date, but before the financial statements are complete, are reviewed to determine if they should be recognized. On February 19, 2011, 125,000 common stock warrants to Laurus Fund, Ltd expired unexercised. We have no other material subsequent events to be disclosed.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on this 21st day of October 2011.

TRANSGENOMIC, INC.

By: /s/ CRAIG J.
TUTTLE
Craig J. Tuttle,
President and Chief
Executive Officer

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on this 21st day of October, 2011.

By: /s/ CRAIG J.
TUTTLE
Craig J. Tuttle,
President and Chief
Executive Officer