INTERLEUKIN GENETICS INC
Form 10-Q
August 14, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2015

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

For the transition period from _______ to _______

Commission File Number: 001-32715

INTERLEUKIN GENETICS, INC.

(Exact name of registrant in its charter)

Delaware	**94-3123681**

(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
135 Beaver Street, Waltham, MA	**02452**
(Address of principal executive offices)	(Zip Code)

Registrant's Telephone Number: **(781) 398-0700**

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

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

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

Large accelerated filer ¨	Accelerated filer ¨
Non-Accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ¨ NO x

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at August 12, 2015
Common Stock, par value $0.001 per share	**172,841,047**

INTERLEUKIN GENETICS, INC.

FORM 10-Q

FOR THE QUARTER ENDED JUNE 30, 2015

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Smaller Reporting Company – Scaled Disclosure

Pursuant to Item 10(f) of Regulation S-K promulgated under the Securities Act of 1933, as amended, as indicated herein, we have elected to comply with the scaled disclosure requirements applicable to "smaller reporting companies".

PART I —FINANCIAL INFORMATION

Item 1. Financial Statements

INTERLEUKIN GENETICS, INC.

CONDENSED BALANCE SHEETS

	June 30, 2015 (Unaudited)	**December 31,** 2014
ASSETS		
Current assets:		
Cash and cash equivalents	$7,691,919	$11,466,807
Accounts receivable from related party	50,326	23,544
Trade accounts receivable	7,623	14,013
Inventory	159,048	171,575
Prepaid expenses	565,913	504,719
Total current assets	8,474,829	12,180,658
Fixed assets, net	691,934	773,779
Intangible assets, net	156,937	195,765
Other assets	105,063	116,919
Total assets	$9,428,763	$13,267,121
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$360,238	$513,927
Accrued expenses	407,498	343,225
Deferred revenue	2,968,819	3,154,498
Total current liabilities	3,736,555	4,011,650
Long Term Debt	4,773,466	4,738,614
Total Liabilities	8,510,021	8,750,264
Commitments and contingencies (Note 6)		
Stockholders' equity:		
Common stock, $0.001 par value — 300,000,000 shares authorized; 172,786,907 and 172,683,342 shares issued and outstanding at June 30, 2015 and December 31, 2014, respectively	172,789	172,686
Additional paid-in capital	125,846,246	125,434,483
Accumulated deficit	(125,100,293)	(121,090,312)

Total stockholders’ equity	918,742	4,516,857
Total liabilities and stockholders’ equity	$9,428,763	$13,267,121

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

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INTERLEUKIN GENETICS, INC.

CONDENSED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Ended June 30, 2015	Six Months Ended June 30, 2014
Revenue:				
Genetic testing	$324,837	$483,214	$672,737	$903,547
Other	51,214	45,381	106,526	112,614
Total revenue	376,051	528,595	779,263	1,016,161
Cost of revenue	331,555	361,746	662,596	756,517
Gross profit	44,496	166,849	116,667	259,644
Operating expenses:				
Research and development	384,538	215,519	567,068	424,696
Selling, general and administrative	1,655,226	1,506,057	3,218,017	3,032,663
Amortization of intangibles	19,414	23,525	38,828	47,050
Total operating expenses	2,059,178	1,745,101	3,823,913	3,504,409
Loss from operations	(2,014,682)	(1,578,252)	(3,707,246)	(3,244,765)
Other income (expense):				
Interest income	—	1,605	222	3,599
Interest expense	(152,104)	—	(302,957)	—
Total other income (expense)	(152,104)	1,605	(302,735)	3,599
Loss before income taxes	(2,166,786)	(1,576,647)	(4,009,981)	(3,241,166)
Benefit for income taxes	—	—	—	—
Net loss	$(2,166,786)	$(1,576,647)	$(4,009,981)	$(3,241,166)
Basic and diluted net loss per common share	$(0.01)	$(0.01)	$(0.02)	$(0.03)
Weighted average common shares outstanding, basic and diluted	172,786,907	122,516,317	172,762,366	122,499,091

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

INTERLEUKIN GENETICS, INC.

CONDENSED STATEMENTS OF STOCKHOLDERS' EQUITY

(Unaudited)

	Convertible Preferred Stock		**Common Stock**				
	Shares	**Amount**	**Shares**	**Amount**	**Additional Paid-in Capital**	**Accumulated Deficit**	**Total**
Balance as of December 31, 2013	**—**	**—**	**122,448,707**	**$122,449**	**$119,885,371**	**$(114,754,598)**	**$5,253,222**
Net loss	—	—	—	—	—	(3,241,166)	(3,241,166)
Common stock issued:							
Employee stock purchase plan	—	—	67,610	69	19,175	—	19,244
Stock-based compensation expense	—	—	—	—	244,799	—	244,799
Balance as of June 30, 2014	**—**	**—**	**122,516,317**	**$122,518**	**$120,149,345**	**$(117,995,764)**	**$2,276,099**
Balance as of December 31, 2014	**—**	**—**	**172,683,342**	**$172,686**	**$125,434,483**	**$(121,090,312)**	**$4,516,857**
Net loss	—	—	—	—	—	(4,009,981)	(4,009,981)
Common stock issued:							
Private Placement					(7,100)		(7,100)
Horizon Warrant					8,887		8,887
Employee stock purchase plan	—	—	103,565	103	10,741	—	10,844
Stock-based compensation expense	—	—	—	—	399,235	—	399,235
Balance as of June 30, 2015	**—**	**—**	**172,786,907**	**$172,789**	**$125,846,246**	**$(125,100,293)**	**$918,742**

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

INTERLEUKIN GENETICS, INC.

CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

	For the Six Months Ended June 30, 2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (4,009,981)	$ (3,241,166)
Adjustments to reconcile loss to net cash used in operating activities:		
Depreciation and amortization	142,193	118,300
Amortization of loan issuance costs and FV of warrants	55,593	—
Stock-based compensation expense	399,235	244,799
Changes in operating assets and liabilities:		
Accounts receivable	6,390	(11,725)
Receivable from related party	(26,782)	489,048
Inventory	12,527	(108)
Prepaid expenses and other current assets	(61,194)	28,623
Accounts payable	(153,689)	(433,965)
Accrued expenses	64,273	41,981
Deferred revenue	(185,679)	(544,706)
Net cash used in operating activities	(3,757,114)	(3,308,919)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital additions	(21,518)	(61,250)
Net cash used in investing activities	(21,518)	(61,250)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Private placement offering costs	(7,100)	—
Proceeds from employee stock purchase plan	10,844	19,244
Net cash provided by financing activities	3,744	19,244
Net (decrease) in cash and cash equivalents	(3,774,888)	(3,350,925)
Cash and cash equivalents, beginning of period	11,466,807	7,542,281
Cash and cash equivalents, end of period	$ 7,691,919	$ 4,191,356
Supplemental disclosures of cash flow information:		
Cash paid for interest	$ 237,500	—

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

INTERLEUKIN GENETICS, INC.

NOTES TO CONDENSED FINANCIAL STATEMENTS

JUNE 30, 2015

(UNAUDITED)

Note 1—Basis of Presentation

Interleukin Genetics, Inc. (“the Company”) develops genetic tests for sale into the emerging personalized health market and performs testing services that can help individuals improve and maintain their health through preventive or therapeutic measures. The Company’s principal operations and markets are located in the United States.

The accompanying condensed financial statements include the accounts of the Company as of June 30, 2015 and December 31, 2014 and for the three and six months ended June 30, 2015 and 2014.

The financial statements have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America for interim financial reporting. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. These unaudited condensed financial statements, which, in the opinion of management, reflect all adjustments (including normal recurring adjustments) necessary for a fair presentation, should be read in conjunction with the financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014. Operating results are not necessarily indicative of the results that may be expected for any future interim period or for the entire 2015 fiscal year.

For information regarding our critical accounting policies and estimates, please refer to “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Estimates” contained in our Annual Report on Form 10-K for the year ended December 31, 2014 and Note 3 to our condensed financial statements contained herein.

Note 2—Operating Matters and Liquidity

The Company has experienced net operating losses since its inception through June 30, 2015. The Company had net losses of $6.3 million and $7.1 million for the years ended December 31, 2014 and 2013, respectively, and $4.0 million for the six months ended June 30, 2015, contributing to an accumulated deficit of $125.1 million as of June 30, 2015.

The Company continues to take steps to reduce genetic test processing costs. Cost savings are primarily achieved through test process improvements. Management believes that the current laboratory space is adequate to process high volumes of genetic tests.

On May 17, 2013, the Company entered into a Common Stock Purchase Agreement (the “2013 Purchase Agreement”) with various accredited investors (the “2013 Investors”), pursuant to which the Company sold securities to the 2013 Investors in a private placement transaction (the “May 2013 Private Placement”). In the May 2013 Private Placement, the Company sold an aggregate of 43,715,847 shares of common stock at a price of $0.2745 per share for gross proceeds of $12,000,000. The 2013 Investors also received warrants to purchase up to an aggregate of 32,786,885 shares of common stock an exercise price of $0.2745 per share (the “2013 Warrants”). The 2013 Warrants are all currently exercisable and have a term of seven years from the date they became exercisable.

On December 23, 2014, the Company entered into a Securities Purchase Agreement (the “2014 Purchase Agreement”) with various accredited investors (the “2014 Investors”), pursuant to which the Company sold to the 2014 Investors in a private placement transaction (the “December 2014 Private Placement”) an aggregate of 50,099,700 shares of common stock at a price of $0.1003 per share for gross proceeds of approximately $5.025 million. The 2014 Investors also received warrants to purchase up to an aggregate of 50,099,700 shares of common stock an exercise price of $0.1003 per share (the “2014 Warrants”). The 2014 Warrants are all currently exercisable and have a term of seven years.

On December 23, 2014, the Company entered into a Venture Loan and Security Agreement (the “Loan Agreement”) with Horizon Technology Finance Corporation (the “Lender”) under which the Company has borrowed $5.0 million. The loan bears interest at a floating rate equal to the One Month LIBOR Rate (with a floor of 0.50%) plus 8.50%. In the event that the One Month LIBOR Rate, as reported in the Wall Street Journal, exceeds 0.50%, the interest rate will be adjusted by an amount equal to the difference between such rates at the end of that particular month. At June 30, 2015, the rate was 9.0% per annum. The loan is to be repaid in forty-five (45) monthly payments consisting of fifteen (15) monthly payments of only interest followed by thirty (30) equal monthly payments of principal and interest. In addition, at the end of the repayment term (or at early termination of the loan) a final payment equal to 4.5% of the loan will be due and payable. The Company’s obligations under the Loan Agreement are secured by a first priority security interest in substantially all of its assets other than its intellectual property. The Company has also agreed not to pledge or otherwise encumber its intellectual property assets, subject to certain exceptions. In connection with the Loan Agreement, the Company issued to the Lender and its affiliates warrants to purchase a total of 2,492,523 shares of common stock at an exercise price of $0.1003 per share, which the Company refers to herein as the Lender Warrants. The Lender Warrants have a term of ten (10) years.

The Company's financial statements have been prepared assuming that it will continue as a going concern which contemplates the realization of assets and satisfaction of liabilities in the normal course of business. The financial statements do not include any adjustments that might result from the outcome of this uncertain realization. The Company expects to incur additional losses in 2015 and, accordingly, is dependent on financings and potential revenue to fund its operations and support the market adoption of the PerioPredict® test. The timing of any revenues that the Company may receive from the PerioPredict® test is uncertain at this time, and is contingent upon a number of factors, including the Company's ability to consummate arrangements with partners to promote the PerioPredict® test, the Company and its partners' ability to develop insurance plans that provide for use and reimbursement of the PerioPredict® test, or other possible arrangements, and to develop a viable market for such plans, and the timing of utilization of the PerioPredict® test pursuant to such plans. The Company expects to have the cash resources necessary to fund its operations for at least the next twelve months.

The ability of the Company to realize the carrying value of its fixed assets and intangible assets is dependent on management's ability to successfully execute on its plan. The Company needs to generate additional funds in order to meet its financial obligations. If it is unsuccessful in doing so, the Company may not be able to realize the carrying value of its fixed assets and intangible assets.

Note 3—Summary of Significant Accounting Policies

Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements, as well as the reported amounts of revenue and expenses during the reported periods. Actual results could differ from those estimates. The Company's most critical accounting policies are more fully discussed in these notes to the financial statements.

Revenue Recognition

Revenue from genetic testing services is recognized when there is persuasive evidence of an arrangement, service has been rendered, the sales price is determinable and collectability is reasonably assured. Service is deemed to be rendered when the results have been reported to the individual who ordered the test. To the extent that tests have been prepaid but results have not yet been reported, recognition of all related revenue is deferred. As of June 30, 2015 and December 31, 2014, the Company had deferred genetic test revenue of $3.0 million and $3.2 million, respectively.

Included in deferred revenue at June 30, 2015 is $2.9 million for test kits that are still outstanding one year or longer after initial kit sale, of which $0.5 million was sold directly to consumers (credit card payments) and $2.4 million was sold to distributors for the Body Key promotional bundle.

The Company recognizes breakage revenue related to genetic test kits utilizing the remote method. Under the remote method, breakage revenue should be recognized when the likelihood of the customer exercising rights of redemption becomes remote. The term remote requires statistical analysis of customer redemption patterns for all tests sold and returned. The Company analyzed redemption patterns from 2009 through 2014 and determined the period of time after which the likelihood of test redemption was remote was three years after the sale of a genetic test kit. Included in genetic test revenue in the three and six months ended June 30, 2015 is $52,305 and $128,205, respectively, of breakage revenue related to unredeemed genetic test kits sold in the first and second quarters of 2012, compared to breakage revenue included in genetic test revenue in the three and six months ended June 30, 2014 of $92,364 and $156,861, respectively, related to unredeemed genetic test kits sold in the first and second quarters of 2011. The Company expects to continue to recognize breakage revenue on a quarterly basis based on the historical analysis.

Sales Commission

On October 26, 2009, the Company entered into a Merchant Network and Channel Partner Agreement with Amway Corp., d/b/a/ Amway Global ("Amway Global"), a subsidiary of Alticor Inc. ("Alticor"). Pursuant to this Agreement, Amway Global sells the Company's Inherent Health® brand of genetic tests through its e-commerce website via a hyperlink to our e-commerce site. The Company accounts for sales commissions due to Amway Global under the Merchant Network and Channel Partner Agreement in accordance with SEC Staff Accounting Bulletin ("SAB") 104. Commissions are recorded as an expense at the time they become due which is at the point of sale. The cost of commissions was $80,000 and $59,000 for the three months ended June 30, 2015 and 2014, respectively, and $168,000 and $101,000 for the six months ended June 30, 2015 and 2014, respectively.

Accounts Receivable

Accounts receivable is stated at estimated net realizable value, which is generally the invoiced amount less any estimated discount related to payment terms. The Company offers its commercial genetic test customers a 2% cash discount if payment is made by bank wire transfer within 10 days of the invoice date. No accounts receivable reserve is required at June 30, 2015 as all accounts receivable are expected to be collected.

Inventory

Inventory is carried at lower of cost (first-in, first-out method) or market and no inventory reserve is deemed necessary at June 30, 2015. As the Company does not manufacture any products, no overhead costs are included in inventory. The Company has contracted with a fulfillment provider to supply its PerioPredict® genetic tests kits to dental offices. The agreement with the provider provides that the vendor will purchase and fulfill all materials related to the PerioPredict® test and Body Key™ genetic test kits, with the Company's approval. The Company pays for materials and fulfillment charges when the product is shipped. During the six months ended June 30, 2015, the Company purchased $33,000 of inventory related to its PerioPredict® test, which is held at our fulfillment center. When a kit is sold, the corresponding cost of the kit is recorded as deferred cost of goods sold and removed from inventory. Any kit components remaining at the fulfillment center are reflected in inventory with a corresponding offset to accounts payable. At December 31, 2014 $48,000 of raw materials were at the fulfillment center and reflected in inventory with a corresponding entry to accounts payable.

Inventory consisted of the following:

	June 30, 2015	December 31, 2014
Raw materials	$ 150,123	$ 163,239
Finished goods	8,925	8,336
Total inventory, net	$ 159,048	$ 171,575

Stock-Based Compensation

The Company accounts for stock-based compensation expense in accordance with FASB ASC 718, *Compensation – Stock Compensation*. The standard addresses all forms of share-based payment (SBP) awards, including shares issued under employee stock purchase plans, stock options, restricted stock and stock appreciation rights. We expense SBP awards within compensation cost for SBP transactions measured at fair value. Compensation cost for the portion of awards for which the requisite service has not been rendered that are outstanding as of the effective date shall be recognized as the requisite service is rendered on or after the effective date. The compensation cost for that portion of awards shall be based on the grant-date fair value of those awards as calculated under the Black-Scholes option pricing model. Common stock purchased pursuant to our employee stock purchase plan will be expensed based upon the fair market value in excess of purchase price.

Income Taxes

The Company accounts for income taxes in accordance with FASB ASC 740, *Income Taxes*, which requires the recognition of taxes payable or refundable for the current year and deferred tax liabilities and assets for the future tax consequences of events that have been recognized in the financial statements or tax returns. The measurement of current and deferred tax liabilities and assets is based on provisions of the enacted tax law; the effects of future changes in tax laws or rates are not anticipated. The Company records a valuation allowance to reduce its deferred tax assets to the amount that is more likely than not to be realized.

Significant management judgment is required in determining the Company's provision (benefit) for income taxes, its deferred tax assets and liabilities and any valuation allowance recorded against deferred tax assets. The Company has recorded a full valuation allowance against its deferred tax assets of approximately $33.4 million as of June 30, 2015, due to uncertainties related to its ability to utilize these assets. The valuation allowance is based on management's estimates of taxable income by jurisdiction in which the Company operates and the period over which the deferred tax assets will be recoverable. In the event that actual results differ from these estimates or management adjusts these estimates in future periods, the Company may need to adjust its valuation allowance, which could materially impact its financial position and results of operations.

As a result of the Company's change in its capital structure during the quarters ending June 30, 2013 and December 23, 2014, the Company may have undergone an IRC section 382 ownership change which would limit its ability to realize the benefit of its tax attributes (i.e., federal/state net operating losses and research and development credits) during their respective carry forward periods. Furthermore, pursuant to the change in capital structure, the Company realized cancellation of indebtedness income under IRC section 108(e)(8), which reduced the Company's federal net operating loss carry-forward pursuant to IRC section 108(b)(2)(A), due to the fact that the Company's liabilities exceeded the fair market value of its assets. Accordingly, the Company had a reduction in its deferred tax asset and a corresponding reduction in its valuation allowance for the quarter ending June 30, 2013. The cancellation of indebtedness income resulted from a shareholder's conversion of debt of approximately $14.3 million into common stock of the Company prior to an additional investment by an unrelated investor.

The Company reviews its recognition threshold and measurement process for recording in the financial statements uncertain tax positions taken or expected to be taken in a tax return. The Company reviews all material tax positions for all years open to statute to determine whether it is more likely than not that the positions taken would be sustained based on the technical merits of those positions. The Company did not recognize any adjustments for uncertain tax positions as of and during the six months ended June 30, 2015.

Research and Development

Research and development costs are expensed as incurred.

Basic and Diluted Net Loss per Common Share

The Company applies the provisions of FASB ASC 260, *Earnings per Share*, which establishes standards for computing and presenting earnings per share. Basic and diluted net loss per share was determined by dividing net loss applicable to common stockholders by the weighted average number of shares of common stock outstanding during the period. Diluted net loss per share is the same as basic net loss per share for all the periods presented, as the effect of the potential common stock equivalents is anti-dilutive due to the loss in each period. Potential common stock equivalents excluded from the calculation of diluted net loss per share are as follows:

	As of June 30,	
	2015	**2014**
Options outstanding	22,288,867	5,989,800
Warrants outstanding	88,301,079	37,269,125
Total	110,589,946	43,258,925

Fair Value of Financial Instruments

The Company, using available market information, has determined the estimated fair values of financial instruments. The stated values of cash and cash equivalents, accounts receivable and accounts payable approximate fair value due to the short-term nature of these instruments. The fair value of warrants is calculated using the Black-Scholes pricing model.

Cash and Cash Equivalents

The Company maintains its cash and cash equivalents with domestic financial institutions that the Company believes to be of high credit standing. The Company believes that, as of June 30, 2015, its concentration of credit risk related to cash and cash equivalents was not significant. Cash and cash equivalents are available on demand and are generally in excess of FDIC insurance limits.

Fixed Assets

Fixed assets are stated at cost, less accumulated depreciation and amortization. Depreciation and amortization are provided using the straight-line method over estimated useful lives of three to five years. Leasehold improvements are amortized over the shorter of the estimated useful life of the asset or the remaining term of the lease.

Assets that have not yet been placed in service, have the costs incurred presented as part of Projects in Progress. Once the asset has been placed in service, the related costs are transferred to the appropriate category and depreciation commences. For the six months ended June 30, 2015 there is no balance in the Projects in Progress account.

Segment Reporting

As of June 30, 2015 and 2014, the Company has one segment, the genetic test business. The Company develops genetic tests for sale into the emerging personalized health market and performs testing services that can help individuals improve and maintain their health through preventive measures. The Company's principal operations and markets are located in the United States.

Recent Accounting Pronouncements

FASB ASU 2015-03 - Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.

In April 2015, the FASB issued ASU No. 2015-03, which requires that debt issuance costs be reported in the balance sheet as a direct deduction from the face amount of the related liability, consistent with the presentation of debt discounts. Prior to the amendments, debt issuance costs were presented as a deferred charge (i.e., an asset) on the balance sheet. Further, the amendments require the amortization of debt issuance costs to be reported as interest expense. Similarly, debt issuance costs and any discount or premium are considered in the aggregate when determining the effective interest rate on the debt. The amendments are effective for public business entities for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. The amendments must be applied retrospectively. All entities have the option of adopting the new requirements as of an earlier date for financial statements that have not been previously issued. The Company does not expect this ASU to have a material impact on its consolidated financial statements.

FASB ASC 606 ASU 2014-09 - Revenue from contracts with customers.

In May 2014, the FASB issued amended guidance on contracts with customers to transfer goods or services or contracts for the transfer of nonfinancial assets, unless those contracts are within the scope of other standards (e.g., insurance contracts or lease contracts). The guidance requires an entity to recognize revenue on contracts with customers 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 or services. The guidance requires that an entity depict the consideration by applying the following five steps:

- Identify the contract(s) with a customer.
- Identify the performance obligations in the contract.
- Determine the transaction price.
- Allocate the transaction price to the performance obligations in the contract.
- Recognize revenue when (or as) the entity satisfies a performance obligation.

The amendments in this ASU are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. This amendment is to be either retrospectively adopted to each prior reporting period presented or retrospectively with the cumulative effect of initially applying this ASU recognized at the date of initial application.

In April, 2015 the FASB voted to defer the required implementation date of ASU 2014-09 to December 2017. Public companies may elect to adopt the standard along the original timeline. We are evaluating the impact of the adoption of this guidance to determine whether or not it has a material impact on the Company's financial statements.

FASB ASC 606 ASU 2014-15 - Presentation of Financial Statements—Going Concern (Subtopic 205-40); Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern.

In August 2014, the FASB issued ASU No. 2014-15, which applies should a company be facing probable liquidation within one year of the issuance of the financial statements, but is not actually in liquidation at the time of issuance. The applicable basis for presentation remains as a going concern, but if liquidation within one year is probable, then certain disclosures must be included in the financial statement presentation. ASU 2014-15 is effective for annual and interim periods beginning after December 15, 2016, with early adoption permitted. We are evaluating the impact of ASU 2014-15 on our financial disclosures, but are not electing early adoption at this time.

Note 4—Related Party Transactions

Since March 2003, the Company has maintained a broad strategic alliance with several affiliates of the Alticor Inc. family of companies, a related party. The alliance initially included an equity investment, a multi-year research and development agreement, a licensing agreement with royalties on marketed products, the deferment of outstanding loan repayment and the refinancing of bridge financing obligations.

On October 26, 2009, the Company entered into a Merchant Network and Channel Partner Agreement with Amway Corp., d/b/a/ Amway Global ("Amway Global"), a subsidiary of Alticor Inc. Pursuant to this Agreement, Amway Global sells the Company's Inherent Health® brand of genetic tests through its e-commerce website via a hyperlink to the Company's e-commerce site. The Company paid Amway Global $80,000 and $59,000 in commissions for the three months ended June 30, 2015 and 2014, respectively, and $168,000 and $101,000 in commissions for the six months ended June 30, 2015 and 2014, respectively, representing a percentage of net sales to their customers. The Company expenses commissions owed to Amway Global in the month of sale to the customer.

Beginning in September 2012 and again in 2013, Access Business Group LLC ("ABG"), an affiliate of Alticor, placed purchase orders totaling approximately $3.3 million consisting of Weight Management test kits. The kits are included as part of a promotional bundle of products that Amway is now selling to their Individual Business Owners (IBOs). Of the $3.3 million in orders, $1.5 million was received for the 2013 program and $1.8 million for the 2014 program. As a component of the 2013 promotional program, and not reflective of actual product expiry, the kits were required to be redeemed by December 31, 2013. In February 2014, the Company removed the redemption date requirement for the 2013 promotional program, for which ABG paid the Company $519,000 as a retrospective increase in the product purchase price. All cash received related to the 2013 promotional program, including the $519,000, will be treated as deferred revenue until specific kits are returned for processing or the breakage analysis determines the probability of eventual redemption is remote. In October 2014, the Company received $250,000 as a retrospective increase in the product purchase price for unsold kits as consideration for extending the required redemption date of the 2014 promotional program to December 31, 2017. All cash received for these kits will be treated as deferred revenue until specific kits are returned for processing or on the final allowed redemption date of December 31, 2017.

On September 21, 2012, the Company entered into a License Agreement with Access Business Group International LLC (“ABGI”), an affiliate of Alticor. Pursuant to the License Agreement, the Company has granted ABGI and its affiliates a non-exclusive license to use the technology related to Interleukin’s Weight Management genetic test and to sell the Weight Management test in Europe, Russia and South Africa (the “Territories”). ABGI, or a laboratory designated by ABGI, will be responsible for processing the tests, and the Company will receive a royalty for each test sold, which royalty will increase if certain pending patent applications are issued. The License Agreement has an initial term of five years from the date of first commercial sale of the Weight Management test under the agreement which was June 2013. Thereafter, the term will automatically renew for additional one-year periods unless notice is delivered by either party at least 60 days prior to the anniversary date. During the three and six months ended June 30, 2015, $49,000 and $103,203, respectively, was earned, compared to $43,000 and $97,885 in the same periods in 2014

In connection with the execution of the License Agreement, the Company and ABGI also entered into a Professional Services Agreement (the “PSA”) pursuant to which the Company has agreed to provide services to ABGI in connection with its sale and processing of the tests within the Territories. No fees were earned in the year ended December 31, 2014 or the six months ended June 30, 2015 under the PSA.

For the three months ended June 30, 2015 and 2014, approximately 46% and 39%, respectively, of the Company’s revenue came from sales through the Merchant Network and Channel Partner Agreement with Amway Global, and 16% and 38%, respectively, of the Company’s revenue came from sales through ABG’s promotional product bundle program. For the six months ended June 30, 2015 and 2014, approximately 51% and 37%, respectively, of the Company’s revenue came from sales through the Merchant Network and Channel Partner Agreement with Amway Global, and 15% and 38%, respectively, of the Company’s revenue came from sales through ABG’s promotional product bundle program.

On February 25, 2013, the Company entered into a Preferred Participation Agreement with Renaissance Health Services Corporation ("RHSC"), for itself and on behalf of certain of its affiliates and subsidiaries. RHSC is a related party through its affiliation with Delta Dental of Michigan, Inc. ("DDMI"), a stockholder of the Company. Pursuant to this agreement, affiliates of RHSC agreed to reimburse the Company a fixed price for each PerioPredict® genetic test that the Company processed for a customer of affiliates of RHSC. In addition, if during the term of the agreement the Company offered the PerioPredict® test to any other person or party for a lower price, such lower price would then be applicable to tests processed for a customer of affiliates of RHSC for the remainder of the term of the agreement. The pricing arrangement was subject to the satisfaction of certain milestones, including that (1) within a specified timeframe, RHSC affiliates were to develop and offer dental benefit plans for which a significant portion of such affiliate's clients are eligible that provided for use of the PerioPredict® test and reimbursement of the test at the agreed upon price (each such plan, hereinafter referred to as a "Reimbursed Dental Plan") and (2) prior to a specified date, RHSC affiliates were to have sold policies for Reimbursed Dental Plans for the year beginning January 1, 2014. The Company agreed that for a one year period beginning on the date on which RHSC affiliates first offered a Reimbursed Dental Plan, it would make the PerioPredict® test available solely to RHSC affiliates and not to any other third party or person. This agreement had a term of three years beginning on February 25, 2013.

On November 1, 2013, the Company entered into an Amended and Restated Preferred Participation Agreement with RHSC, for itself and on behalf of certain of its affiliates and subsidiaries. Pursuant to this agreement, affiliates of RHSC have agreed to reimburse the Company a fixed price for each PerioPredict® genetic test that the Company processes for a customer of affiliates of RHSC. In addition, if during the term of the agreement the Company offers the PerioPredict® test to any other person or party for a lower price, such lower price shall then be applicable to tests processed for a customer of such affiliates of RHSC for the remainder of the term of the agreement. RHSC and its affiliates will continue to receive the preferred pricing (or any lower market price during the term) only for so long as affiliates of RHSC continue to: (a) work to develop and to offer Reimbursed Dental Plans for which a significant portion of employees of RHSC's affiliates' customers are eligible; and (b) exercise their commercially-reasonable best efforts to maximize the number of customers that offer a Reimbursed Dental Plan. In addition, under the terms of the amended agreement, the Company is no longer obligated to make the PerioPredict® test available solely to RHSC affiliates and not to any other third party or person. This amended agreement has a term of three years beginning February 25, 2013, unless terminated earlier (1) upon the mutual written agreement of us and RHSC, (2) if either party becomes the subject of bankruptcy, insolvency, liquidation or other similar proceedings, or (3) in the event of an uncured breach of the amended agreement by either party.

The timing of any revenues that the Company may receive under the amended agreement with RHSC is dependent upon the timing of the offering of Reimbursed Dental Plans and the subsequent adoption of such Reimbursed Dental Plans by RHSC customers, the timing of which is very uncertain at this time and is dependent on a viable market developing for such plans. RHSC has informed us that it has presented the scientific data underlying Reimbursed Dental Plans to a number of customers and will make available Reimbursed Dental Plans as an alternative to a customer's current plan for any customer that expresses an interest in such a plan. The Company may never receive significant revenues under this agreement.

Note 5—Debt Instruments

Venture Loan and Security Agreement

On December 23, 2014, the Company entered into the Loan Agreement with Horizon Technology Finance Corporation (the "Lender") under which the Company borrowed \$5.0 million. The loan bears interest at a floating rate equal to the One Month LIBOR Rate (with a floor of 0.50%) plus 8.50%. In the event that the One Month LIBOR Rate, as reported in the Wall Street Journal, exceeds 0.50%, the interest rate will be adjusted by an amount equal to the difference between such rates at the end of that particular month. At June 30, 2015, the rate was 9.0% per annum. The loan is to be repaid in forty-five (45) monthly payments consisting of fifteen (15) monthly payments of only interest followed by thirty (30) equal monthly payments of principal and interest. In addition, at the end of the repayment term (or at early termination of the loan) a final payment equal to 4.5% of the loan, or \$225,000, will be due and payable. The Company's obligations under the Loan Agreement are secured by a first priority security interest in substantially all of its assets other than its intellectual property. The Company has also agreed not to pledge or otherwise encumber its intellectual property assets, subject to certain exceptions. In connection with the Loan Agreement, the Company issued to the Lender and its affiliates warrants to purchase a total of 2,492,523 shares of common stock at an exercise price of \$0.1003 per share, which the Company refers to herein as the Lender Warrants. The Lender Warrants have a term of ten (10) years.

Additionally, $88,918 in cash fees paid to the Lender and $261,386, the intrinsic value of the Lender Warrants, were recorded as a discount on the loan and amortized over the term of the loan. The final non-principal payment of $225,000 will be accrued as additional interest expense, using the effective interest method, over the term of the loan. As of June 30, 2015, the unamortized discount associated with the loan was $303,597. Cash interest expense for the three and six months ending June 30, 2015 was $113,750 and $226,250, respectively. Non-cash interest expense for the three and six months ending June 30, 2015 was $38,354 and $76,707, respectively.

Note 6—Commitments and contingencies

Operating Lease

The Company leases its office and laboratory space under a non-cancelable operating lease which was originally scheduled to expire on March 31, 2014. In May 2010, the Company completed a sublease of 6,011 square feet of underutilized office and laboratory space and on March 31, 2014, the sublease expired. On February 7, 2014, the Company entered into the Second Amendment to Commercial Lease which, among other things a) extended the term of the lease from March 31, 2014 to March 31, 2017; b) reduced the 19,000 square feet, the amount of space under the master lease, by approximately 6,011 square feet, to approximately 13,000 square feet, which is the amount of space the Company currently occupies; and, c) set an initial base rent with an escalation of 2.06% of base rent in year two and another 2.06% in year three.

Rent expense, net of the benefit of the sublease in 2014, was $94,000 and $79,000 for the three months ended June 30, 2015 and 2014, respectively, and $173,000 and $150,000 for the six months ended June 30, 2015 and 2014, respectively.

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on its financial condition, results of operations or cash flows.

Employment Agreements

On April 6, 2015 the Company entered into an Executive Employment Agreement (the "Agreement"), pursuant to which Mark B. Carbeau was appointed as the Company's Chief Executive Officer and a member of the Company's Board of Directors. Effective upon Mr. Carbeau's appointment, Dr. Kenneth S. Kornman resigned as Chief Executive Officer and remained as the Company's President and Chief Scientific Officer.

Pursuant to the Agreement, Mr. Carbeau will receive an initial annual base salary of $365,000 per year and is eligible to receive an annual target bonus of 35% of his base salary, with a stretch bonus opportunity of 150% of the target bonus. Under the terms of the Agreement, Mr. Carbeau has been granted options to purchase up to 14,245,227 shares of Interleukin's common stock (the "Options") at an exercise price of $0.1525 per share (the closing price of the common stock on April 6, 2015). The Options will vest as to 25% of the shares on April 6, 2016, and as to an additional 2.083% of the shares on the last day of each successive month thereafter, provided that he remains employed by Company on the vesting date.

The Agreement provides that if Mr. Carbeau's employment with the Company is terminated for any reason other than Cause (as defined in the Agreement) and on execution of a release of claims agreement, he will be entitled to (i) severance payments equal to 12 months of base salary and (ii) continuation of medical benefits for up to 12 months. In addition to the above, if termination is within one year following a Change of Control event and is for any reason other than Cause, all outstanding unvested equity awards will immediately vest and be exercisable.

On November 12, 2008, the Company entered into an employment agreement with Dr. Kornman, its President and Chief Scientific Officer, for a three-year term, commencing on March 31, 2009, the date his previous employment agreement expired. Effective March 31, 2012, this agreement was extended through November 30, 2012, and was extended again on November 20, 2012 through November 30, 2015. Under this agreement, Dr. Kornman received an initial annual salary of $360,000 and is eligible to receive salary increases and/or annual bonuses solely at the discretion of the Board of Directors. Under the agreement, Dr. Kornman is entitled to participate in employee benefit plans that the Company provides or may establish for the benefit of its executive management generally. In addition, while Dr. Kornman remains employed by the Company, it will reimburse him $3,296 annually for payment of life insurance premiums.

The agreement is terminable immediately by the Company with cause or upon thirty days prior written notice without cause. The agreement is terminable by Dr. Kornman upon thirty days prior written notice. If the Company terminates Dr. Kornman without cause or Dr. Kornman terminates his employment with good reason, then, in addition to payment of any accrued, but unpaid compensation prior to the termination, the Company must continue to pay his base salary and to provide health insurance benefits until the earlier of (1) expiration of the agreement or (2) twelve months. If the Company terminates Dr. Kornman in connection with a Cessation of the Company's Business (as defined in the agreement), then, in addition to payment of any accrued, but unpaid compensation prior to the termination, the Company must continue to pay his base salary and to provide health insurance benefits until the earlier of (1) expiration of the agreement or (2) three months. The agreement also includes non-compete and non-solicitation provisions for a period of twelve months following the termination of Dr. Kornman's employment.

In April 2010, Dr. Kornman was issued an option to purchase 30,000 shares of the Company's common stock at an exercise price of $0.745 per share. The option vests as to 20% of the shares on each of the first five anniversaries of the date of grant.

In May 2011, Dr. Kornman was issued an option to purchase 100,000 shares of the Company's common stock, exercisable at $0.46 per share. The option vests as to 25% of the shares on each of the first four anniversaries of the date of grant.

In December 2012, Dr. Kornman was issued an option to purchase 300,000 shares of the Company's common stock, exercisable at $0.34 per share. The option vests as to 25%, 33% and 42% of the shares on each of the first three anniversaries of the date of grant.

In October 2013, Dr. Kornman was issued an option to purchase 2,250,000 shares of the Company's common stock, at an exercise price of $0.3799 per share. The option vests as to 25% of the shares on the first anniversary of the grant date, and as to 2.08% of the remaining shares at the end of each month thereafter beginning on October 31, 2014.

In January 2015, Dr. Kornman was granted an option to purchase 2,030,000 shares of the Company's common stock. This option has an exercise price of $0.26 per share. The option vests as to 1/48 of the shares at the beginning of each month beginning on February 1, 2015.

On December 26, 2012, the Company entered into an employment agreement with Scott Snyder for the position of Chief Marketing Officer beginning on January 2, 2013. The agreement provides for a minimum annual base salary of $265,000. He is eligible for a bonus of up to 30% of his base salary, based on factors such as evaluation of individual performance, the Company's financial performance, economic conditions generally, and the policy terms applicable to such bonus. Mr. Snyder is entitled to a maximum of $34,000 in expense reimbursement in calendar year 2013, and an additional $16,000 for the six months ending June 30, 2014, for travel and housing expenses from his residence to Interleukin's offices. On July 23, 2013, the Compensation Committee agreed to amend Mr. Snyder's employment agreement and increase the aggregate amount of travel and lodging expenses that may be reimbursed to an aggregate of $60,000. On August 4, 2014, the Compensation Committee agreed to amend Mr. Snyder's employment agreement again and increase the aggregate amount of reimbursable travel and lodging expenses through December 2014 to $80,000. On January 9, 2015, the Compensation Committee agreed to amend Mr. Snyder's employment agreement again to increase the amount of reimbursable travel and lodging expenses to include $40,000 for calendar year 2015. Upon hire, Mr. Snyder was granted an option to purchase 200,000 shares of the Company's common stock at an exercise price of $0.29 per share. The option vests in three installments of 50,000, 66,000 and 84,000 shares on each of the first three anniversaries of the grant date.

Mr. Snyder's agreement is terminable at will by the Company or by Mr. Snyder. If the Company terminates Mr. Snyder without cause, then the Company will pay Mr. Snyder, in addition to any accrued, but unpaid compensation prior to termination, an amount equal to six months of his base salary in effect at the time of the termination.

In October 2013, Mr. Snyder was issued an option to purchase 675,000 shares of the Company's common stock, at an exercise price of $0.3799 per share. The option vests as to 25% of the shares on the first anniversary of the grant date, and as to 2.08% of the remaining shares at the end of each month thereafter beginning on October 31, 2014

In January 2015, Mr. Snyder was granted an option to purchase 660,000 shares of the Company's common stock. This option has an exercise price of $0.26 per share. The option vests as to 1/48 of the shares at the beginning of each month beginning on February 1, 2015.

Note 7—Capital Stock

Authorized Preferred and Common Stock

As of June 30, 2015, the Company has 6,000,000 shares of preferred stock, par value $0.001 authorized and 300,000,000 shares of common stock, par value $0.001 authorized. On July 21, 2015, the Company's shareholders' approved an amendment to the Company's Restated Certificate of Incorporation to increase the number of authorized shares of common stock from 300,000,000 to 450,000,000. As of June 30, 2015 the Company had 172,786,907 shares of common stock outstanding and the following shares of common stock are reserved for issuance:

	Reserved for issuance	Strike Price	Expiry
Shares reserved under outstanding stock options and options available for grant	22,311,279		
Shares reserved for future issuance under the Employee Stock Purchase Plan	400,387		
Warrants to purchase common stock associated with December 2014 private placement	50,189,431	$0.1003	Dec 23, 2021
Warrants to purchase common stock associated with December 2014 venture loan and security agreement	2,492,523	$0.1003	Dec 23, 2024
Warrants to purchase common stock associated with September 2014 consulting agreement with Danforth Advisors	100,000	$0.2500	Sep 8, 2024
Outstanding warrants issued in June 2012	437,158	$0.2745	Jun 29, 2017
Outstanding warrants issued in May 2013, vesting May 2013	20,655,737	$0.2745	May 17, 2020
Outstanding warrants issued in May 2013, vesting August 2013	14,426,230	$0.2745	Aug 9, 2020
Total common shares reserved for issuance at June 30, 2015	111,012,745		
Total common shares issued and outstanding at June 30, 2015	172,786,907		
Total common shares outstanding and reserved for issuance at June 30, 2015	283,799,652		

On May 17, 2013, the Company entered into the 2013 Purchase Agreement with the 2013 Investors, pursuant to which the Company sold securities to the 2013 Investors in the May 2013 Private Placement. In the May 2013 Private Placement, the Company sold an aggregate of 43,715,847 shares of its common stock at a price of $0.2745 per share for gross proceeds of $12,000,000. The 2013 Investors also received the 2013 Warrants to purchase up to an aggregate of 32,786,885 shares of common stock an exercise price of $0.2745 per share. . The 2013 Warrants were immediately exercisable as to 63% of the shares issuable thereunder. The remaining 37% of the shares issuable under the 2013 Warrants were to become exercisable upon an increase in the number of authorized shares of common stock. On August 9, 2013, the Company's shareholders' approved an amendment to the Company's Certificate of Incorporation to increase the number of authorized shares of common stock from 150,000,000 to 300,000,000 shares, which provided for adequate authorized shares for all potential common stock equivalents issued pursuant to the May 2013 Private Placement. The 2013 Warrants are all currently exercisable and have a term of seven years from the date they became exercisable.

For its services in this transaction, the placement agent received cash compensation in the amount of approximately $780,000 and the placement agent and an affiliate received warrants to purchase an aggregate of 2,295,082 shares of common stock, at an exercise price of $0.2745 per share (the “2013 Placement Agent Warrants”). The 2013 Placement Agent Warrants became exercisable on August 9, 2013, following shareholder approval of an increase in the Company’s authorized shares of common stock and expire August 9, 2020. The cash compensation and the fair value of the warrants were recorded as issuance costs resulting in a reduction to shareholders’ equity.

In September, 2014, the Company issued warrants to the Company's financial consultant, Danforth Advisors, to purchase up to 100,000 shares of common stock at a price of $0.25 per share. The warrants have a ten year term and vest on a monthly basis over two years, provided that, if the Company terminates the agreement without cause before the one year anniversary, 50% of the warrants immediately vest, and the remaining 50% of the warrants immediately vest if the Company terminates the agreement without cause after the extension of the agreement after one year. The warrant will also become exercisable in full upon a change of control of the Company if the agreement is still in effect. The fair value of the warrants at issuance was recorded as equity totaling $23,800 and will be amortized to consulting fees over the remaining service requirement. The non-cash compensation expense for the three and six months ended June 30, 2015 was $3,000 and $6,000, respectively.

On December 23, 2014, the Company entered into the 2014 Purchase Agreement with the 2014 Investors, pursuant to which it sold to the 2014 Investors in the December 2014 Private Placement an aggregate of 50,099,700 shares of common stock at a price of $0.1003 per share for gross proceeds of approximately $5.025 million. The 2014 Investors also received 2014 Warrants to purchase up to an aggregate of 50,099,700 shares of common stock an exercise price of $0.1003 per share. The 2014 Warrants are all currently exercisable and have a term of seven years.

For services related to this transaction, the placement agent and legal counsel received an aggregate of $218,126 in cash fees and the placement agent and an affiliate received warrants to purchase an aggregate of 89,731 shares of common stock (the "2014 Placement Agent Warrants"). The cash fees and the fair value of the 2014 Placement Agent Warrants were recorded as equity issuance costs resulting in a reduction to shareholders' equity.

The 2014 Warrants (and the 2014 Placement Agent Warrants) were recorded as equity at fair value on the date of issuance. Flign=left> Realty Trust (until 1994); President, Maxwell Building Corp. (until 1991).

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Non-Independent Trustee[3]

Name, age *Position(s) held with Fund* **Principal occupation(s) and other directorships during past 5 years**	**Trustee of Fund since[1]**	**Number of John Hancock funds overseen by Trustee**
James R. Boyle, Born: 1959 President, John Hancock Annuities; Executive Vice President, John Hancock Life Insurance Company (since June, 2004); Chairman and Director, John Hancock Advisers, LLC (the Adviser); John Hancock Funds, LLC (John Hancock Funds) and The Berkeley Financial Group, LLC (The Berkeley Group) (holding company) (since 2005); President U.S. Annuities; Senior Vice President, The Manufacturers Life Insurance Company (U.S.A.) (prior to 2004).	2005	237

Principal officers who are not Trustees

Name, age ***Position(s) held with Fund*** **Principal occupation(s) and** **directorships during past 5 years**	**Officer** **of Fund** **since**
Keith F. Hartstein, Born: 1956 *President and Chief Executive Officer* Senior Vice President, Manulife Financial Corporation (since 2004); Director, President and Chief Executive Officer, the Adviser and The Berkeley Group; Director, President and Chief Executive Officer, John Hancock Funds; Director, President and Chief Executive Officer, Sovereign Asset Management LLC ("Sovereign"); Director, John Hancock Signature Services, Inc.; President, John Hancock Trust; Chairman and President, NM Capital Management, Inc. (NM Capital) (since 2005); Chairman, Investment Company Institute Sales Force Marketing Committee (since 2003); Executive Vice President, John Hancock Funds (until 2005).	2005
William H. King, Born: 1952 *Vice President and Treasurer* Vice President and Assistant Treasurer, the Adviser; Vice President and Treasurer of each of the John Hancock funds advised by the Adviser; Assistant Treasurer of each of the John Hancock funds (until 2001).	1994
Francis V. Knox, Jr., Born: 1947 *Vice President and Chief Compliance Officer* Vice President and Chief Compliance Officer for John Hancock Investment Company, John Hancock Life Insurance Company (U.S.A.), John Hancock Life Insurance Company and John Hancock Funds (since 2005); Fidelity Investments - Vice President and Assistant Treasurer, Fidelity Group of Funds (until 2004); Fidelity Investments - Vice President and Ethics & Compliance Officer (until 2001).	2005
John G. Vrysen, Born: 1955 *Executive Vice President and Chief Financial Officer; Director, the Adviser, The Berkeley Group and John Hancock Funds.* Executive Vice President and Chief Financial Officer, the Adviser, Sovereign, The Berkeley Group and John Hancock Funds (since 2005); Vice President and General Manager, Fixed Annuities, U.S. Wealth Management (until 2005); Vice President, Operations, Manulife Wood Logan (July 2000 thru September 2004).	2005

Notes to Trustees and Officers pages

The business address for all Trustees and Officers is 601 Congress Street, Boston, Massachusetts 02210-2805.

The Statement of Additional Information of the Fund includes additional information about members of the Board of Trustees of the Fund and is available, without charge, upon request, by calling 1-800-225-5291.

[1] Each Trustee serves until resignation, retirement age or until his or her successor is elected.

[2] Member of Audit Committee.

[3] Non-independent Trustees hold positions with the Fund's investment adviser, underwriter and certain other affiliates.

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OF FUNDS

Equity	Balanced Fund
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	Core Equity Fund
	Focused Equity Fund
	Greater China Opportunities Fund
	Growth Trends Fund
	International Fund
	Large Cap Equity Fund
	Large Cap Select Fund
	Mid Cap Growth Fund
	Multi Cap Growth Fund
	Small Cap Equity Fund
	Small Cap Fund
	Small Cap Growth Fund
	Sovereign Investors Fund
	U.S. Global Leaders Growth Fund
Allocation	Allocation Growth + Value Portfolio
	Allocation Core Portfolio
Sector	Financial Industries Fund
	Health Sciences Fund
	Real Estate Fund
	Regional Bank Fund
	Technology Fund
	Technology Leaders Fund
Income	Bond Fund
	Government Income Fund
	High Yield Fund

	Investment Grade Bond Fund Strategic Income Fund
Tax-Free Income	California Tax-Free Income Fund High Yield Municipal Bond Fund Massachusetts Tax-Free Income Fund New York Tax-Free Income Fund Tax-Free Bond Fund
Money Market	Money Market Fund U.S. Government Cash Reserve

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For more information

The Fund□s proxy voting policies, procedures and records are available without charge, upon request:

By phone	On the Fund□s Web site	On the SEC□s Web site
1-800-225-5291	www.jhfunds.com/proxy	www.sec.gov

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Stock symbol
Listed New York Stock
Exchange:
BTO

For shareholder assistance refer to page 23

How to contact us

Internet	www.jhfunds.com	
Mail	**Regular mail:** Mellon Investor Services 85 Challenger Road Overpeck Centre Ridgefield Park, NJ 07660	
Phone	Customer service representatives	**1-800-852-0218**
	Portfolio commentary	**1-800-344-7054**
	24-hour automated information	**1-800-843-0090**
	TDD line	**1-800-231-5469**

A listing of month-end portfolio holdings is available on our Web site, www.jhfunds.com. A more detailed portfolio holdings summary is available on a quarterly basis 60 days after the fiscal quarter on our Web site or upon request by calling 1-800-225-5291, or on the Securities and Exchange Commission□s Web site, www.sec.gov.

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1-800-852-0218
1-800-843-0090 EASI-Line

1-800-231-5469 (TDD)

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P900A 10/05
12/05

ITEM 2. CODE OF ETHICS.

As of the end of the period, October 31, 2005, the registrant has adopted a code of ethics, as defined in Item 2 of Form N-CSR, that applies to its Chief Executive Officer, Chief Financial Officer and Treasurer (respectively, the principal executive officer, the principal financial officer and the principal accounting officer, the Senior Financial Officers). A copy of the code of ethics is filed as an exhibit to this Form N-CSR.

The code of ethics was amended effective February 1, 2005 to address new Rule 204A-1 under the Investment Advisers Act of 1940 and to make other related changes.

The most significant amendments were:

(a) Broadening of the General Principles of the code to cover compliance with all federal securities laws.

(b) Eliminating the interim requirements (since the first quarter of 2004) for access persons to preclear their personal trades of John Hancock mutual funds. This was replaced by post-trade reporting and a 30 day hold requirement for all employees.

(c) A new requirement for heightened preclearance with investment supervisors by any access person trading in a personal position worth $100,000 or more.

ITEM 3. AUDIT COMMITTEE FINANCIAL EXPERT.

Charles L. Ladner is the audit committee financial expert and is independent, pursuant to general instructions on Form N-CSR Item 3.

ITEM 4. PRINCIPAL ACCOUNTANT FEES AND SERVICES.

(a) Audit Fees

The aggregate fees billed for professional services rendered by the principal accountant(s) for the audit of the registrants annual financial statements or services that are normally provided by the accountant(s) in connection with statutory and regulatory filings or engagements amounted to $36,950 for the fiscal year ended October 31, 2004 and $38,000 for the fiscal year ended October 31, 2005. These fees were billed to the registrant and were approved by the registrants audit committee.

(b) Audit-Related Services

There were no audit-related fees during the fiscal year ended October 31, 2004 and fiscal year ended October 31, 2005 billed to the registrant or to the registrant's investment adviser (not including any sub-adviser whose role is primarily portfolio management and is subcontracted with or overseen by another investment adviser), and any entity controlling, controlled by, or under common control with the adviser that provides ongoing services to the registrant ("control affiliates").

(c) Tax Fees

The aggregate fees billed for professional services rendered by the principal accountant(s) for the tax compliance, tax advice and tax planning (tax fees) amounted to $2,250 for the fiscal year ended October 31, 2004 and $2,400 for the fiscal year ended October 31, 2005. The nature of the services comprising the tax fees was the review of the registrant’s income tax returns and tax distribution requirements. These fees were billed to the registrant and were approved by the registrant’s audit committee. There were no tax fees billed to the control affiliates.

(d) All Other Fees

There were no other fees during the fiscal year ended October 31, 2004 and fiscal year ended October 31, 2005 billed to the registrant or to the control affiliates.

(e)(1) See attachment "Approval of Audit, Audit-related, Tax and Other Services", with the audit committee pre-approval policies and procedures.

(e)(2) There were no fees that were approved by the audit committee pursuant to the de minimis exception for the fiscal years ended October 31, 2004 and October 31, 2005 on behalf of the registrant or on behalf of the control affiliates that relate directly to the operations and financial reporting of the registrant.

(f) According to the registrant’s principal accountant, for the fiscal year ended October 31, 2005, the percentage of hours spent on the audit of the registrant's financial statements for the most recent fiscal year that were attributed to work performed by persons who were not full-time, permanent employees of principal accountant was less than 50%.

(g) The aggregate non-audit fees billed by the registrant's accountant(s) for services rendered to the registrant and rendered to the registrant's control affiliates for each of the last two fiscal years of the registrant were $2,250 for the fiscal year ended October 31, 2004, and $69,600 for the fiscal year ended October 31, 2005.

(h) The audit committee of the registrant has considered the non-audit services provided by the registrant’s principal accountant(s) to the control affiliates and has determined that the services that were not pre-approved are compatible with maintaining the principal accountant(s)' independence.

ITEM 5. AUDIT COMMITTEE OF LISTED REGISTRANTS.

The registrant has a separately-designated standing audit committee comprised of independent trustees. The members of the audit committee are as follows:

Charles L. Ladner - Chairman
Richard P. Chapman, Jr.
Dr. John A. Moore
Patti McGill Peterson

ITEM 6. SCHEDULE OF INVESTMENTS.

Not applicable.

ITEM 7. DISCLOSURE OF PROXY VOTING POLICIES AND PROCEDURES FOR CLOSED-END MANAGEMENT INVESTMENT COMPANIES.

See attached Exhibit “Proxy Voting Policies and Procedures”.

ITEM 8. PORTFOLIO MANAGERS OF CLOSED-END MANAGEMENT INVESTMENT COMPANIES.

Not applicable.

ITEM 9. PURCHASES OF EQUITY SECURITIES BY CLOSED-END MANAGEMENT INVESTMENT COMPANY AND AFFILIATED PURCHASERS.

Not Applicable.

ITEM 10. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

(a) The registrant has adopted procedures by which shareholders may recommend nominees to the registrant's Board of Trustees. A copy of the procedures is filed as an exhibit to this Form N-CSR. See attached "John Hancock Funds - Administration Committee Charter".

ITEM 11. CONTROLS AND PROCEDURES.

(a) Based upon their evaluation of the registrant's disclosure controls and procedures as conducted within 90 days of the filing date of this Form N-CSR, the registrant's principal executive officer and principal financial officer have concluded that those disclosure controls and procedures provide reasonable assurance that the material information required to be disclosed by the registrant on this report is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

(b) There were no changes in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal half-year (the registrant's second fiscal half-year in the case of an annual report) that have materially affected, or are reasonably likely to materially affect, the registrant's internal control over financial reporting.

ITEM 12. EXHIBITS.

(a)(1) Code of Ethics for Senior Financial Officers is attached.

(a)(2) Separate certifications for the registrant's principal executive officer and principal financial officer, as required by Section 302 of the Sarbanes-Oxley Act of 2002 and Rule 30a-2(a) under the Investment Company Act of 1940, are attached.

(b)(1) Separate certifications for the registrant's principal executive officer and principal financial officer, as required by 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and Rule 30a-2(b) under the Investment Company Act of 1940, are attached. The certifications furnished pursuant to this paragraph are not deemed to be "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that section. Such certifications are not deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that the Registrant specifically incorporates them by reference.

(c)(1) Proxy Voting Policies and Procedures are attached.

(c)(2) Submission of Matters to a Vote of Security Holders is attached. See attached "John Hancock Funds - Administration Committee Charter".

(c)(3) Approval of Audit, Audit-related, Tax and Other Services is attached.

(c)(4) Contact person at the registrant.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

John Hancock Bank and Thrift Opportunity Fund

By: /s/ Keith F. Hartstein

Keith F. Hartstein
President and Chief Executive Officer

Date: December 21, 2005

Pursuant to the requirements of the Securities Exchange Act of 1934 and the Investment Company Act of 1940, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Keith F. Hartstein

Keith F. Hartstein

President and Chief Executive Officer

Date: December 21, 2005

By: /s/ John G. Vrysen

John G. Vrysen

Executive Vice President and Chief Financial Officer

Date: December 21, 2005