
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

Form 10-Q

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended March 31, 2017

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF SECURITIES EXCHANGE ACT OF 1934
For the transition period from ____ to ____

Commission file number 001-37809

Gemphire Therapeutics Inc.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

47-2389984
(IRS Employer Identification No.)

17199 N. Laurel Park Drive, Suite 401, Livonia, MI
(Address of principal executive offices)

48152
(Zip Code)

(248) 681-9815
(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a smaller reporting company)

Smaller reporting company

Emerging growth company

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12(b)-2 of the Securities Exchange Act of 1934). Yes No

The number of outstanding shares of the registrant's common stock, \$0.001 par value, as of May 1, 2017 was 10,600,045.

Gemphire Therapeutics Inc.
FORM 10-Q
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PART I – FINANCIAL INFORMATION
ITEM 1 – FINANCIAL STATEMENTS**Gemphire Therapeutics Inc.**
Condensed Balance Sheets
(in thousands, except share amounts and par value)

	<u>March 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
	<u>(unaudited)</u>	
Assets		
Current assets:		
Cash and cash equivalents	\$ 29,282	\$ 24,033
Prepaid expenses	552	713
Total current assets	<u>29,834</u>	<u>24,746</u>
Deposits	8	8
Total assets	<u>\$ 29,842</u>	<u>\$ 24,754</u>
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 3,541	\$ 2,008
Accrued liabilities	1,002	2,113
Total current liabilities	4,543	4,121
Other liabilities	2	1
Total liabilities	<u>4,545</u>	<u>4,122</u>
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized as of March 31, 2017 and December 31, 2016, no shares issued or outstanding as of March 31, 2017 and December 31, 2016.	—	—
Common stock, \$0.001 par value; 100,000,000 shares authorized as of March 31, 2017 and December 31, 2016, 10,596,838 and 9,270,255 shares issued and outstanding at March 31, 2017 and December 31, 2016, respectively.	18	17
Additional paid-in capital	59,834	47,674
Accumulated deficit	<u>(34,555)</u>	<u>(27,059)</u>
Total stockholders' equity	<u>25,297</u>	<u>20,632</u>
Total liabilities and stockholders' equity	<u>\$ 29,842</u>	<u>\$ 24,754</u>

See accompanying notes to condensed financial statements.

Gemphire Therapeutics Inc.
Condensed Statements of Comprehensive Loss
(in thousands, except share and per share amounts)
(unaudited)

	For the Three Months Ended	
	March 31,	
	2017	2016
Operating expenses:		
General and administrative	\$ 2,223	\$ 1,050
Research and development	5,280	1,176
Total operating expenses	<u>7,503</u>	<u>2,226</u>
Loss from operations	(7,503)	(2,226)
Interest income	12	127
Other expense	(5)	(4)
Loss before income taxes	<u>(7,496)</u>	<u>(2,103)</u>
Provision (benefit) for income taxes	—	—
Net loss	<u>(7,496)</u>	<u>(2,103)</u>
Other comprehensive loss, net of tax	—	—
Comprehensive loss	<u>\$ (7,496)</u>	<u>\$ (2,103)</u>
Net loss	\$ (7,496)	\$ (2,103)
Adjustment to redemption value on Series A convertible preferred stock	—	(149)
Net loss attributable to common stockholders	<u>\$ (7,496)</u>	<u>\$ (2,252)</u>
Net loss per share:		
Basic and diluted (Note 10)	<u>\$ (0.79)</u>	<u>\$ (0.65)</u>
Number of shares used in per share calculations:		
Basic and diluted	<u>9,521,224</u>	<u>3,468,764</u>

See accompanying notes to condensed financial statements.

Gemphire Therapeutics Inc.
Condensed Statements of Changes in Convertible Preferred Stock and Stockholders' Equity (Deficit)
(in thousands, except share amounts)
(unaudited)

	Series A Convertible Preferred Stock		Common Stock		Additional Paid-In Capital	Accumulated Deficit	Total Equity (Deficit)
	Shares	Amount	Shares	Amount			
Balance at January 1, 2016	745,637	\$ 7,953	3,758,488	\$ 12	\$ —	\$ (12,392)	\$ (12,380)
Redemption value adjustment — Series A preferred stock	—	149	—	—	(123)	(26)	(149)
Share-based compensation — employee	—	—	—	—	46	—	46
Share-based compensation — non-employee	—	—	—	—	77	—	77
Net loss	—	—	—	—	—	(2,103)	(2,103)
Balance at March 31, 2016	<u>745,637</u>	<u>\$ 8,102</u>	<u>3,758,488</u>	<u>\$ 12</u>	<u>\$ —</u>	<u>\$ (14,521)</u>	<u>\$ (14,509)</u>
Balance at January 1, 2017	—	\$ —	9,270,255	\$ 17	\$ 47,674	\$ (27,059)	\$ 20,632
Issuance of common stock from private placement offering	—	—	1,324,256	1	8,978	—	8,979
Issuance of detachable stock warrants in connection with private placement offering	—	—	—	—	3,562	—	3,562
Issuance costs of private placement offering	—	—	—	—	(1,219)	—	(1,219)
Exercise of stock options	—	—	2,327	—	3	—	3
Share-based compensation — employee	—	—	—	—	829	—	829
Share-based compensation — non-employee	—	—	—	—	7	—	7
Net loss	—	—	—	—	—	(7,496)	(7,496)
Balance at March 31, 2017	<u>—</u>	<u>\$ —</u>	<u>10,596,838</u>	<u>\$ 18</u>	<u>\$ 59,834</u>	<u>\$ (34,555)</u>	<u>\$ 25,297</u>

See accompanying notes to condensed financial statements.

Gemphire Therapeutics Inc.
Condensed Statements of Cash Flows
(in thousands)
(unaudited)

	For the Three Months Ended March 31,	
	2017	2016
Operating activities		
Net loss	\$ (7,496)	\$ (2,103)
Adjustments to reconcile net loss to net cash used in operating activities:		
Share-based compensation	836	123
Non-cash interest on convertible notes to related parties	—	31
Non-cash interest on convertible notes	—	78
Non-cash discount amortization on convertible notes to related parties	—	(55)
Non-cash discount amortization on convertible notes	—	(159)
Revaluation of premium conversion derivative	—	(22)
Change in assets and liabilities:		
Prepaid expenses and other assets	161	(1)
Accounts payable	1,473	(242)
Accrued and other liabilities	(1,197)	294
Net cash used in operating activities	<u>(6,223)</u>	<u>(2,056)</u>
Investing activities		
Net cash provided by (used in) investing activities	<u>—</u>	<u>—</u>
Financing activities		
Proceeds from issuance of convertible notes	—	50
Proceeds from issuance of convertible notes to related parties	—	101
Exercise of stock options	3	—
Proceeds from offering	12,541	—
Offering costs	(1,072)	(86)
Net cash provided by financing activities	<u>11,472</u>	<u>65</u>
Net increase (decrease) in cash and cash equivalents	5,249	(1,991)
Cash and cash equivalents at beginning of period	24,033	3,620
Cash and cash equivalents at end of period	<u>\$ 29,282</u>	<u>\$ 1,629</u>
<i>Supplemental disclosure of cash flow information:</i>		
Cash paid for income taxes	<u>\$ —</u>	<u>\$ —</u>
Cash paid for interest	<u>\$ —</u>	<u>\$ —</u>
<i>Supplemental non-cash financing transactions:</i>		
Redemption value change of Series A preferred stock	<u>\$ —</u>	<u>\$ 149</u>
Bifurcation of premium conversion derivative related to convertible notes	<u>\$ —</u>	<u>\$ 9</u>
Offering costs in accounts payable and accrued liabilities	<u>\$ 147</u>	<u>\$ 46</u>

See accompanying notes to condensed financial statements.

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited)

1. The Company and Basis of Presentation

On November 10, 2008, Michigan Life Therapeutics, LLC (MLT) was organized as a limited liability company (LLC) in Michigan. On October 30, 2014, Gemphire Therapeutics Inc. (Gemphire or the Company) was incorporated as a C corporation in the state of Delaware. On November 1, 2014, MLT entered into a merger agreement with Gemphire whereby MLT was merged with and into Gemphire with Gemphire as the surviving entity; all outstanding membership interests of MLT were exchanged for shares of Gemphire's common stock. The purpose of the merger was to change the jurisdiction of MLT from Michigan to Delaware and to convert from an LLC to a corporation. The Company's headquarters are located in Livonia, Michigan.

The Company is a clinical-stage biopharmaceutical entity focused on developing and commercializing therapies for the treatment of dyslipidemia, a serious medical condition that increases the risk of life threatening cardiovascular disease, and NAFLD/NASH (nonalcoholic fatty liver disease). The Company's primary activities have been conducting research and development activities, planning clinical trials, performing business and financial planning, recruiting personnel and raising capital. The Company is subject to certain risks, which include the need to research, develop, and clinically test potentially therapeutic products, initially one product candidate gemcabene (also known as CI-1027); obtain regulatory approval for its products and commercialize them around the world; expand its management scientific staff; finance its operations; and, find collaboration partners to further advance development and commercial efforts.

Initial Public Offering

On August 4, 2016, the Company's Registration Statement on Form S-1 (File No 333-210815) relating to its initial public offering (IPO) of its common stock was declared effective by the Securities and Exchange Commission (SEC). Pursuant to such Registration Statement, on August 10, 2016, the Company closed its IPO whereby 3,000,000 shares of its common stock were issued and sold at a public offering price of \$10.00 per share. On September 8, 2016, the Company closed the sale of 27,755 shares of its common stock at the public offering price of \$10.00 per share, representing a partial exercise of the underwriters' over-allotment option, following which, the IPO terminated. The Company received net proceeds of approximately \$26.1 million after deducting underwriting discounts and commissions of \$2.1 million and other offering expenses of \$2.1 million.

Immediately prior to the IPO, the Company amended and restated its certificate of incorporation and bylaws to, among other things, change its authorized capital stock to consist of (i) 100,000,000 shares of common stock and (ii) 10,000,000 shares of undesignated preferred stock. Both the common stock and the preferred stock have a par value of \$0.001 per share.

Private Placement Offering

On March 10, 2017, the Company entered into a securities purchase agreement for a private placement (the Private Placement) with a select group of accredited investors whereby, on March 15, 2017 the Company issued and sold 1,324,256 units at a price of \$9.47 per unit for gross proceeds of approximately \$12.5 million. Each unit consists of one share of the Company's common stock and a warrant to purchase 0.75 shares of common stock. The warrants have an exercise price of \$10.40 per share and are exercisable for a period of five years from the date of issuance. The resale of the shares of common stock issued in the Private Placement and the shares of common stock to be issued upon exercise of the warrants issued in the Private Placement was subsequently registered in April 2017 under the Securities Act of 1933, as amended.

Basis of Presentation

The accompanying condensed financial statements have been prepared by the Company, without audit, pursuant to the rules and regulations of the SEC. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to such rules and regulations. The condensed financial statements may not include all disclosures required by U.S. GAAP; however, the Company believes that the disclosures are adequate to make the information presented not misleading. These unaudited condensed financial statements should be read in conjunction with the audited financial

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited) - continued

statements and the notes thereto for the fiscal year ended December 31, 2016 included in the Company's Annual Report on Form 10-K filed with the SEC on March 21, 2017. The condensed balance sheet at December 31, 2016 was derived from the audited financial statements.

In the opinion of management, all adjustments, consisting of only normal recurring adjustments that are necessary to present fairly the financial position, results of operations, and cash flows for the interim periods, have been made. The results of operations for the interim periods are not necessarily indicative of the operating results for the full fiscal year or any future periods.

Reverse Stock Split

In April 2016, the board of directors approved an amendment to the Company's certificate of incorporation to effect a 1-for-3.119 reverse stock split (the Reverse Stock Split) for all common and Series A preferred stock. The Reverse Stock Split became effective on April 27, 2016 upon the filing of the amendment to the certificate of incorporation. The authorized shares and par value of the common stock and Series A preferred stock were not adjusted as a result of the Reverse Stock Split. All issued and outstanding common and Series A preferred stock, options for common stock and per share amounts contained in the financial statements have been retroactively adjusted to reflect this Reverse Stock Split for all periods presented.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of condensed financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the condensed financial statements and accompanying notes. Actual results could differ from those estimates.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of 90 days or less at the time of deposit to be cash equivalents. The Company invests excess cash in readily available checking and savings accounts and highly liquid investments in money market accounts.

Fair Value of Financial Instruments

The Company's condensed financial instruments include principally cash and cash equivalents, other current assets, accounts payable, accrued liabilities and debt. The carrying amounts for these condensed financial instruments reported in the balance sheets approximate their fair values. See Note 11 — Fair Value Measurements, for further discussion of fair value.

General and Administrative Expenses

General and administrative expenses consist primarily of personnel-related costs, including salaries and share-based compensation costs, for personnel in functions not directly associated with research and development activities. Other significant costs include legal fees related to intellectual property and corporate matters and professional fees for accounting and other services.

Research and Development Expenses

Research and development expenses consist of costs incurred in performing research and development activities, including compensation for research and development employees, costs associated with preclinical studies and trials, regulatory activities, manufacturing activities to support clinical activities, license fees, non-legal patent costs, fees paid to external service providers that conduct certain research and development, clinical costs and an allocation of overhead expenses. Research and development costs are expensed as incurred.

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited) - continued

Income Taxes

The Company utilizes the liability method of accounting for income taxes as required by Accounting Standards Codification (ASC) 740, *Income Taxes*. Under this method, deferred tax assets and liabilities are determined based on differences between financial reporting and the tax basis of assets and liabilities and are measured using enacted tax rates and laws that will be in effect when the differences are expected to reverse. Currently, there is no provision for income taxes, as the Company has incurred operating losses to date, and a full valuation allowance has been provided on the net deferred tax assets. MLT was treated as a partnership for federal and state income tax purposes. Accordingly, no provision was made for income taxes for periods prior to November 1, 2014, since the Company's net loss (subject to certain limitations) was passed through to the income tax returns of its members. Upon incorporation on October 30, 2014, the Company became taxed as a corporation.

Share-Based Compensation

The Company accounts for share-based compensation in accordance with the provisions of ASC 718, *Compensation — Stock Compensation* (ASC 718). Accordingly, compensation costs related to equity instruments granted are recognized at the grant-date fair value. Additionally, as a result of the early adoption of ASU 2016-09, *Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*, the Company has made an accounting policy election to record forfeitures when they occur. Share-based compensation arrangements to non-employees are accounted for in accordance with the applicable provisions of ASC 718 and ASC 505, *Equity*, using a fair value approach. The compensation costs of these arrangements are subject to re-measurement as the equity instruments vest and are recognized as expense over the related service period (typically the vesting period of the awards).

Common Stock Valuation

Due to the absence of an active market for the Company's common stock prior to the close of the IPO, the Company utilized methodologies in accordance with the framework of the American Institute of Certified Public Accountants' Technical Practice Aid, *Valuation of Privately-Held Company Equity Securities Issued as Compensation*, to estimate the fair value of its common stock. The valuation methodology includes estimates and assumptions that require the Company's judgment. These estimates and assumptions included a number of objective and subjective factors, including external market conditions affecting the biopharmaceutical industry sector, and the likelihood of achieving a liquidity event, such as an IPO or sale. Significant changes to the key assumptions used in the valuations have resulted in different fair values of common stock at each valuation date.

Convertible Preferred Stock

On March 31, 2015, the Company issued 745,637 shares of Series A convertible preferred stock (the Series A preferred stock). On August 10, 2016, immediately prior to the closing of the IPO, the Company's Series A preferred stock, together with accrued dividends thereon, converted into 827,205 shares of common stock. The Series A preferred stock prior to conversion was classified outside of permanent equity, in mezzanine equity, on the Company's condensed balance sheet. The Company initially recorded preferred stock that may be redeemed at the option of the holder, or based on the occurrence of events outside of the Company's control, at the value of the proceeds received. Subsequently, if it was probable that the preferred stock would become redeemable, the Company recognized changes in the redemption value immediately as they occurred and adjusted the carrying amount of the instrument to equal the redemption value at the end of each reporting period. If it was not probable that the preferred stock would become redeemable, the Company did not adjust the carrying value. In the absence of retained earnings, these charges were recorded against additional paid-in-capital, if any, and then to accumulated deficit. See Note 7 — *Convertible Series A Preferred Stock* for further discussion. As a result of their conversion to common stock on August 10, 2016 as described above, no shares of Series A preferred stock were outstanding as of March 31, 2017 and December 31, 2016.

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited) - continued

Segment Information

Operating segments are components of an enterprise for which separate financial information is available and is evaluated regularly by the Company's chief operating decision maker in deciding how to allocate resources and assessing performance. The Company's chief operating decision maker is its Chief Executive Officer. The Company's Chief Executive Officer views the Company's operations and manages its business in one operating segment, which is the business of development and commercialization of therapeutics for the treatment of dyslipidemia, a serious medical condition that increases the risk of life threatening cardiovascular disease and NAFLD/NASH. Accordingly, the Company has a single reporting segment.

Jumpstart Our Business Startups Act Accounting Election

As an emerging growth company under the Jumpstart Our Business Startups Act (JOBS Act), the Company is eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies. The Company has irrevocably elected not to avail itself of this exemption and, therefore, will be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

Recent Accounting Pronouncements

In January 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-01, *Financial Instruments — Overall: Recognition and Measurement of Financial Assets and Financial Liabilities*. The guidance affects the accounting for equity investments, financial liabilities under the fair value option and the presentation and disclosure requirements of financial instruments. The guidance is effective in the first quarter of fiscal 2019. Early adoption is permitted for the accounting guidance on financial liabilities under the fair value option. The Company is currently evaluating the impact of the new guidance on its financial statements.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)* and subsequently amended the guidance relating largely to transition considerations under the standard in January 2017. The objective of this update is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. This ASU is effective for fiscal years beginning after December 15, 2018, including interim periods within those annual periods and is to be applied utilizing a modified retrospective approach. The Company is currently evaluating the new guidance to determine the impact it may have on its financial statements.

In March 2016, the FASB issued ASU 2016-09, *Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. This ASU simplifies the accounting for share-based payment award transactions including: income tax consequences, classification of awards as either equity or liabilities and classification on the statement of cash flows. This ASU is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted. The Company adopted this standard effective July 1, 2016 on a retrospective basis for each period presented. The adoption of this standard did not have a material impact on the Company's financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash*. The objective of this ASU is to eliminate the diversity in practice related to the classification of restricted cash or restricted cash equivalents in the statement of cash flows. For public business entities, this ASU is effective for annual and interim reporting periods beginning after December 15, 2017, with early adoption permitted. The amendments in this update should be applied retrospectively to all periods presented. The Company is currently evaluating the requirements of this new guidance and has not yet determined its impact on the Company's financial statements.

In January 2017, the FASB issued several amendments to ASU 2014-09, *Revenue from Contracts with Customers — Topic 606* (ASU 2014-09), including clarification on accounting for principal versus agent considerations (i.e., reporting gross versus net), licenses of intellectual property and identifying performance obligations. These amendments do not change the core principle of the standard, but provide clarity and implementation guidance. ASU 2014-09, which supersedes the revenue recognition requirements in FASB ASC 605, primarily states that an entity should recognize

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited) - continued

revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. In 2015, the FASB agreed to allow companies to delay the implementation of this standard for one year effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. Early application is permitted only for periods beginning after December 15, 2016. The Company plans to adopt this standard on January 1, 2018 and to select the modified retrospective transition method. The Company plans to modify its accounting policies to reflect the requirements of this standard however, the planned adoption will not affect the Company's financial statements and related disclosures for these periods or future periods until the Company generates revenues.

3. Accrued Liabilities

Accrued liabilities consist of the following (in thousands):

	As of March 31, 2017	As of December 31, 2016
Accrued offering costs	\$ 60	\$ —
Legal costs	166	54
Accrued compensation costs	303	706
Other research and development expenses	339	1,259
Other general and administrative expenses	134	94
Total	<u>\$ 1,002</u>	<u>\$ 2,113</u>

4. Debt

Interim Notes

On July 31, 2015, the Company entered into a convertible interim note financing (collectively with the notes issued in December 2015, February 2016 and April 2016, the Interim Notes), pursuant to which certain investors agreed to loan the Company approximately \$2.8 million. On August 10, 2016, immediately prior to the closing of the IPO, the Company's Interim Notes, together with accrued interest thereon, converted into 1,656,807 shares of common stock.

The Interim Notes accrued interest at a rate of 8% per annum, compounded annually, and would automatically convert into shares issued to investors in the Company's next equity financing round that results in gross proceeds of at least \$5.0 million (a Qualified Financing). The conversion would be equal to unpaid principal at 115% plus any unpaid accrued interest. The investors would be paid out principal at 200% if a change of control occurred before the next financing round. In the event that a Qualified Financing, change of control, or an IPO did not occur before July 31, 2016, the parties would then negotiate a price for conversion into a new round of stock.

In December 2015, the Company amended the Interim Notes and certain investors agreed to loan the Company an additional \$2.7 million for a revised financing total of \$5.5 million. The Interim Notes continued to accrue interest at an 8% rate per annum compounded annually, but were amended to automatically convert into shares of the same class of the Company's next convertible preferred stock financing round (the Preferred Stock Financing). The conversion into shares issued in the Preferred Stock Financing would be equal to unpaid principal at 115% plus unpaid accrued interest. In the event that either a change of control occurred or the Company completed a public transaction which resulted in the Company's stockholders holding securities listed on a national securities exchange, including an IPO, before the Preferred Stock Financing, the Interim Notes, as amended, would automatically convert into shares of the Company's common stock at a conversion price of \$6.70585 per share (which represents the original issue price of the Series A preferred stock) based on 100% of outstanding principal and unpaid accrued interest. Lastly, if a Preferred Stock Financing, change of control, or public transaction did not occur before December 31, 2016, the parties agreed to then negotiate a conversion price into a new round of stock.

In February 2016, certain investors agreed to loan the Company an additional \$0.2 million for a revised financing total of \$5.6 million. The Interim Notes continued to accrue interest at an 8% rate per annum compounded annually, but were amended to automatically convert into shares of the same class of the Company's next Preferred Stock Financing. The conversion into shares issued in the Preferred Stock Financing would be equal to unpaid principal at 115% plus unpaid

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited) - continued

accrued interest. In the event that either a change of control occurred or the Company completed a public transaction which resulted in the Company's stockholders holding securities listed on a national securities exchange, including an IPO, before the Preferred Stock Financing, the Interim Notes, as amended, would automatically convert into shares of the Company's common stock at a conversion price of \$6.70585 per share (which represents the original issue price of the Series A preferred stock as adjusted for the Reverse Stock Split (as defined below)) based on 100% of outstanding principal and unpaid accrued interest. Lastly, if a Preferred Stock Financing, change of control, or public transaction did not occur before December 31, 2016, the parties agreed to then negotiate a conversion price into a new round of stock.

In April 2016, the Company amended the Interim Notes and certain investors agreed to loan the Company an additional \$5.0 million for a revised financing total, including Interim Notes previously issued, of \$10.6 million. The Interim Notes continued to accrue interest at an 8% rate per annum compounded annually, but were amended so that 125% of the unpaid principal and accrued interest, would automatically convert into shares of the same class of the Company's next convertible preferred stock financing round of at least \$5.0 million (the Qualified Financing). In the event that either a change of control occurred or the Company completed a public transaction which resulted in the Company's stockholders holding securities listed on a national securities exchange, including an IPO, before the Qualified Financing, 100% of outstanding principal and unpaid accrued interest on the Interim Notes, as amended, would automatically convert into shares of the Company's common stock at a conversion price of \$6.70585 per share, as adjusted for the Reverse Stock Split. Lastly, if a Qualified Financing, change of control, or public transaction did not occur, the Interim Notes would become payable on demand any time after December 31, 2016. The Company incurred issuance costs related to the April 2016 financing in the amount of \$10,000. The Interim Notes were discounted for the issuance costs, and the discount was amortized to interest expense over their remaining term using the straight-line method.

On August 10, 2016, immediately prior to the closing of the IPO, the Company's Interim Notes, together with accrued interest thereon, converted into 1,656,807 shares of common stock. At the time of their issuance, the Interim Notes contained a conversion premium with regard to the conversion into shares at the time of the next Qualified Financing. The Company determined that the redemption feature under the Interim Notes qualified as an embedded derivative and was separated from its debt host. The bifurcation of the embedded derivative from its debt host resulted in a discount to the Interim Notes. The discount was amortized to interest expense over the term of the Interim Notes using the straight-line method. The embedded derivative was accounted for separately on a fair market value basis. As a result of the conversion of the Interim Notes, together with accrued interest thereon, into common stock immediately prior to the closing of the IPO, there was no premium conversion derivative outstanding as of March 31, 2017 and December 31, 2016. The Company recorded the fair value changes of the premium conversion derivative associated with the Interim Notes to interest income (expense) that amounted to zero and \$(22,000) for the three months ended March 31, 2017 and 2016, respectively.

As a result of their conversion to common stock on August 10, 2016 as described above, there were no Interim Notes outstanding as of March 31, 2017 and December 31, 2016.

5. Commitments and Contingencies

Pfizer License Agreement

In April 2011, the Company and Pfizer Inc. (Pfizer) entered into an exclusive license agreement (the Pfizer Agreement) for the clinical product candidate gemcabene. In exchange for this worldwide exclusive right and license to certain patent rights to make, use, sell, offer for sale and import the clinical product gemcabene, the Company agreed to certain milestone and royalty payments on future sales (See Note 6 — *License Agreement*). As of March 31, 2017, there was sufficient uncertainty with regard to both the outcome of the clinical trials and the ability to obtain sufficient funding to support any of the cash milestone payments under the license agreement, and as such, no liabilities were recorded related to the license agreement.

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Notes to Condensed Financial Statements (unaudited) - continued

Series A Preferred Stock Dividends

Holders of the Series A preferred stock were entitled to cumulative accruing dividends at a simple rate of 8% per year on the original issue price of the preferred stock of \$6.70585 per share, as adjusted for the Reverse Stock Split. The dividends effectively accrued daily on each share of preferred stock. The dividends were payable upon the earliest to occur of (1) the date determined by the Board, (2) the liquidation of the Company (including a deemed liquidation event) or (3) the conversion or redemption of at least a majority of the outstanding shares of Series A preferred stock. If the board reasonably believed that the Company was not legally able to pay the dividends in cash at the payment date, or if elected by the majority of the Series A preferred stockholders or if issued in connection with an IPO, the dividends were to be paid in shares of common stock at the conversion price for the Series A preferred stock in effect at that time, which was the original issue price of the Series A preferred stock as adjusted from time to time for any stock dividends, combinations, splits or recapitalizations. On August 10, 2016, immediately prior to the closing of the IPO, the Company's Series A preferred stock, together with accrued dividends thereon, converted into 827,205 shares of common stock, and as such, there were no cumulative unpaid dividends for the Series A preferred stock as of March 31, 2017 and December 31, 2016.

Other Agreements

Both cancellable and non-cancellable facility agreements were in place that provided for fixed monthly rent for the quarters ended March 31, 2017 and 2016. The total rent expense was \$26,000 and \$8,000 for the three months ended March 31, 2017 and 2016, respectively. In May 2016, the Company entered into a new lease agreement for its headquarters location, commencing in August 2016. The initial term of the agreement is 3 years with an initial monthly base rent of approximately \$8,400. In conjunction with entering into the new lease agreement for its headquarters location, the Company cancelled its original Northville, Michigan lease agreement, as amended, effective August 31, 2016 and renegotiated a new cancellable lease agreement for limited use of office space in the Northville location that expires in September 2017.

6. License Agreement

In April 2011, the Company entered into the Pfizer Agreement for a worldwide exclusive license to certain patent rights to make, use, sell, offer for sale and import the clinical product candidate gemcabene. In exchange for this license, the Company agreed to issue shares of its common stock to Pfizer representing 15% of the Company's fully diluted capital at the close of its first arms-length Series A financing, which occurred on March 31, 2015.

The Company agreed to make milestone payments totaling up to \$37 million upon the achievement of certain milestones, including the first regulatory submission in any country, regulatory approval in each of the United States, Europe and Japan, the first anniversary of the first regulatory approval in any country, and upon achieving certain aggregate sales levels of gemcabene or any product containing gemcabene. Future milestone payments under the Pfizer Agreement, if any, are not expected to begin for at least several years and extend over a number of subsequent years.

The Company also agreed to pay Pfizer tiered royalties on a country-by-country basis based upon the annual amount of net sales, as specified in the Pfizer Agreement until expiration of the last valid claim of the licensed patent rights including any patent term extensions or supplemental protection certificates. Under the Pfizer Agreement, the Company is obligated to use commercially reasonable efforts to develop and commercialize gemcabene.

On March 31, 2015, upon the closing of the Series A preferred stock financing, the Company issued 675,250 shares of its common stock, at a fair market value of \$0.9 million, to Pfizer in connection with the first equity payment, pursuant to which Pfizer became the owner of more than 5% of the Company's capital stock. The transaction was recorded as acquired in-process research and development expenses based on the fair market value of the common shares issued since no processes or activities that would constitute a "business" were acquired and none of the rights and underlying assets acquired had alternative future uses or reached a stage of technological feasibility. None of the other milestone or royalty payments were triggered as of March 31, 2017.

The Pfizer Agreement will expire upon expiration of the last royalty term. Either party may terminate the Pfizer

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Notes to Condensed Financial Statements (unaudited) - continued

Agreement for the other party's uncured material breach or upon specified bankruptcy events. Pfizer may terminate the Pfizer Agreement if the Company or any of its sublicenses challenge the validity, enforceability or ownership of the licensed patents. Upon termination of the license agreement for cause by Pfizer, the Company must grant Pfizer a non-exclusive license to use any intellectual property rights arising from the development or commercialization of gemcabene. Additionally, Pfizer may revoke the license if the Company is unable to adequately commercialize gemcabene by April 2021.

Pfizer has a non-exclusive, sub licensable, royalty-free right and license for non-commercial research or development purposes to intellectual property rights relating to gemcabene that are developed by us after the effective date of the license with Pfizer.

7. Convertible Series A Preferred Stock

On March 31, 2015, the Company issued 745,637 shares of Series A preferred stock at a per share price of \$6.70585, as adjusted for the Reverse Stock Split, or \$5.0 million in the aggregate, consisting of \$1.5 million in cash and \$3.5 million representing 125% of the principal and accrued and unpaid interest on the Convertible Notes, all of which converted into shares of Series A preferred stock. On August 10, 2016, immediately prior to the closing of the IPO, the Company's Series A preferred stock, together with accrued dividends thereon, converted into 827,205 shares of common stock.

Prior to their conversion into shares of common stock, the Series A preferred stock had the following rights and preferences:

Dividend Rights

Dividends effectively accrued on a daily basis at a simple rate of 8% per annum on the sum of the original per share issue price. Dividends were effectively deemed declared daily and were payable upon the occurrence of certain events. In addition, the holders of the Series A preferred stock had rights to participate in common stock dividends, entitling holders of Series A preferred stock to a dividend payable at the same time as the dividend paid on common stock based on the number of shares of common stock each share of Series A preferred stock would convert into if such shares had converted on the record date.

There were no dividends deemed payable and accrued as of March 31, 2017 or December 31, 2016 due to the conversion of the Series A preferred stock, together with accrued dividends thereon, on August 10, 2016 immediately prior to the closing of the IPO.

Voting Rights

Each share of Series A preferred stock was entitled to vote together with the common stock on all actions to be taken by the stockholders of the Company, based on the number of shares of common stock into which each share of Series A preferred stock could be converted. A separate vote of a majority of the outstanding shares of Series A preferred stock was required to (1) issue or authorize any class or series of equity securities or equivalents, (2) effect any transaction that results in a change in control, (3) change the principal business of the Company, enter new lines of business, or exit the current line of business, (4) issue convertible debt above a certain threshold, or (5) materially sell, transfer, license, pledge or encumber technology or intellectual property. A management stock option plan approved by the board of directors, however, was not subject to a separate vote of the Series A preferred stockholders, but any subsequent increases to the authorized option pool were subject to approval by the Series A preferred stock holders via a separate vote.

Liquidation Rights

In the event of any liquidation, dissolution, or winding-up of the Company, whether voluntary or involuntary, merger, consolidation or transaction in which over 50% of the Company's voting power was transferred, or a sale, lease, transfer, exclusive license or disposition of all or substantially all of the assets of the Company, the Series A preferred stock holders were entitled to the assets of the Company legally available for distribution before any distribution or payment

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was made to the holders of common stock. The distribution amount would have been equal the original issue price of the Series A preferred stock (as adjusted for any stock dividends, combinations, splits or other recapitalizations since issuance), plus any accrued or declared but unpaid dividends thereon. After payment of the full liquidation preference to the Series A preferred stock holders, the remaining assets legally available for distribution would have been distributed to the holders of common stock and holders of the Series A preferred stock pro rata based on the number of shares of common stock each share of Series A preferred stock would convert into if such shares had converted immediately prior to such liquidation, dissolution, or winding-up.

Conversion Rights

Shares of Series A preferred stock, at the option of the holder, could have been converted at any time into shares of common stock. The conversion rate would have been obtained by dividing the Series A preferred stock original issue price of \$6.70585 per share, as adjusted for the Reverse Stock Split, by the conversion price per share in effect at the time of conversion. The Series A conversion price was initially equal to the original issue price, but could be adjusted on a broad-based weighted average basis in connection with certain dilutive events. The Series A holder was also entitled to receive additional shares of common stock for any unpaid Series A dividends (whether or not declared).

Shares of Series A preferred stock would have automatically converted into common stock based upon the then-effective Series A conversion price upon the affirmative vote or consent of the holders of at least a majority of the outstanding shares of the Series A preferred stock, or at the closing of a firmly underwritten public offering.

The conversion price for the Series A preferred stock was \$6.70585 per share (as adjusted for the Reverse Stock Split) at the time of the conversion of the Series A preferred stock, together with accrued dividends thereon, immediately prior to the closing of the IPO on August 10, 2016.

Redemption Rights

The holders of at least 80% of the outstanding shares of Series A preferred stock could have required the Company to redeem all outstanding shares of Series A preferred stock at any time on or after December 31, 2020 at a redemption price equal to the greater of 150% of the liquidation preference of the Series A preferred stock or the fair market value per share plus any unpaid declared dividends. The liquidation preference of the Series A preferred stock was defined as an amount per share equal to \$6.70585, as adjusted from time to time for any stock dividends, combinations, splits or recapitalizations, plus any accrued or declared but unpaid dividends thereon.

The redemption value for redeemable preferred stock could have at times been based on fair market value. The assumptions used in calculating the estimated fair market value at each reporting period represented the Company's best estimate, however, inherent uncertainties were involved. As a result, if factors or assumptions changed, the estimated fair value could have been materially different.

The Company recognized changes in the redemption value immediately as they occurred and adjusted the carrying amount of the instrument to equal the redemption value at the end of each reporting period since it was probable that the instruments would have become redeemable. In the absence of retained earnings, these charges were recorded against additional paid-in-capital, if any, and then to accumulated deficit.

The Company evaluated the Series A preferred stock and determined that it was considered an equity host under ASC 815, *Derivatives and Hedging*. In making this determination, the Company's analysis followed the whole instrument approach that compared an individual feature against the entire Series A preferred stock instrument that included that feature. The Company's analysis was based on a consideration of the economic characteristics and risks of the Series A preferred stock. More specifically, the Company evaluated all of the stated and implied substantive terms and features of the Series A preferred stock, including: (1) redemption features and their underlying exercisability, (2) existence of any protective covenants, (3) nature of dividends rights, (4) nature of voting rights, and (5) the existence and nature of any conversion rights. As a result of the above, the Company concluded that the Series A preferred stock represented an equity host, and as such, the redemption and/or conversion features of the Series A preferred stock were considered to be clearly and closely related to the associated Series A preferred stock host instrument. Accordingly, the redemption

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Notes to Condensed Financial Statements (unaudited) - continued

and/or conversion features of the Series A preferred stock were not considered an embedded derivative that required bifurcation.

8. Stockholders' Equity

Common Stock

The Company had 10,596,838 and 9,270,255 shares of its common stock issued and outstanding as of March 31, 2017 and December 31, 2016, respectively. Voting, dividend and liquidation rights of the holders of the common stock are subject to the Company's articles of incorporation, corporate bylaws and underlying shareholder agreements.

On March 15, 2017, the Company issued and sold 1,324,256 units at a price of \$9.47 per unit for gross proceeds of approximately \$12.5 million in connection with the Private Placement. Each unit consisted of one share of the Company's common stock and a warrant to purchase 0.75 shares of common stock. The issuance costs incurred through March 31, 2017 related to the Private Placement were \$1.2 million.

Warrants

In connection with the Private Placement, the Company issued warrants to the investors participating in the financing to purchase an additional 993,204 shares of common stock. The warrants have a term of five years and were exercisable immediately upon issue with an exercise price equal to \$10.40 per share. The warrants were classified as additional paid-in capital and recorded based on their relative fair value to the underlying common shares issued in the Private Placement. The fair market value of the warrants was approximately \$4.9 million. The warrants were valued using the Black-Scholes method with the following assumptions: a risk-free interest rate of 2.0%, a contractual term of five years, zero dividend yield and a volatility factor of 65.1%.

Dividend Rights

Common stock holders are entitled to receive dividends at the sole discretion of the board of directors of the Company. There have been no dividends declared on common stock as of March 31, 2017.

Voting Rights

The holders of common stock are entitled to one vote for each share of common stock along with all other classes and series of stock of the Company on all actions to be taken by the stockholders of the Company, including actions that would amend the certificate of incorporation of the Company to increase the number of authorized shares of the common stock.

Liquidation Rights

In the event of any liquidation, dissolution, or winding-up of the Company, the holders of common stock shall be entitled to share in the remaining assets of the Company available for distribution post preferential distributions made to the Series A preferred stockholders.

Offering Costs

IPO offering costs of \$4.1 million, consisting of underwriting discounts and commissions, legal, accounting and other direct fees and costs, were initially capitalized and subsequently offset against the Company's IPO proceeds upon the close of the offering in August 2016. In addition, costs incurred related to the Private Placement of \$1.2 million through March 31, 2017 were offset against proceeds received from the Private Placement.

Gemphire Therapeutics Inc.
Notes to Condensed Financial Statements (unaudited) - continued

9. Share-Based Compensation

Share-based compensation expense was included in general and administrative and research and development costs as follows in the accompanying condensed statements of comprehensive loss (in thousands):

	Three Months Ended March 31,	
	2017	2016
General and administrative	\$ 569	\$ 123
Research and development	267	—
Total share-based compensation	<u>\$ 836</u>	<u>\$ 123</u>

Restricted Stock Awards

During the three months ended March 31, 2017 and 2016, the Company did not grant any restricted stock awards (RSAs). The RSAs were subject to various vesting schedules and generally vested ratably over a six to 24 month period coinciding with their respective service periods. During the three months ended March 31, 2017 and 2016, 4,009 and 165,505 RSAs vested, respectively and no RSAs were forfeited during these periods.

Stock Options

In April 2015, the Company adopted a 2015 Equity Incentive Plan (the 2015 Plan) under which 320,615 shares of the Company's common stock were reserved for issuance to employees, directors and consultants. The 2015 Plan permits the grant of incentive and non-statutory stock options, appreciation rights, restricted stock, restricted stock units, performance stock and cash awards, and other stock-based awards.

Amendment and Restatement of 2015 Equity Incentive Plan

In April 2016, the Company's board of directors approved the Company's amended and restated 2015 Plan (the A&R 2015 Plan). The Company's stockholders also approved the A&R 2015 Plan in April 2016 and the A&R 2015 Plan became effective immediately upon the execution and delivery of the underwriting agreement related to the IPO. The A&R 2015 Plan provides for the grant of stock options, stock appreciation rights, restricted stock awards, restricted stock unit awards, performance-based stock awards and other forms of equity awards, as well as performance cash awards. The Company initially reserved 2,400,000 shares of common stock for issuance under the A&R 2015 Plan.

Inducement Plan

In September 2016, the Company's board of directors approved the Company's Inducement Plan (the Inducement Plan). The Company initially reserved 300,000 shares of its common stock to be used exclusively for grants of awards to individuals who were not previously employees or directors of the Company, as an inducement material to the individual's entry into employment with the Company within the meaning of Rule 5635(c)(4) of the NASDAQ Listing Rules. The Plan was approved by the Company's board of directors without stockholder approval pursuant to Rule 5635(c)(4), and the terms and conditions of the Plan are substantially similar to the Company's stockholder-approved A&R 2015 Plan.

Adoption of 2016 Employee Stock Purchase Plan

In April 2016, the Company's board of directors approved the 2016 Employee Stock Purchase Plan (the ESPP) in order to enable eligible employees to purchase shares of the Company's common stock at a discount following the effective date of the IPO. The Company's stockholders also approved the ESPP in April 2016 and the ESPP became effective immediately upon the execution and delivery of the underwriting agreement related to the IPO. The Company initially

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Notes to Condensed Financial Statements (unaudited) - continued

reserved 150,000 shares of common stock for issuance under the ESPP. As of March 31, 2017, no shares were purchased under the ESPP.

During the three months ended March 31, 2017, the Company granted an aggregate of 123,500 stock options under the A&R 2015 Plan and the Inducement Plan to its officers, directors, employees and consultants, generally vesting over a four-year period with a weighted average grant date fair value of \$6.32 per share. There were no options granted during the three month period ending March 31, 2016.

The Company measures the fair value of stock options with service-based and performance-based vesting criteria to employees, consultants and directors on the date of grant using the Black-Scholes option pricing model. The fair value of equity instruments issued to non-employees is re-measured as the award vests. The Company does not have history to support a calculation of volatility and expected term. As such, the Company has used a weighted-average volatility considering the volatilities of several guideline companies.

For purposes of identifying similar entities, the Company considered characteristics such as industry, length of trading history, and stage of life cycle. The assumed dividend yield was based on the Company's expectation of not paying dividends in the foreseeable future. The average expected life of the options was determined based on the mid-point between the vesting date and the end of the contractual term according to the "simplified method" as described in Staff Accounting Bulletin 110. The risk-free interest rate is determined by reference to implied yields available from U.S. Treasury securities with a remaining term equal to the expected life assumed at the date of grant. As a result of the early adoption of ASU 2016-09, *Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*, the Company has made an accounting policy election to record forfeitures when they occur.

The weighted-average assumptions used in the Black-Scholes option-pricing model are as follows:

	Three Months Ended	
	March 31,	
	2017	2016
Expected stock price volatility	65.1%	—
Expected life of options (years)	6.1	—
Expected dividend yield	0%	—
Risk free interest rate	2.1%	—

During the three months ended March 31, 2017 and 2016, 136,353 and 35,385 stock options vested, respectively, and 3,250 and zero stock options were forfeited, respectively. As of March 31, 2017, 336,950 shares were available for future issuance under the A&R 2015 and Inducement Plans.

Unrecognized share-based compensation cost stock options issued under the A&R 2015 Plan and the Inducement Plan was \$11.2 million as of March 31, 2017. The non-employee portion of the unrecognized compensation cost was estimated utilizing the Company's fair market value for its common stock as of March 31, 2017. The unrecognized share-based expense is expected to be recognized over a weighted average period of 3.1 years for the stock options. There was no remaining unrecognized stock-based compensation related to the RSAs as of March 31, 2017.

10. Net Loss Per Common Share

Basic earnings or loss per share of common stock is computed by dividing net loss by the weighted average number of shares of common stock outstanding during the period. The holders of the Series A preferred stock had rights to participate in common stock dividends, entitling the holders of Series A preferred stock to a dividend payable at the same time and rate per share as the dividend paid on common stock based the number of shares of common stock each share of Series A preferred stock would have converted into if such shares had converted on the record date. The Series A preferred stock, however, did not have a contractual obligation to share in the losses of the Company, and as such, no losses were allocated to the Series A preferred stock for the purposes of the basic loss per share calculation while they were outstanding.

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Notes to Condensed Financial Statements (unaudited) - continued

Diluted earnings or loss per share of common stock is computed similarly to basic earnings or loss per share except the weighted average shares outstanding are increased to include additional shares from the assumed exercise of any common stock equivalents, if dilutive. The Company's RSAs, stock options, shares of Series A preferred stock, Convertible Notes and Interim Notes are considered common stock equivalents while outstanding for this purpose. Diluted earnings are computed utilizing the treasury method for the RSAs and stock options, and in the case of the Series A preferred stock, either the two-class method or the if-converted method, whichever was more dilutive. Diluted earnings with respect to the Convertible Notes and Interim Notes utilized the if-converted method, but was not applicable during the three months ended March 31, 2017 and 2016 as no conditions required for conversion had occurred during these periods while the instruments were outstanding. No incremental common stock equivalents were included in calculating diluted loss per share because such inclusion would be anti-dilutive given the net loss reported for the three months ended March 31, 2017 and 2016. The following table sets forth the computation of basic and diluted loss per share as of March 31, 2017 and 2016 (in thousands, except share and per share amounts):

	Three Months Ended March 31,	
	2017	2016
Numerator:		
Net loss	\$ (7,496)	\$ (2,103)
Adjustment to redemption value on Series A convertible preferred stock		
Premium upon substantial modification of convertible notes with certain stockholders	—	(149)
Net loss attributed to common stock holders	<u>\$ (7,496)</u>	<u>\$ (2,252)</u>
Denominator:		
Basic and diluted weighted average common shares outstanding	9,521,224	3,468,764
Basic and diluted net loss per share	<u>\$ (0.79)</u>	<u>\$ (0.65)</u>

The following potential common shares were not considered in the computation of diluted net loss per share as their effect would have been anti-dilutive:

	Three Months Ended March	
	31,	2016
	2017	2016
Stock options	2,360,723	302,842
Warrants	993,204	—
Restricted stock awards	—	182,588
Convertible Notes	—	867,498
Series A	—	745,637

11. Fair Value Measurements

The Company follows accounting guidance that emphasizes that fair value is a market-based measurement, not an entity specific measurement. Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." Fair value measurements are defined on a three level hierarchy:

Level 1 inputs: Unadjusted quoted prices for identical assets or liabilities in active markets;

Level 2 inputs: Quoted prices for similar assets and liabilities in active markets, quoted prices in markets that are not active, or inputs which are observable, whether directly or indirectly, for substantially the full term of the asset or liability;

Level 3 inputs: Unobservable inputs that reflect the Company's own assumptions about the assumptions market participants would use in pricing the asset or liability in which there is little, if any, market activity for the asset or liability at the measurement date.

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Notes to Condensed Financial Statements (unaudited) - continued

As of March 31, 2017 and December 31, 2016, the fair values of cash and cash equivalents, other assets, accounts payable and accrued liabilities approximated their carrying values because of the short-term nature of these assets or liabilities. The estimated fair value of the Company's Interim Notes prior to conversion upon the close of the IPO was based on amortized cost which was deemed to approximate fair value. The derivative liability associated with the conversion premium on the Interim Notes was based on cash flow models discounted at current implied market rates evidenced in recent arms-length transactions representing expected returns by market participants for similar instruments which were based on Level 3 inputs. There were no transfers between fair value hierarchy levels during the three months ended March 31, 2017 and 2016.

The following table provides a roll-forward of the Company's premium conversion derivative liabilities measured at fair value on a recurring basis using unobservable level 3 inputs (in thousands):

	Three Months Ended March 31,	
	2017	2016
Balance as of beginning of period	\$ —	\$ 345
Issuance of underlying convertible notes	—	8
Change in fair value of premium conversion derivative	—	(22)
Reversal of premium conversion derivative associated with note extinguishment	—	—
Redemption of underlying convertible notes	—	—
Balance as of end of period	<u>\$ —</u>	<u>\$ 331</u>

There were no instruments measured on a recurring fair value basis as of March 31, 2017 and December 31, 2016. In addition, no financial instruments were measured on a non-recurring basis for any of the periods presented.

12. Income Taxes

The effective tax rate for the three months ended March 31, 2017 and 2016 was zero percent. As a result of the analysis of all available evidence as of March 31, 2017 and December 31, 2016, the Company recorded a full valuation allowance on its net deferred tax assets. Consequently, the Company reported no income tax benefit for the three month period ended March 31, 2017, or for the comparable period in 2016. If the Company's assumptions change and the Company believes that it will be able to realize these deferred tax assets, the tax benefits relating to any reversal of the valuation allowance on deferred tax assets will be recognized as a reduction of future income tax expense. If the assumptions do not change, each period the Company could record an additional valuation allowance on any increases in the deferred tax assets.

13. Related Party Transactions

The Company rented an office in Northville, Michigan from an LLC owned by one current and one former officer under short-term agreements during the three month periods ended March 31, 2017 and 2016. The original facility lease, as amended, was cancelled and replaced with a cancellable lease agreement in August 2016 for limited use of office space in the same Northville location. The new lease agreement became effective in August 2016 and expires in September 2017 with a nominal base rent over its term. Rent expense under the related party agreements was zero and \$8,000 during the three months ended March 31, 2017 and 2016, respectively.

On March 31, 2015, 68,649 and 63,967 shares of Series A preferred stock were issued to two officers and to investors related to one board member and three officers of the Company, respectively. These issuances were the result of the conversion of a series of convertible note financings that were outstanding at the time.

During the third quarter of 2015, the Company issued \$2.8 million of Interim Notes as described in Note 4 — *Debt*. Such Interim Notes included five notes issued to two officers and three board members (or entities they control) in the amount of \$0.5 million. In addition, such Interim Notes included four notes to investors who were related to three of the Company's officers and to one of the Company's key employees in the amount of \$0.3 million.

In December 2015, the Company issued an additional \$2.7 million of Interim Notes, as described in Note 4 — *Debt*, which included six notes issued to two officers and four board members in the amount of \$0.6 million. The December

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2015 Interim Note issuances also included five notes to investors who were related to three of the Company's officers in the amount of \$0.2 million.

In February 2016, the Company issued an additional \$0.2 million of Interim Notes, as described in Note 4 — *Debt*, which included two notes issued to two board members (or entities they control) in the amount of \$81,000. The February 2016 Interim Note issuances also included a \$20,000 note to an investor who is related to an officer of the Company.

In April 2016, the Company issued an additional \$5.0 million of Interim Notes, as described in Note 4 — *Debt*, which included two notes to investors who were related to two of the Company's officers in the aggregate amount of \$0.2 million. The April 2016 Interim Notes issuances also included three notes to investors who were related to three of the Company's directors in the aggregate amount of \$2.3 million.

The IPO included 154,450 shares sold to five officers and three board members, totaling \$1.5 million. In addition, 500,000 shares were sold to one investor who is related to one of the Company's directors, totaling \$5.0 million, and 47,000 shares totaling \$0.5 million were sold to 14 investors who are related to five officers of the Company.

Lastly, the Private Placement included 56,678 units sold to three board members, for aggregate proceeds totaling approximately \$0.5 million, and 52,798 units sold to one investor who is related to one board member, for proceeds totaling approximately \$0.5 million.

14. Subsequent Events

On April 20, 2017, the registration statement on Form S-1 (File No 333-217296) for the resale of the shares of common stock issued in the Private Placement and the shares of common stock to be issued upon exercise of the warrants issued in the Private Placement was declared effective by the SEC.

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

The following discussion of our financial condition and results of operations should be read in conjunction with the financial statements and notes included in Part I "Financial Information", Item 1 "Financial Statements" of this Quarterly Report on Form 10-Q and the audited financial statements and related footnotes included in our Annual Report on Form 10-K filed on March 21, 2017.

Forward-Looking Statements

Certain statements contained in this Quarterly Report on Form 10-Q are not statements of historical fact and are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements give current expectations or forecasts of future events or our future financial or operating performance. We may, in some cases, use words such as "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "potential," "predict," "project," "should," "will," "would" or the negative of those terms, and similar expressions that convey uncertainty of future events or outcomes to identify these forward-looking statements.

These forward-looking statements reflect our management's beliefs and views with respect to future events, are based on estimates and assumptions as of the date of this report and are subject to risks and uncertainties, many of which are beyond our control, that could cause our actual results to differ materially from those in these forward-looking statements. We discuss many of these risks in greater detail under Part I, Item 1A "Risk Factors" in our Annual Report on Form 10-K filed on March 21, 2017 and subsequent reports filed with or furnished to the SEC. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

Any forward-looking statement made by us in this report speaks only as of the date hereof or as of the date specified herein. We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future developments or otherwise, except as may be required by applicable laws or regulations.

Overview

We are a clinical-stage biopharmaceutical company focused on developing and commercializing therapies for the treatment of dyslipidemia, a serious medical condition that increases the risk of life threatening cardiovascular disease, and nonalcoholic fatty liver disease (NAFLD/NASH). Dyslipidemia is generally characterized by an elevation of LDL-C, or bad cholesterol, triglycerides, or fat in the blood, as well as inflammation, especially in diabetes patients. We are developing our product candidate gemcabene, a novel, once-daily, oral therapy, for high risk cardiovascular patients who are unable to achieve normal levels of LDL-C or triglycerides with currently approved therapies, primarily statin therapy, and for those patients who present with NASH. Gemcabene's mechanism of action is designed to enhance the clearance of VLDLs in the plasma and inhibit the production of fatty acids and cholesterol in the liver. In addition, gemcabene has been shown to markedly lower C-reactive protein and improve insulin sensitization. Gemcabene has been tested as monotherapy and in combination with statins and other drugs in 895 subjects, which we define as healthy volunteers and patients, across 18 Phase 1 and Phase 2 clinical trials and has demonstrated promising evidence of efficacy, safety and tolerability.

We are pursuing gemcabene in the following indications as a treatment in addition to maximally tolerated statin therapy for patients who are unable to reach their lipid-lowering goals: HoFH, HeFH, ASCVD, SHTG and NASH. We believe we can design an efficient development plan to provide a new treatment alternative for HoFH patients while demonstrating gemcabene's potential ability to treat patients in the most severe segment of the dyslipidemia market, which can further enhance brand awareness among key thought leaders and physicians. We are developing in parallel

gemcabene for HeFH, ASCVD, SHTG and NASH given gemcabene's: (1) promising clinical data and mechanism in these indications; (2) cost-effective manufacturing process; (3) convenient oral dosing; (4) viability as adjunct combination therapy; and (5) large commercial potential. During 2016, we initiated three late stage clinical trials for gemcabene in HoFH, hypercholesterolemia, including HeFH and ASCVD patients on maximally tolerated statins, and SHTG. By the end of the second and third quarters of 2017, we expect to report top line data from the COBALT-1 and ROYAL-1 trials, respectively, and expect to report top line data from the INDIGO-1 trial by the first quarter of 2018. We plan to initiate a fourth Phase 2 clinical trial in the second half of 2017 to study gemcabene in NASH with top line data expected in the second half of 2018. Upon completion of one or more of these clinical trials, we intend to request an End of Phase 2 (EOP2) meeting with the FDA to reach an agreement on the design of Phase 3 registration trials and long term safety exposure for our target indications. We intend to pursue similar discussions with Canadian and European health authorities.

Our Company was co-founded in November 2008 as a limited liability company under the name Michigan Life Therapeutics, LLC (MLT) by former Pfizer Inc. employees, including Dr. Charles Bisgaier, who were responsible for licensing exclusive worldwide rights to gemcabene from Pfizer in April 2011. In October 2014, we incorporated a new entity under the name Gemphire Therapeutics Inc. in Delaware. In November 2014, we entered into a merger agreement with Gemphire whereby MLT was merged with and into Gemphire, with Gemphire as the surviving entity and all outstanding units of membership interest in MLT were exchanged for shares of common stock of Gemphire. The purpose of the merger was to change the jurisdiction of our incorporation from Michigan to Delaware and to convert from a limited liability company to a corporation.

In April 2016, our board of directors approved an amendment to our certificate of incorporation to effect a 1-for-3.119 reverse stock split (the Reverse Stock Split) for all common and Series A preferred stock. The Reverse Stock Split became effective on April 27, 2016 upon the filing of the amendment to the certificate of incorporation. The authorized shares and par value of the common stock and Series A preferred stock were not adjusted as a result of the Reverse Stock Split.

On August 4, 2016, our Registration Statement on Form S-1 (File No 333-210815) relating to our initial public offering ("IPO") of our common stock was declared effective by the SEC. Pursuant to such Registration Statement, on August 10, 2016, we closed our IPO whereby 3,000,000 shares of our common stock were sold at a public offering price of \$10.00 per share. On September 8, 2016, we closed the sale of 27,755 shares of our common stock at the public offering price of \$10.00 per share, representing a partial exercise of the underwriters' over-allotment option, following which, the IPO terminated. We received net proceeds of approximately \$26.1 million after deducting underwriting discounts and commissions of \$2.1 million and other offering expenses of \$2.1 million.

On March 10, 2017, we entered into a securities purchase agreement for a private placement (the Private Placement) with a select group of accredited investors whereby, on March 15, 2017, we issued and sold 1,324,256 units at a price of \$9.47 per unit for net proceeds of approximately \$11.3 million after deducting offering expenses of approximately \$1.2 million. Each unit consists of one share of our common stock and a warrant to purchase 0.75 shares of common stock. The warrants have an exercise price of \$10.40 per share and are exercisable for a period of five years from the date of issuance.

To date, our primary activities have been conducting research and development activities, planning and conducting clinical trials, performing business and financial planning, recruiting personnel and raising capital. We do not have any products approved for sale and have not generated any revenue. We do not expect to generate revenue until, and unless, the FDA or other regulatory authorities approve gemcabene and we successfully commercialize gemcabene. Until such time, if ever, as we can generate substantial product revenue, we expect to finance our cash needs through a combination of equity and debt financings as well as collaborations, strategic alliances and licensing arrangements. Through March 31, 2017, we have funded our operations primarily through the issuance of common stock in our Private Placement totaling \$12.5 million in gross proceeds, our IPO totaling \$30.3 million in gross proceeds, and, prior to our IPO, the issuance of preferred stock and convertible notes totaling \$14.8 million in gross proceeds. Our net losses were \$7.5 million and \$2.1 million for the three month periods ending March 31, 2017 and 2016, respectively, and \$14.6 million,

\$9.0 million and \$0.3 million during the years ended December 31, 2016, 2015 and 2014, respectively. As of March 31, 2017, we had an accumulated deficit of \$34.6 million. We anticipate that our expenses will increase substantially as we:

- continue clinical trials for gemcabene and for any other product candidate in our future pipeline;
- seek regulatory approvals for any product candidates that successfully complete clinical trials;
- contract to manufacture our product candidates;
- establish on our own or with partners, a sales, marketing and distribution infrastructure to commercialize any products for which we may obtain regulatory approval;
- maintain, expand and protect our intellectual property portfolio;
- hire additional staff, including clinical, scientific, operational and financial personnel, to execute our business plan;
- add operational, financial and management information systems and personnel, including personnel to support our product development and potential future commercialization efforts; and
- to enable us to operate as a public company.

Our net losses may fluctuate significantly from quarter-to-quarter and year-to-year, depending on the timing of our preclinical studies, clinical trials and our expenditures on other research and development activities.

Financial Operations Overview

Revenue

To date, we have not generated any revenue. We do not expect to generate revenue unless or until we obtain regulatory approval of and commercialize gemcabene. If we fail to complete the development of gemcabene, or any other product candidate we may pursue in the future, in a timely manner, or fail to obtain regulatory approval, our ability to generate future revenue would be compromised.

Operating Expenses

Our operating expenses are classified into two categories: general and administrative and research and development.

General and Administrative

General and administrative expenses consist primarily of personnel-related costs, including salaries and share-based compensation costs, for personnel in functions not directly associated with research and administrative activities. Other significant costs include legal fees relating to intellectual property and corporate matters and professional fees for accounting and other services. We anticipate that our general and administrative expenses will continue to trend significantly above comparable prior period levels in the future to support our research and development activities, potential commercialization of gemcabene, if approved, and any future product candidates we may develop and the increased costs of operating as a public company. These increases will include increased costs related to personnel, fees for legal and professional services, significantly increased share-based compensation costs related to stock options issued in conjunction with and subsequent to our IPO and anticipated future option grants in conjunction with personnel additions, as well as other public-company related costs.

Research and Development

To date, our research and development expenses have related primarily to the clinical stage development of gemcabene. Research and development expenses consist of costs incurred in performing research and development activities, including compensation for research and development employees, costs associated with preclinical studies and trials, regulatory activities, manufacturing activities to support clinical activities, license fees, nonlegal patent costs, fees paid to external service providers that conduct certain research and development, clinical costs and an allocation of overhead expenses. Research and development costs are expensed as incurred and costs incurred by third parties are expensed as the contracted work is performed. We accrue for costs incurred as the services are being provided by monitoring the status of the study or project, and the invoices received from our external service providers. We adjust our accrual as actual costs become known. Research and development activities are central to our business model.

We expect that gemcabene will have higher development costs during its later stages of clinical development, as compared to costs incurred during its earlier stages of development, primarily due to the increased size and duration of the later-stage clinical trials, so we expect our research and development expenses to continue to trend significantly above comparable prior period levels in the future as we continue to conduct preclinical studies and clinical trials for gemcabene and potentially develop other product candidates. However, it is difficult to determine with certainty the duration, costs and timing to complete our current or future preclinical programs and clinical trials of gemcabene. The duration, costs and timing of clinical trials and development of gemcabene will depend on a variety of factors that include, but are not limited to, the following:

- per patient trial costs;
- the number of patients that participate in the trials;
- the number of sites included in the trials;
- the countries in which the trials are conducted;
- the length of time required to enroll eligible patients;
- the number of doses that patients receive;
- the drop-out or discontinuation rates of patients;
- potential additional safety monitoring or other studies requested by regulatory agencies;
- the duration of patient follow-up;
- the phase of development of the product candidate;
- arrangements with contract research organizations and other service providers; and
- the efficacy and safety profile of the product candidates.

Interest Income

Interest income consists of cash interest earnings from short term, highly liquid money market accounts from proceeds received from the IPO and Private Placement and, in 2016, non-cash interest activity related to the Interim Notes and activity associated with the underlying premium conversion derivative related to such notes. The notes we issued had an annual interest rate of 8%. The interest on the Interim Notes compounded on an annual basis. The principal and accrued and unpaid interest on the Interim Notes converted into shares of common stock immediately prior to the closing of the IPO.

We expect to continue to earn interest income in future periods from the investment of the net proceeds from the Private Placement and IPO.

Other Expense

Other expense relates to foreign currency exchange net losses over gains. Foreign currency exchange gains and losses relate to transactions and monetary asset and liability balances denominated in currencies other than the U.S. dollar. Foreign currency gains and losses may continue to fluctuate in the future due to changes in foreign currency exchange rates.

Provision for Income Taxes

Provision for income taxes consists of federal and state income taxes in the United States, as well as deferred income taxes and changes in related valuation allowance reflecting the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Currently, there is no provision for income taxes, as we have incurred operating losses to date, and a full valuation allowance has been provided on the net deferred tax assets as of March 31, 2017 and December 31, 2016.

Results of Operations

The following table summarizes our operating results for the periods indicated:

	For the Three Months Ended		
	March 31,		
	2017	2016	Change
	(in thousands)		
Operating expenses:			
General and administrative	\$ 2,223	\$ 1,050	\$ 1,173
Research and development	5,280	1,176	4,104
Total operating expenses	<u>7,503</u>	<u>2,226</u>	<u>5,277</u>
Loss from operations	(7,503)	(2,226)	(5,277)
Interest income	12	127	(115)
Other expense	(5)	(4)	(1)
Loss before income taxes	(7,496)	(2,103)	(5,393)
Provision (benefit) for income taxes	—	—	—
Net loss	<u>\$ (7,496)</u>	<u>\$ (2,103)</u>	<u>\$ (5,393)</u>

Comparison of Three Months Ended March 31, 2017 and 2016

General and Administrative

General and administrative expenses for the three months ended March 31, 2017 increased to \$2.2 million compared to \$1.1 million for the three months ended March 31, 2016. Increased infrastructure costs to support the clinical trials and public company requirements, focused primarily in increased personnel costs, including share-based compensation expense, and professional services were the primary drivers of the increase over the prior year period. General and administrative expenses included \$0.6 million and \$0.1 million in share-based compensation expense during the three months ended March 31, 2017 and 2016, respectively.

Research and Development

Research and development expenses for the three months ended March 31, 2017 were \$5.3 million compared to \$1.2 million for the three months ended March 31, 2016. The \$4.1 million increase was primarily attributable to increased clinical trial activities encompassing three separate Phase 2b clinical trials on-going in the current year period.

versus no active clinical studies in the prior year period. Research and development expenses included \$0.3 million in share-based compensation expense during the three months ended March 31, 2017. There was no share-based compensation expense included in research and development expense during the three months ended March 31, 2016.

Interest Income

Interest income for the three months ended March 31, 2017 and 2016 was \$12,000 and \$0.1 million, respectively. Interest income during the three months ended March 31, 2017 represented cash interest earned from proceeds received from the IPO and Private Placement that were held in short term, highly liquid money market accounts. Interest income during the three months ended March 31, 2016 represented non-cash interest income on a net basis resulting from the amortization of the note premium associated with the July 2015 Interim Notes coupled with the bifurcation of the conversion premium liability and subsequent fair value adjustments associated with the Interim Notes. The Interim Notes were converted to common stock upon the close of the IPO.

Liquidity and Capital Resources

Capital Resources

As of March 31, 2017, our principal sources of liquidity consisted of cash and cash equivalents of approximately \$29.3 million. Our cash and cash equivalents are invested primarily in cash deposits and money market accounts.

We have not generated any revenue, and we anticipate that we will continue to incur losses for the foreseeable future.

We anticipate that our expenses will increase substantially as we:

- continue clinical trials for gemcabene and for any other product candidate in our future pipeline;
- seek regulatory approvals for any product candidates that successfully complete clinical trials;
- contract to manufacture our product candidates;
- establish on our own or with partners, a sales, marketing and distribution infrastructure to commercialize any products for which we may obtain regulatory approval;
- maintain, expand and protect our intellectual property portfolio;
- hire additional staff, including clinical, scientific, operational and financial personnel, to execute our business plan;
- add operational, financial and management information systems and personnel, including personnel to support our product development and potential future commercialization efforts; and
- to enable us to operate as a public company.

Historical Capital Resources

On March 15, 2017, we issued and sold 1,324,256 units at a price of \$9.47 per unit for gross proceeds of approximately \$12.5 million in connection with the Private Placement prior to the deduction of approximately \$1.2 million in offering expenses. Each unit consisted of one share of our common stock and a warrant to purchase 0.75 shares of common stock. The warrants have an exercise price of \$10.40 per share and are exercisable for a period of five years from the date of issuance. The resale of the shares of common stock issued in the Private Placement and the shares of common stock to be issued upon exercise of the warrants issued in the Private Placement was subsequently registered in April 2017 under the Securities Act of 1933, as amended.

On August 4, 2016, our Registration Statement on Form S-1 (File No 333-210815) relating to our IPO of our common stock was declared effective by the Securities and Exchange Commission. Pursuant to such Registration Statement, on August 10, 2016, we closed our IPO whereby 3,000,000 shares of our common stock were sold at a public offering price of \$10.00 per share. On September 8, 2016, we closed the sale of 27,755 shares of our common stock at the public offering price of \$10.00 per share, representing a partial exercise of the underwriters' over-allotment option, following which, the IPO terminated. We received net proceeds of approximately \$26.1 million after deducting underwriting discounts and commissions of \$2.1 million and other offering expenses of \$2.1 million.

Our primary source of cash prior to the Private Placement and IPO had been proceeds received from the issuance of preferred stock and from the issuance of convertible notes and promissory notes. The proceeds from the issuances of preferred stock and from the issuances of the convertible and promissory notes had been used to fund our operations.

From March 2009 through October 2014, we issued promissory notes for aggregate net proceeds of \$0.3 million. The promissory notes compounded at an 8% rate per annum basis and were exchanged for convertible notes on November 1, 2014.

From November 2014 through February 2015, we issued Convertible Notes for aggregate net proceeds of \$2.4 million. The Convertible Notes converted into shares of the Company's Series A preferred stock upon close of the Series A preferred stock financing on March 31, 2015. The conversion equaled 125% of the unpaid principal plus unpaid accrued interest on the convertible notes.

In March 2015, we issued preferred stock for aggregate net proceeds of approximately \$1.5 million. On August 10, 2016, immediately prior to the closing of the IPO, the Company's Series A preferred stock, together with accrued dividends thereon, converted into 827,205 shares of common stock.

In July and December 2015, we entered into convertible note financings in which we issued 8% Interim Notes in an aggregate principal amount of \$5.5 million to various investors. In February and April 2016, we issued additional 8% Interim Notes in an aggregate principal amount of \$5.2 million to various investors. The principal and accrued and unpaid interest on the Interim Notes converted into shares of common stock immediately prior to the closing of the IPO.

The following table summarizes our cash flows for the periods indicated:

	For the Three Months Ended March 31,	
	2017	2016
	(in thousands)	
Net cash used in operating activities	\$ (6,223)	\$ (2,056)
Net cash provided by (used in) investing activities	—	—
Net cash provided by financing activities	11,472	65
Net increase (decrease) in cash	\$ 5,249	\$ (1,991)

Cash Flow from Operating Activities

For the three months ended March 31, 2017, cash used in operating activities of \$6.2 million was attributable to a net loss of \$7.5 million coupled with \$0.8 million in non-cash expense adjustments and a net change of \$0.4 million in our net operating assets and liabilities. The non-cash expenses consisted of \$0.8 million of share-based compensation. The change in operating assets and liabilities was primarily attributable to a decrease in our accrued liabilities offset in part by an increase in accounts payable associated with fluctuations in our operating expense payments.

For the three months ended March 31, 2016, cash used in operating activities of \$2.1 million was substantially attributable to a net loss of \$2.1 million. The non-cash share-based compensation expense of \$0.1 million was offset by the \$0.1 million of non-cash interest income related to both the convertible notes and to the premium conversion derivative. The change in operating assets and liabilities was primarily attributable to a net increase in accrued liabilities associated with fluctuations in our operating expense payments.

Cash Flow from Investing Activities

There were no sources or uses of funds from investing activities for all periods presented.

Cash Flow from Financing Activities

Net cash provided by financing activities during the three months ended March 31, 2017 was \$11.5 million related to the proceeds from our Private Placement, net of discounts, commissions and other costs totaling \$1.1 million paid through March 31, 2017.

Net cash provided by financing activities during the three months ended March 31, 2016 was \$65,000 consisting of \$0.2 million in proceeds from the issuance of convertible notes in February 2016 offset in part by financing costs of \$86,000 associated with the IPO.

Liquidity and Capital Resource Requirements

We have no current source of revenue to sustain our present activities, and we do not expect to generate revenue until, and unless, the FDA or other regulatory authorities approve gemcabene and we successfully commercialize gemcabene. Until such time, if ever, as we can generate substantial product revenue, we expect to finance our cash needs through a combination of equity and debt financings as well as collaborations, strategic alliances and licensing arrangements. We do not have any committed external source of funds. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the ownership interest of our stockholders will be diluted, and the terms of these securities may include liquidation or other preferences that adversely affect your rights as a common stockholder. Debt financing, if available, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, making capital expenditures or declaring dividends. If we raise additional funds through collaborations, strategic alliances or licensing arrangements with pharmaceutical partners, we may have to relinquish valuable rights to our technologies, future revenue streams or grant licenses on terms that may not be favorable to us. If we are unable to raise additional funds through equity or debt financings or through collaborations, strategic alliances or licensing arrangements when needed, we may be required to delay, limit, reduce or terminate our product development, future commercialization efforts, or grant rights to develop and market gemcabene that we would otherwise prefer to develop and market ourselves.

The development of gemcabene is subject to numerous uncertainties, and we have based these estimates on assumptions that may prove to be substantially different than we currently anticipate and could use our cash resources sooner than we expect. Additionally, the process of advancing early-stage product candidates and testing product candidates in clinical trials is costly, and the timing of progress in these clinical trials is uncertain. Our ability to successfully transition to profitability will be dependent upon achieving a level of product sales adequate to support our cost structure. We cannot assure that we will ever be profitable or generate positive cash flow from operating activities.

Furthermore, we will need to raise additional capital to continue to fund the further development of gemcabene and other potential product candidates, our operations, and commercialization of gemcabene and other potential product candidates, if approved.

Critical Accounting Policies and Estimates

Our financial statements are prepared in accordance with GAAP. These accounting principles require us to make estimates and judgments that can affect the reported amounts of assets and liabilities as of the date of the financial statements as well as the reported amounts of revenue and expense during the periods presented. We believe that the estimates and judgments upon which we rely are reasonably based upon information available to us at the time that we

make these estimates and judgments. To the extent that there are material differences between these estimates and actual results, our financial results will be affected. The accounting policies that reflect our more significant estimates and judgments and which we believe are the most critical to aid in fully understanding and evaluating our reported financial results are described in Note 2 of “Part 1, Item 1 – Financial Statements” in this report.

During the three months ended March 31, 2017, there were no material changes to our critical accounting policies or estimates disclosed in “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in our Annual Report on Form 10-K filed on March 21, 2017.

Related Party Transactions

See Note 13 — “*Related Party Transactions*” included in Part I “Financial Information”, Item I “Financial Statements” in this Report regarding the impact of certain related party transactions with respect to facility rent and financing activity.

Off-Balance Sheet Arrangements

We did not have during the periods presented, and we do not currently have, any off-balance sheet arrangements as defined under the rules and regulations of the Securities and Exchange Commission.

Recent Accounting Pronouncements

Refer to Note 2 to our condensed financial statements included in Part I “Financial Information”, Item I “Financial Statements” in this Report for a discussion of recently issued accounting pronouncements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The market risk inherent in our financial instruments and in our financial position is the potential loss arising from adverse changes in interest rates. As of March 31, 2017, we had cash and cash equivalents of \$29.3 million. We generally hold our excess cash in interest-bearing money market accounts. Our primary exposure to market risk is interest rate sensitivity, which is affected by changes in the general level of U.S. interest rates. Due to the short-term maturities of our cash equivalents and the low risk profile of our investments, an immediate 100 basis point change in interest rates would not have a material effect on the fair market value of our cash equivalents.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information we are required to disclose in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

We designed and evaluate our disclosure controls and procedures recognizing that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance and not absolute assurance of achieving the desired control objectives. Also, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of simple error or mistake. The design of any system of controls is based, in part, upon certain assumptions about the likelihood of future events and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Under the supervision of and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the effectiveness of our disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15(d)-15(e) promulgated under the Exchange Act as of March 31, 2017. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2017.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the quarter ended March 31, 2017, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company may be subject to claims and lawsuits that arise primarily in the ordinary course of business. The Company believes that the disposition or ultimate resolution of any such claims and lawsuits will not have a material adverse effect on the financial position, results of operations or cash flows of the Company.

ITEM 1A. RISK FACTORS

In addition to the other information set forth elsewhere in this report, you should carefully consider the factors discussed in Part I, Item 1A "Risk Factors" of the Company's Annual Report on Form 10-K for the year ended December 31, 2016. Those factors, if they were to occur, could cause our actual results to differ materially from those expressed in our forward-looking statements in this report, and materially adversely affect our financial condition or future results. Although we are not aware of any other factors that we currently anticipate will cause our forward-looking statements to differ materially from our future actual results, or materially affect the Company's financial condition or future results, additional risks and uncertainties not currently known to us or that we currently deem to be immaterial might materially adversely affect our actual business, financial condition and/or operating results.

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

USE OF PROCEEDS

(a) Sales of Unregistered Securities

On March 10, 2017, we entered into a securities purchase agreement for a private placement with a select group of accredited investors whereby, on March 15, 2017 we issued and sold 1,324,256 units at a price of \$9.47 per unit for gross proceeds of approximately \$12.5 million. Each unit consists of one share of our common stock and a warrant to purchase 0.75 shares of common stock. The warrants have an exercise price of \$10.40 per share and are exercisable for a period of five years from the date of issuance. The private placement included 56,678 units sold to three board members, for aggregate proceeds totaling approximately \$0.5 million and 52,798 units sold to one investor who is related to one board member, for proceeds totaling approximately \$0.5 million. Piper Jaffray & Co. acted as sole lead placement agent and Laidlaw & Company (UK) Ltd. and LifeSci Capital LLC acted as co-placement agents in connection with the private placement and received fees of approximately \$1.0 million in the aggregate.

The securities were issued and sold in the private placement only to accredited investors in reliance on the exemption from registration provided by Section 4(a)(2) of the Securities Act of 1933, as amended (the "Securities Act"), and Rule 506 of Regulation D promulgated thereunder, have not been registered under the Securities Act, or state securities laws, and may not be offered or sold in the United States absent registration with the Securities and Exchange Commission or

an applicable exemption from such registration requirements. The resale of the securities from the private placement was subsequently registered, and the registration statement on Form S-1 (File No 333-217296) was declared effective on April 20, 2017 by the SEC.

(b) Use of Proceeds from Public Offering of Common Stock

On August 4, 2016, our Registration Statement on Form S-1 (File No 333-210815) relating to our IPO was declared effective by the SEC. The Registration Statement registered an aggregate of 3,450,000 shares of our common stock, including 450,000 shares of common stock registered to cover in full over-allotments by the underwriters. On August 10, 2016, we closed our IPO whereby 3,000,000 shares of our common stock were sold at a public offering price of \$10.00 per share. On September 8, 2016, we closed the sale of 27,755 shares of our common stock at the public offering price of \$10.00 per share, representing a partial exercise of the underwriters' over-allotment option, following which, the IPO terminated.

The managing underwriters of the IPO were Jefferies LLC and RBC Capital Markets, LLC. We paid to the underwriters of the initial public offering underwriting discounts and commissions totaling approximately \$2.1 million. In addition, we incurred expenses of approximately \$2.1 million which, when added to the underwriting discounts and commissions, amounted to total expenses of approximately \$4.2 million. Thus, the net offering proceeds, after deducting underwriting discounts and commissions and offering expenses, were approximately \$26.1 million.

There has been no material change in the planned use of proceeds from our IPO as described in our final prospectus filed with the SEC pursuant to Rule 424(b) on August 8, 2016.

(c) Stock Repurchases

None.

ITEM 3. DEFAULT UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

Not Applicable.

ITEM 6. EXHIBITS

EXHIBIT NUMBER	DESCRIPTION OF DOCUMENT
4.1	Form of Warrant to Purchase Common Stock (incorporated by reference to Exhibit 4.1 to the Registrant's Current Report on Form 8-K, File No. 001-37809, filed on March 13, 2017).
10.1	Form of Securities Purchase Agreement, dated March 10, 2017 (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K, File No. 001-37809, filed on March 13, 2017).
10.2	Form of Registration Rights Agreement, dated March 10, 2017 (incorporated by reference to Exhibit 10.2 to the Registrant's Current Report on Form 8-K, File No. 001-37809, filed on March 13, 2017).
31.1	Certification of Principal Executive Officer Pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a), as Adopted Pursuant to Section 302 of The Sarbanes Oxley Act of 2002.
31.2	Certification of Principal Financial Officer Pursuant to Exchange Act Rule 13a-14(a) or 15d-14(a), as Adopted Pursuant to Section 302 of The Sarbanes Oxley Act of 2002.
32.1	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

SIGNATURES

Pursuant to the requirements 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.

Registrant: Gemphire Therapeutics Inc.

<u>SIGNATURE</u>	<u>TITLE</u>	<u>DATE</u>
<u>/s/ MINA SOOCH</u> Mina Sooch	President and Chief Executive Officer (Principal Executive Officer)	May 10, 2017
<u>/s/ JEFFREY S. MATHIESEN</u> Jeffrey S. Mathiesen	Chief Financial Officer (Principal Financial and Accounting Officer)	May 10, 2017

Gemphire Therapeutics Inc.
Form 10-Q

EXHIBIT INDEX

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**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO EXCHANGE ACT RULE 13a-14(a) OR 15d-14(a), AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES OXLEY ACT OF 2002**

I, Mina Sooch, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Gemphire Therapeutics Inc. for the quarterly period ended March 31, 2017;

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

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

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

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

(b) [Intentionally Omitted];

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

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

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

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

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

Date: May 10, 2017

/s/ MINA SOOCH

Name: Mina Sooch

Title: President and Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO EXCHANGE ACT RULE 13a-14(a) OR 15d-14(a), AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES OXLEY ACT OF 2002**

I, Jeffrey S. Mathiesen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Gemphire Therapeutics Inc. for the quarterly period ended March 31, 2017;

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

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

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

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

(b) [Intentionally Omitted];

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

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

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

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

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

Date: May 10, 2017

/s/ JEFFREY S. MATHIESEN
Name: Jeffrey S. Mathiesen
Title: Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER,
PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002***

Pursuant to the requirement set forth in Rule 13a-14(b) or Rule 15d-14(b) of the Securities and Exchange Act of 1934, as amended (the "Exchange Act"), and Section 1350 of Chapter 63 of Title 18 of the United States Code, Mina Sooch, President and Chief Executive Officer of Gemphire Therapeutics Inc. (the "Company"), and Jeffrey S. Mathiesen, Chief Financial Officer of the Company, each hereby certify that, to the best of their knowledge:

1. The Company's Quarterly Report on Form 10-Q for the period ended March 31, 2017, to which this Certification is attached as Exhibit 32.1 (the "Quarterly Report") fully complies with the requirements of Section 13(a) or Section 15(d) of the Exchange Act, and
2. The information contained in the Quarterly Report fairly presents, in all material respects, the financial condition of the Company at the end of the period covered by the Quarterly Report and results of operations of the Company for the period covered by the Quarterly Report.

/s/ MINA SOOCH
President and Chief Executive Officer

/s/ JEFFREY S. MATHIESEN
Chief Financial Officer

Dated: May 10, 2017

Dated: May 10, 2017

- * This certification accompanies the report to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of Gemphire Therapeutics Inc. under the Securities Act of 1933, as amended, or the Exchange Act made before or after the date of the report, irrespective of any general incorporation language contained in such filing.
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