NovaBay Pharmaceuticals, Inc.
Form 10-Q
May 03, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2012

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 number 001-33678

NOVABAY PHARMACEUTICALS, INC.
(Exact name of registrant as specified in its charter)

Delaware	68-0454536
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

5980 Horton Street, Suite 550, Emeryville CA 94608
(Address of principal executive offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: (510) 899-8800

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. Yesx Noo

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yesx Noo

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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o		Accelerated filer	o
Non-accelerated filer o		Smaller reporting company	x

(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). Yeso Nox

As of April 30, 2012, there were 28,940,562 shares of the registrant’s common stock outstanding.

NOVABAY PHARMACEUTICALS, INC.

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Unless the context requires otherwise, all references in this report to "we," "our," "us," the "Company" and "NovaBay" refer to NovaBay Pharmaceuticals, Inc. and its subsidiaries.

PART I
FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)
CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)	March 31, 2012 (unaudited)	December 31, 2011 (Note 2)
ASSETS		
Current assets:		
Cash and cash equivalents	$6,121	$8,428
Short-term investments	5,232	5,710
Accounts receivable	1,009	3
Prepaid expenses and other current assets	427	417
Total current assets	12,789	14,558
Property and equipment, net	1,148	1,270
Other assets	105	135
TOTAL ASSETS	$14,042	$15,963
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities:		
Current liabilities:		
Accounts payable	$439	$472
Accrued liabilities	1,161	1,061
Deferred revenue	1,334	1,305
Total current liabilities	2,934	2,838
Deferred revenues - non-current	869	945
Deferred rent	115	115
Warrant liability	2,756	2,721
Total liabilities	6,674	6,619
Stockholders' Equity:		
Preferred stock, $0.01 par value; 5,000 shares authorized; none outstanding at at March 31, 2012 and December 31, 2011	—	—
Common stock, $0.01 par value; 65,000 shares authorized at March 31, 2012 and December 31, 2011; 28,827 and 28,587 issued and outstanding at March 31, 2012 and December 31, 2011, respectively	288	286
Additional paid-in capital	42,937	42,386
Accumulated other comprehensive loss	(42)	(44)
Accumulated deficit during development stage	(35,815)	(33,284)
Total stockholders' equity	7,368	9,344
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$14,042	$15,963

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

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NOVABAY PHARMACEUTICALS, INC.
(a development stage company)
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(unaudited)

(in thousands, except per share data)	Three Months Ended March 31, 2012	2011	Cumulative Period from July 1, 2002 (inception) to March 31, 2012
Revenue:			
License and collaboration revenue	$1,315	$2,490	$ 51,914
Other revenues	5	—	31
Total revenue	1,320	2,490	51,945
Operating expenses:			
Research and development	2,264	2,920	53,135
General and administrative	1,541	1,515	35,195
Total operating expenses	3,805	4,435	88,330
Operating loss	(2,485)	(1,945)	(36,385)
Non-cash loss on increase in fair value of warrants	(35)	—	(767)
Other income (expense), net	(5)	(31)	1,416
Loss before income taxes	(2,525)	(1,976)	(35,736)
Provision for income taxes	(6)	(12)	(79)
Net loss	(2,531)	(1,988)	(35,815)
Change in unrealized gains (losses) on available-for-sale securities	2	14	(42)
Total comprehensive loss	$(2,529)	$(1,974)	$ (35,857)
Net loss per share:			
Basic and diluted	$(0.09)	$(0.08)	
Shares used in per share calculations:			
Basic and diluted	28,572	23,428	

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

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

(in thousands)	Three Months Ended March 31, 2012	2011	Cumulative Period from July 1, 2002 (inception) to March 31, 2012
Cash flows from operating activities:			
Net loss	$(2,531)	$(1,988)	$(35,815)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	91	107	2,020
Accretion of discount on short-term investments	—	—	(252)
Net realized loss on sales of short-term investments	12	17	37
Loss on disposal of property and equipment	30	—	163
Stock-based compensation expense for options issued to employees and directors	342	293	5,086
Compensation expense for warrants issued for services	20	—	182
Stock-based compensation expense for options and stock issued to non-employees	127	130	1,126
Non-cash loss on increase in fair value of warrants	35	—	767
Taxes paid by LLC	—	—	1
Changes in operating assets and liabilities:			
(Increase) decrease in accounts receivable	(1,006)	500	(1,009)
(Increase) decrease in prepaid expenses and other assets	24	194	(351)
Increase in accounts payable and accrued liabilities	167	252	1,720
Increase (decrease) in deferred revenue	(47)	511	2,202
Net cash provided by (used in) operating activities	(2,736)	16	(24,123)
Cash flows from investing activities:			
Purchases of property and equipment	—	(117)	(3,213)
Proceeds from disposal of property and equipment	1	—	47
Purchases of short-term investments	(712)	(750)	(109,258)
Proceeds from maturities and sales of short-term investments	1,175	1,250	104,147
Cash acquired in purchase of LLC	—	—	516
Net cash provided by (used in) investing activities	464	383	(7,761)
Cash flows from financing activities:			
Proceeds from preferred stock issuances, net	—	—	11,160
Proceeds from common stock issuances	—	—	17
Proceeds from exercise of options and warrants	36	8	2,055
Proceeds from initial public offering, net of costs	—	—	17,077
Proceeds from (payment on) shelf offering, net of costs	—	(8)	6,575
Proceeds from stock subscription receivable	—	—	873
Proceeds from issuance of notes	—	—	405
Principal payments on capital lease	—	—	(157)

Proceeds from short-term borrowing	—	—	88
Principal payment on short-term borrowing	(71)	—	(88)
Proceeds from borrowings under equipment loan	—	—	1,216
Principal payments on equipment loan	—	(64)	(1,216)
Net cash provided by (used in) financing activities	(35)	(64)	38,005
Net increase (decrease) in cash and cash equivalents	(2,307)	335	6,121
Cash and cash equivalents, beginning of period	8,428	11,534	—
Cash and cash equivalents, end of period	$6,121	$11,869	$6,121

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

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

NOTE 1. ORGANIZATION

NovaBay Pharmaceuticals is a clinical-stage biotechnology company focused on addressing the large unmet therapeutic needs of the global anti-infective market with its two distinct categories of products.

Aganocide® Compounds
NovaBay's first-in-class Aganocide® compounds, led by NVC-422, are patented, synthetic molecules with a broad spectrum of activity against bacteria, viruses and fungi. Mimicking the mechanism of action that human white blood cells use against infections, Aganocides possess a reduced likelihood that bacteria or viruses will be able to develop resistance, which is critical for advanced anti-infectives. Having demonstrated therapeutic proof-of-concept in Phase 2 clinical studies, these compounds are well suited to treat and prevent a wide range of local, non-systemic infections. NovaBay is currently focused in three large therapeutic markets:

- Dermatology - Partnered with Galderma, a leading dermatology company, the companies are developing a gel formulation of NVC-422 for treating the highly contagious skin infection, impetigo. A Phase 2b clinical study is planned for 2012.

- Ophthalmology - NovaBay is developing an eye drop formulation of NVC-422 for treating viral conjunctivitis, for which there is currently no FDA-approved treatment. The Company expects to launch a global Phase 2b clinical study in this indication in the second quarter of 2012.

- Urology – NovaBay's irrigation solution containing NVC-422 is currently in Phase 2 clinical studies, with the goal of reducing the incidence of urinary catheter blockage and encrustation (UCBE) and the associated urinary tract infections. The Company reported positive data from Part A of this study and expects to announce top-line results from Part B of this study later in 2012.

NeutroPhase®
In addition to our Aganocide compounds, NovaBay is also developing NeutroPhase®, which is an FDA 510(k)-cleared product for wound care. NeutroPhase is a patented pure hypochlorous acid solution and has the potential to be well suited to treat the six-million-patients in the U.S. who suffer from chronic non-healing wounds, such as pressure, venous stasis and diabetic ulcers.

NovaBay has begun securing commercial partnerships for NeutroPhase. In January 2012, NovaBay announced it had entered into a strategic marketing agreement with Pioneer Pharma Co., Ltd., a Shanghai-based company that markets high-end pharmaceutical products into China. NovaBay expects to announce additional marketing agreements in select geographic markets around the world during 2012.

The Company was incorporated under the laws of the State of California on January 19, 2000 as NovaCal Pharmaceuticals, Inc. The Company had no operations until July 1, 2002, on which date it acquired all of the operating assets of NovaCal Pharmaceuticals, LLC, a California limited liability company. In February 2007, the Company changed its name from NovaCal Pharmaceuticals, Inc. to NovaBay Pharmaceuticals, Inc. In August 2007, two subsidiaries were formed—NovaBay Pharmaceuticals Canada, Inc., a wholly-owned subsidiary incorporated under the laws of British Columbia (Canada), which may conduct research and development in Canada, and DermaBay,

Inc., a wholly-owned U.S. subsidiary, which may explore and pursue dermatological opportunities. In June 2010, the Company changed the state in which it is incorporated (the Reincorporation), and is now incorporated under the laws of the State of Delaware. All references to "we," "us," "our," or "the Company" herein refer to the California corporation prior to the date of the Reincorporation, and to the Delaware corporation on and after the date of the Reincorporation. The Company currently operates in one business segment.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited consolidated financial statements of NovaBay Pharmaceuticals, Inc. have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") for interim reporting including the instructions to Form 10-Q and Rule 8-03 of Regulation S-X. These statements do not include all disclosures for annual audited financial statements required by accounting principles generally accepted in the United States of America ("U.S. GAAP") and should be read in conjunction with the Company's audited consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011. The consolidated balance sheet at December 31, 2011, has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by U.S. GAAP for complete financial statements.

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

The Company believes these consolidated financial statements reflect all adjustments (consisting only of normal, recurring adjustments) that are necessary for a fair presentation of the financial position and results of operations for the periods presented. Results of operations for the interim periods presented are not necessarily indicative of results to be expected for the year.

The financial statements have been prepared under the guidelines for Development Stage Entities. A development stage enterprise is one in which planned principal operations have not commenced, or if its operations have commenced, there have been no significant revenues therefrom. As of March 31, 2012, we continued to conduct clinical trials and had not commenced our planned principal operations.

Principles of Consolidation

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, NovaBay Pharmaceuticals Canada, Inc. and DermaBay, Inc. All inter-company accounts and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. These estimates include useful lives for property and equipment and related depreciation calculations, estimated amortization period for payments received from product development and license agreements as they relate to revenue recognition, assumptions for valuing options and warrants, and income taxes. Actual results could differ from those estimates.

Cash, Cash Equivalents and Short-Term Investments

The Company considers all highly liquid instruments with a stated maturity of three months or less at the date of purchase to be cash and cash equivalents. Cash and cash equivalents are stated at cost, which approximates their fair value. As of March 31, 2012, the Company’s cash and cash equivalents were held in financial institutions in the United States and include deposits in money market funds, which were unrestricted as to withdrawal or use.

The Company classifies all highly liquid investments with a stated maturity of greater than three months at the date of purchase as short-term investments. Short-term investments generally consist of United States government, municipal and corporate debt securities. The Company has classified its short-term investments as available-for-sale. The Company does not intend to hold securities with stated maturities greater than twelve months until maturity. In response to changes in the availability of and the yield on alternative investments as well as liquidity requirements, the Company occasionally sells these securities prior to their stated maturities. These securities are carried at fair value, with the unrealized gains and losses reported as a component of other comprehensive income (loss) until realized. Realized gains and losses from the sale of available-for-sale securities, if any, are determined on a specific identification basis. A decline in the market value below cost of any available-for-sale security that is determined to be other-than-temporary results in a revaluation of its carrying amount to fair value and an impairment charge to earnings, resulting in a new cost basis for the security. No such impairment charges were recorded for the periods presented. The interest income and realized gains and losses are included in other income (expense), net within the

consolidated statements of operations and comprehensive loss. Interest income is recognized when earned.

Concentrations of Credit Risk and Major Partners

Financial instruments which potentially subject us to significant concentrations of credit risk consist primarily of cash and cash equivalents and short-term investments. The Company maintains deposits of cash, cash equivalents and short-term investments with three highly-rated, major financial institutions in the United States.

Deposits in these banks may exceed the amount of federal insurance provided on such deposits. The Company has never experienced any losses related to these balances. All of its non-interest bearing cash balances were fully insured at March 31, 2012, due to a temporary federal program in effect from December 31, 2010 through December 31, 2012. Under the program, there is no limit to the amount of insurance coverage for eligible accounts. Beginning 2013, insurance coverage will revert to the $250,000 per depositor at each financial institution, and The Company's non-interest bearing cash balance may exceed federally insured limits. The Company does not believe it is exposed to significant credit risk due to the financial position of the financial institutions in which these deposits are held. Additionally, the Company has established guidelines regarding diversification and investment maturities, which are designed to maintain safety and liquidity.

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

During the quarters ended March 31, 2012 and 2011, the majority of the Company's operating revenues were derived from one and two collaborative partners, respectively. As of March 31, 2012 and December 31, 2011, the majority of the Company's accounts receivable was from one collaborative partner.

Comprehensive Loss

ASC 220, Comprehensive Income requires that an entity's change in equity or net assets during a period from transactions and other events from non-owner sources be reported. The Company reports unrealized gains and losses on its available-for-sale securities as other comprehensive income (loss).

Fair Value Measurement of Financial Assets and Liabilities

Financial instruments, including accounts payable and accrued liabilities, are carried at cost, which management believes approximates fair value due to the short-term nature of these instruments. The fair value of capital lease obligations and equipment loans approximates its carrying amounts as a market rate of interest is attached to their repayment.

The Company measures the fair value of financial assets and liabilities based on authoritative guidance which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Authoritative guidance has established a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

Level 1 – quoted prices in active markets for identical assets or liabilities
Level 2 – quoted prices for similar assets and liabilities in active markets or inputs that are observable
Level 3 – inputs that are unobservable (for example cash flow modeling inputs based on assumptions)

Property and Equipment

Property and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation is calculated using the straight-line method over the estimated useful lives of the related assets of five to seven years for office and laboratory equipment, three years for software and seven years for furniture and fixtures. Leasehold improvements are amortized over the shorter of their useful life or the term of the lease. Amortization of assets recorded under capital leases is included in depreciation expense.

Impairment of Long-Lived Assets

The Company accounts for long-lived assets by considering whether events or changes in facts and circumstances, both internally and externally, may indicate that an impairment of long-lived assets held for use are present. Management periodically evaluates the carrying value of long-lived assets and has determined that there was

no impairment as of all periods presented. Should there be impairment in the future; the Company would recognize the amount of the impairment based on the discounted expected future cash flows from the impaired assets. The cash flow estimates would be based on management's best estimates, using appropriate and customary assumptions and projections at the time.

Common Stock Warrant Liabilities

The Company generally accounts for warrants issued in connection with equity financings as a component of equity, unless there is a deemed possibility that the Company may have to settle the warrants in cash. For the warrants issued with deemed possibility of cash settlement, the Company records the fair value of the issued warrants as a liability at each balance sheet date and records changes in the estimated fair value as a non-cash gain or loss in the consolidated statement of operations and comprehensive loss.

Revenue Recognition

License and collaboration revenue is primarily generated through agreements with strategic partners for the development and commercialization of the Company's product candidates. The terms of the agreements typically include non-refundable upfront fees, funding of research and development activities, payments based upon achievement of certain milestones and royalties on net product sales. In accordance with revenue recognition criteria under U.S. GAAP, the Company analyzes its multiple element arrangements to determine whether the elements can be separated. The Company performs its analysis at the inception of the arrangement and as each product or service is delivered. If a product or service is not separable, the combined deliverables are accounted for as a single unit of accounting and revenue is recognized over the performance obligation period. Revenue is recognized when the following criteria have been met: persuasive evidence of an arrangement exists; delivery has occurred and risk of loss has passed; the seller's price to the buyer is fixed or determinable; and collectability is reasonably assured.

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Assuming the elements meet the revenue recognition guidelines the revenue recognition methodology prescribed for each unit of accounting is summarized below:

Upfront Fees—The Company defers recognition of non-refundable upfront fees if it has continuing performance obligations without which the technology licensed has no utility to the licensee. If the Company has performance obligations through research and development services that are required because its know-how and expertise related to the technology is proprietary to it, or can only be performed by it, then such up-front fees are deferred and recognized over the period of the performance obligations. The Company bases the estimate of the period of performance on factors in the contract. Actual time frames could vary and could result in material changes to our results of operations.

Funded Research and Development— Revenue from research and development services is recognized during the period in which the services are performed and is based upon the number of full-time-equivalent personnel working on the specific project at the agreed-upon rate. This revenue approximates the cost incurred. Reimbursements from collaborative partners for agreed-upon direct costs including direct materials and outsourced, or subcontracted, pre-clinical studies are classified as revenue and recognized in the period the reimbursable expenses are incurred. Payments received in advance are recorded as deferred revenue until the research and development services are performed or costs are incurred.

Milestones—Substantive milestone payments are considered to be performance bonuses that are recognized upon achievement of the milestone only if all of the following conditions are met: the milestone payments are non-refundable; achievement of the milestone involves a degree of risk and was not reasonably assured at the inception of the arrangement; substantive effort is involved in achieving the milestone; the amount of the milestone is reasonable in relation to the effort expended or the risk associated with achievement of the milestone; and a reasonable amount of time passes between the up-front license payment and the first milestone payment as well as between each subsequent milestone payment. If any of these conditions are not met, the milestone payments are deferred and recognized as revenue over the term of the arrangement as the Company completes the performance obligations.

Royalties—The Company recognizes royalty revenues from licensed products upon the sale of the related products.

Research and Development Costs

The Company expenses research and development costs as incurred. These costs include salaries and benefits for research and development personnel, costs associated with clinical trials managed by contract research organizations, and other costs associated with research, development and regulatory activities. The Company uses external service providers to conduct clinical trials, to manufacture supplies of product candidates and to provide various other research and development-related products and services. Research and development expenses under the collaborative agreements approximate the revenue recognized, excluding milestone and upfront payments received under such arrangements.

Patent Costs

The Company expenses patent costs, including legal expenses, in the period in which they are incurred. Patent expenses are included in general and administrative expenses in our statements of operations and comprehensive loss.

Stock-Based Compensation

The Company accounts for stock-based compensation under the provisions of ASC 718, Compensation-Stock Compensation. Under the fair value recognition provisions, stock-based compensation expense is measured at the grant date for all stock-based awards to employees and directors and is recognized as expense over the requisite service period, which is generally the vesting period. Non-employee stock-based compensation charges are amortized over the vesting period on a straight-line basis. For stock options granted, the fair value of the stock options is estimated using a Black-Scholes-Merton valuation model. See Note 8 for further information regarding stock-based compensation expense and the assumptions used in estimating that expense.

NOVABAY PHARMACEUTICALS, INC.
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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

Income Taxes

The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. A valuation allowance is recognized if it is more likely than not that some portion or all of the deferred tax assets will not be recognized.

Common Stock Warrant Liabilities

For warrants where there is a deemed possibility that the Company may have to settle the warrants in cash, the Company records the fair value of the issued warrants as a liability at each balance sheet date and records changes in the estimated fair value as a non-cash gain or loss in the consolidated statement of operations and comprehensive loss. The fair values of these warrants have been determined using the Binomial Lattice (“Lattice”) valuation model, and the changes in the fair value are recorded in the consolidated statement of operations and comprehensive loss. The Lattice model provides for assumptions regarding volatility, call and put features and risk-free interest rates within the total period to maturity. These values are subject to a significant degree of judgment on the part of the Company.

Net Loss per Share

Basic net loss per share is computed by dividing net loss available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted net loss per share gives effect to all dilutive potential common shares outstanding during the period including stock options and stock warrants, using the treasury stock method, using the if-converted method. Potentially dilutive common share equivalents are excluded from the diluted net loss per share computation since their effect would be anti-dilutive. The following table sets forth the reconciliation between basic net loss per share and diluted net loss per share:

	Three Months Ended March 31,	
(in thousands, except per share amounts)	2012	2011
Net loss	$ (2,531)	$ (1,988)
Basic shares	28,572	23,428
Add: shares issued upon assumed exercise of stock options	—	—
Diluted shares	28,572	23,428
Basic and diluted net loss per share	$ (0.09)	$ (0.08)

The following outstanding stock options and stock warrants were excluded from the diluted net loss per share computation as their effect would have been anti-dilutive:

	Three Months Ended March 31,	
(In thousands)	2012	2011
Stock options	5,958	5,137
Stock warrants	4,923	1,375
	10,881	6,512

Recent Accounting Pronouncements

There have been no recent accounting pronouncement or changes in accounting pronouncements during the three months ended March 31, 2012, as compared to the recent accounting pronouncements described in the Company's Form 10-K for the year ended December 31, 2011, that are of significance, or potential significance to the Company.

NOTE 3. INVESTMENTS

Short-term investments at March 31, 2012 and December 31, 2011 consisted of the following:

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

	March 31, 2012			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Market Value
Corporate bonds	$ 2,624	$ —	$ (42)	$ 2,582
Certificates of Deposit	$ 2,650	$ —	$ —	$ 2,650
	$ 5,274	$ —	$ (42)	$ 5,232

	December 31, 2011			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Market Value
Corporate bonds	$ 3,054	$ —	$ (42)	$ 3,012
Certificates of deposit	2,700	—	(2)	2,698
	$ 5,754	$ —	$ (44)	$ 5,710

All short-term investments at March 31, 2012 and December 31, 2011 mature in less than one year. Unrealized holding gains and losses classified as available-for-sale are recorded in accumulated other comprehensive loss.

The Company recognized realized losses of $12,000 and $17,000, for the three months ended March 31, 2012 and 2011, respectively.

NOTE 4. FAIR VALUE MEASUREMENTS

The Company’s cash equivalents and investments are classified within Level 1 or Level 2 of the fair value hierarchy because they are valued using quoted market prices in active markets, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. The types of investments that are generally classified within Level 1 of the fair value hierarchy include money market securities. The types of investments that are generally classified within Level 2 of the fair value hierarchy include corporate securities and certificates of deposits.

The Company’s warrant liabilities are classified within level 3 of the fair value hierarchy because the value is calculated using significant judgment based on our own assumptions in the valuation of these liabilities.

The following table presents the Company’s assets and liabilities measured at fair value on a recurring basis as of March 31, 2012:

NOVABAY PHARMACEUTICALS, INC.
(a development stage company)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(in thousands)	Balance at March 31, 2012	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Assets				
Cash equivalents	$ 6,121	$ 6,121	$ —	$ —
Short-term investments:				