

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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 **June 30, 2016**

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

For the transition period from _____ to _____

Commission file number: **000-55413**

CELL SOURCE, INC.

(Exact name of registrant as specified in its charter)

Nevada

(State or other jurisdiction of incorporation or organization)

32-0379665

(I.R.S. Employer Identification No.)

**5 Kineret Street
Bnei Brak, Israel**

(Address of principal executive offices)

5126237

(Zip Code)

Registrant's telephone number, including area code **011 972 3 562-1755**

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

Accelerated filer
Smaller reporting
company

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

As of August 10, 2016, the registrant had 24,679,256 shares of \$0.001 par value common stock outstanding.

CELL SOURCE, INC. AND SUBSIDIARY

FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2016

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CELL SOURCE, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED BALANCE SHEETS

	June 30, 2016	December 31, 2015
	<u>(Unaudited)</u>	
Assets		
Current Assets:		
Cash	\$ 3,736	\$ 6,944
Prepaid expenses	108,077	71,882
Other current assets	<u>135,989</u>	<u>134,736</u>
Total Current Assets	247,802	213,562
Property and equipment, net	<u>837</u>	<u>1,267</u>
Total Assets	<u>\$ 248,639</u>	<u>\$ 214,829</u>
Liabilities and Stockholders' Deficiency		
Current Liabilities:		
Accounts payable and accrued expenses, current portion	\$ 727,058	\$ 586,485
Accounts payable and accrued expenses - related parties	208,798	214,629
Accrued compensation	465,703	324,672
Derivative liabilities	3,508,850	3,279,600
Notes payable, net of debt discount of \$35,600 and \$41,600 at June 30, 2016 and December 31, 2015, respectively	1,367,400	708,400
Notes payable - related party, net of debt discount of \$1,900 and \$19,300 at June 30, 2016 and December 31, 2015, respectively	148,100	180,700
Convertible notes payable, current portion, net of debt discount of \$286,807 and \$214,550 at June 30, 2016 and December 31, 2015, respectively	690,693	180,450
Advances payable	<u>200,000</u>	<u>450,000</u>
Total Current Liabilities	7,316,602	5,924,936
Convertible notes payable, non-current portion, net of debt discount of \$241,400 and \$288,832 at June 30, 2016 and December 31, 2015, respectively	148,600	43,668
Accounts payable and accrued expenses, non-current portion	<u>15,384</u>	<u>4,474</u>
Total Liabilities	<u>7,480,586</u>	<u>5,973,078</u>
Commitments and contingencies		
Stockholders' Deficiency:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized; no shares issued and outstanding at June 30, 2016 and December 31, 2015	-	-
Common stock, \$0.001 par value; 200,000,000 shares authorized; 23,929,256 shares issued and outstanding at June 30, 2016 and December 31, 2015	23,929	23,929
Additional paid-in capital	4,767,947	4,720,417
Accumulated deficit	<u>(12,023,823)</u>	<u>(10,502,595)</u>
Total Stockholders' Deficiency	<u>(7,231,947)</u>	<u>(5,758,249)</u>
Total Liabilities and Stockholders' Deficiency	<u>\$ 248,639</u>	<u>\$ 214,829</u>

See Notes to the Condensed Consolidated Financial Statements

CELL SOURCE, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	For the Three Months Ended June 30,		For The Six Months Ended June 30,	
	2016	2015	2016	2015
Revenues	\$ -	\$ -	\$ -	\$ -
Operating Expenses				
Research and development	110,167	124,472	223,588	177,219
Research and development - related party	198,820	200,000	398,820	400,000
Selling, general and administrative	221,179	243,261	552,437	576,778
Total Operating Expenses	530,166	567,733	1,174,845	1,153,997
Loss From Operations	(530,166)	(567,733)	(1,174,845)	(1,153,997)
Other Income (Expense)				
Change in fair value of derivative liabilities	209,900	79,200	370,850	112,700
Interest expense	(55,232)	(5,277)	(118,557)	(6,756)
Amortization of debt discount	(325,288)	(77,100)	(598,676)	(79,500)
Total Other (Expense) Income	(170,620)	(3,177)	(346,383)	26,444
Net Loss	\$ (700,786)	\$ (570,910)	\$ (1,521,228)	\$ (1,127,553)
Net Loss Per Share				
- Basic and Diluted	\$ (0.03)	\$ (0.02)	\$ (0.06)	\$ (0.04)
Weighted Average Number of Common Shares Outstanding				
- Basic and Diluted	25,973,091	25,623,091	25,973,091	25,623,091

See Notes to the Condensed Consolidated Financial Statements

CELL SOURCE, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' DEFICIENCY
FOR THE SIX MONTHS ENDED JUNE 30, 2016

(Unaudited)

	<u>Common Stock</u>		<u>Additional</u>	<u>Accumulated</u>	<u>Total</u>
	<u>Shares</u>	<u>Amount</u>	<u>Paid-In</u>	<u>Deficit</u>	
			<u>Capital</u>		
Balance - December 31, 2015	23,929,256	\$ 23,929	\$ 4,720,417	\$ (10,502,595)	\$ (5,758,249)
Stock-based compensation:					
- warrants	-	-	47,530	-	47,530
Net loss	-	-	-	(1,521,228)	(1,521,228)
Balance - June 30, 2016	<u>23,929,256</u>	<u>\$ 23,929</u>	<u>\$ 4,767,947</u>	<u>\$ (12,023,823)</u>	<u>\$ (7,231,947)</u>

See Notes to the Condensed Consolidated Financial Statements

CELL SOURCE, INC. AND SUBSIDIARY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For The Six Months Ended June 30,	
	2016	2015
Cash Flows From Operating Activities		
Net loss	\$ (1,521,228)	\$ (1,127,553)
Adjustments to reconcile net loss to net cash used in operating activities:		
Change in fair value of derivative liabilities	(370,850)	(112,700)
Amortization of debt discount	598,676	79,500
Depreciation	430	430
Stock-based compensation:		
Warrants	91,962	(33,400)
Changes in operating assets and liabilities:		
Prepaid expenses	(36,195)	(68,395)
Other current assets	(1,253)	(42,701)
Accounts payable and accrued expenses	286,825	190,515
Net Cash Used in Operating Activities	<u>(951,633)</u>	<u>(1,114,304)</u>
Cash Flows From Financing Activities		
Proceeds from issuance of notes payable	1,043,000	750,000
Repayment of note payable, related party	(50,000)	-
Payment of debt issuance costs	(44,575)	-
Proceeds from cash advances	-	450,000
Net Cash Provided by Financing Activities	<u>948,425</u>	<u>1,200,000</u>
Net (Decrease) Increase In Cash	<u>(3,208)</u>	<u>85,696</u>
Cash - Beginning	<u>6,944</u>	<u>19,480</u>
Cash - Ending	<u>\$ 3,736</u>	<u>\$ 105,176</u>
Supplemental Disclosures of Cash Flow Information:		
Non-cash investing and financing transactions:		
Warrants and conversion options issued in connection with issuance of notes payable	\$ 600,100	\$ 265,800
Advance exchanged for a convertible note payable	<u>\$ 250,000</u>	<u>\$ -</u>

See Notes to the Condensed Consolidated Financial Statements

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1 – Organization, Operations and Basis of Presentation

Organization and Operations

Cell Source, Inc. (“CSI” or the “Company”) is a Nevada corporation formed on June 6, 2012 that is the parent company of Cell Source Limited, which was founded in Israel in 2011 in order to commercialize a suite of inventions relating to certain cancer treatments. Cell Source Limited’s target indications include treatment of lymphoma, multiple myeloma and B-cell chronic lymphocytic leukemia (“BCLL”) (which is a common form of leukemia), facilitating transplantation acceptance (initially bone marrow transplantation and subsequently organ transplantation) and ultimately treating a variety of non-malignant diseases. Cell Source Limited’s lead prospective product is its patented Veto Cell immune system management technology, which is an immune tolerance biotechnology that enables the selective blocking of immune responses. Cell Source Limited’s Veto Cell immune system management technology is based on technologies patented, owned, and licensed to Cell Source Limited by Yeda Research and Development Company Limited, an Israeli corporation (“Yeda”).

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, such statements include all adjustments (consisting only of normal recurring items) which are considered necessary for a fair presentation of the condensed consolidated financial position of the Company as of June 30, 2016 and the condensed consolidated results of its operations for the three and six months ended June 30, 2016 and 2015 and cash flows for the six months ended June 30, 2016 and 2015. The results of operations for the three and six months ended June 30, 2016 are not necessarily indicative of the operating results for the full year. It is recommended that these condensed consolidated financial statements be read in conjunction with the audited consolidated financial statements and related disclosures of the Company as of December 31, 2015 and for the year then ended which were filed with the Securities and Exchange Commission (“SEC”) on Form 10-K on April 14, 2016.

Note 2 – Going Concern and Management Plans

The Company has not generated any revenues, has recurring net losses, a working capital deficiency as of June 30, 2016 of approximately \$7,069,000, and used cash in operations of approximately \$952,000 and \$1,114,000 for the six months ended June 30, 2016 and 2015, respectively. These conditions raise substantial doubt about the Company’s ability to continue as a going concern.

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. GAAP, which contemplate continuation of the Company as a going concern and the realization of assets and satisfaction of liabilities in the normal course of business. The ability of the Company to continue its operations is dependent on the execution of management’s plans, which include the raising of capital through the debt and/or equity markets, until such time that funds provided by operations are sufficient to fund working capital requirements. If the Company were not to continue as a going concern, it would likely not be able to realize its assets at values comparable to the carrying value or the fair value estimates reflected in the balances set out in the preparation of the condensed consolidated financial statements.

There can be no assurances that the Company will be successful in generating additional cash from the equity/debt markets or other sources to be used for operations. The condensed consolidated financial statements do not include any adjustments relating to the recoverability of assets and classification of assets and liabilities that might be necessary. Based on the Company’s current resources, the Company will not be able to continue to operate without additional immediate funding. Should the Company not be successful in obtaining the necessary financing to fund its operations, the Company would need to curtail certain or all operational activities and/or contemplate the sale of its assets, if necessary.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 3 – Summary of Significant Accounting Policies

Principles of Consolidation

The Company's financial statements are consolidated and include the accounts of CSI and Cell Source Limited. All significant intercompany transactions have been eliminated in the consolidation.

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of expenses during the reporting period.

Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. The most significant estimates, among other things, are used in accounting for allowances for deferred income taxes, contingencies, as well as the recording and presentation of its common stock and related warrant issuances. Estimates and assumptions are periodically reviewed and the effects of any material revisions are reflected in the financial statements in the period that they are determined to be necessary. Actual results could differ from those estimates and assumptions.

Loss Per Share

The Company computes basic net loss per share by dividing net loss by the weighted average number of common shares outstanding for the period and excludes the effects of any potentially dilutive securities. Diluted earnings per share includes the dilution that would occur upon the exercise or conversion of all dilutive securities into common stock using the "treasury stock" and/or "if converted" methods, as applicable. Weighted average shares outstanding for the three and six months ended June 30, 2016 and 2015 includes the weighted average impact of warrants to purchase an aggregate of 2,043,835 shares of common stock because their exercise price was determined to be nominal.

The following securities are excluded from the calculation of weighted average dilutive common shares because their inclusion would have been anti-dilutive:

	<u>June 30,</u>	
	<u>2016</u>	<u>2015</u>
Warrants	11,374,324	7,629,324
Convertible notes	3,203,450	-
Total	<u>14,577,774</u>	<u>7,629,324</u>

Deferred Financing Costs

The Company has recorded deferred financing costs as a result of fees incurred by the Company in conjunction with its debt financing activities. These costs are amortized using the interest method over the shorter of (a) the term of the related debt or (b) the expected conversion date of the debt into equity instruments. During the six months ended June 30, 2016, the Company adopted Accounting Standards Update ("ASU") No. 2015-03, "Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs" and, as a result, the Company reclassified deferred financing costs for all periods presented such that costs are included as a discount to convertible notes payable on the accompanying condensed consolidated balance sheets.

As of June 30, 2016 and December 31, 2015, there was \$125,443 and \$46,068 of accumulated amortization of deferred financing costs, respectively. As of June 30, 2016 and December 31, 2015, there was \$73,557 and \$152,932, respectively, of unamortized deferred financing costs which were included as a discount to convertible notes payable on the accompanying condensed consolidated balance sheets. See Note 6 – Notes Payable – Summary – for details associated with amortization of deferred financing costs which are included within amortization of debt discount on the condensed consolidated statements of operations.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 3 – Summary of Significant Accounting Policies - Continued

Derivative Financial Instruments

The fair value of an embedded conversion option that is convertible into a variable amount of shares and warrants that include price protection reset provision features are deemed to be “down-round protection” and, therefore, do not meet the scope exception for treatment as a derivative under Accounting Standards Codification (“ASC”) 815 “Derivatives and Hedging”, since “down-round protection” is not an input into the calculation of the fair value of the conversion option and warrants and cannot be considered “indexed to the Company’s own stock” which is a requirement for the scope exception as outlined under ASC 815.

The accounting treatment of derivative financial instruments requires that the Company record the embedded conversion option and warrants at their fair values as of the inception date of the agreement and at fair value as of each subsequent balance sheet date. Any change in fair value is recorded as non-operating, non-cash income or expense for each reporting period at each balance sheet date. The Company reassesses the classification of its derivative instruments at each balance sheet date. If the classification changes as a result of events during the period, the contract is reclassified as of the date of the event that caused the reclassification. As a result of entering into warrant agreements, for which such instruments contained a variable conversion feature with no floor, the Company has adopted a sequencing policy in accordance with ASC 815-40-35-12 whereby all future instruments may be classified as a derivative liability with the exception of instruments related to share-based compensation issued to employees or directors.

The Black-Scholes option pricing model was used to estimate the fair value of the warrants and conversion options. The model includes subjective input assumptions that can materially affect the fair value estimates. The Company determined the fair value under the binomial lattice model and the Black-Scholes model to be materially the same. The expected volatility is estimated based on the most recent historical period of time equal to the weighted average life of the warrants.

Conversion options are recorded as debt discount and are amortized as interest expense over the life of the underlying debt instrument.

Recent Accounting Standards

In March 2016, the Financial Accounting Standards Board issued ASU No. 2016-09, “Compensation – Stock Compensation (Topic 718)” (“ASU 2016-09”). ASU 2016-09 requires an entity to simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, with early adoption permitted. The Company is currently evaluating ASU 2016-09 and its impact on its condensed consolidated financial statements or disclosures.

The Company has evaluated all new accounting standards that are in effect and may impact its condensed consolidated financial statements and does not believe that there are any other new accounting standards that have been issued that might have a material impact on its financial position or results of operations.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 4 - Fair Value

The Company determines the estimated fair value of amounts presented in these condensed consolidated financial statements using available market information and appropriate methodologies. However, considerable judgment is required in interpreting market data to develop the estimates of fair value. The estimates presented in the financial statements are not necessarily indicative of the amounts that could be realized in a current exchange between buyer and seller. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. These fair value estimates were based upon pertinent information available as of June 30, 2016 and December 31, 2015, and, as of those dates, the carrying value of all amounts approximates fair value. The Company estimated the fair value of its common stock during the three and six months ended June 30, 2016. To determine the value of its common stock, the Company considered the following three possible valuation methods (1) the income approach, (2) the market approach and the (3) cost approach to estimate its enterprise value.

The Company has categorized its assets and liabilities at fair value based upon the following fair value hierarchy:

Level 1 - Inputs use quoted prices in active markets for identical assets or liabilities that the Company has the ability to access.

Level 2 - Inputs use directly or indirectly observable inputs. These inputs include quoted prices for similar assets and liabilities in active markets as well as other inputs such as interest rates and yield curves that are observable at commonly quoted intervals.

Level 3 - Inputs are unobservable inputs, including inputs that are available in situations where there is little, if any, market activity for the related asset or liability.

In instances where inputs used to measure fair value fall into different levels in the above fair value hierarchy, fair value measurements in their entirety are categorized based on the lowest level input that is significant to the valuation. The Company's assessment of the significance of particular inputs to these fair measurements requires judgment and considers factors specific to each asset or liability.

Both observable and unobservable inputs may be used to determine the fair value of positions that are classified within the Level 3 category. As a result, the unrealized gains and losses for assets within the Level 3 category presented in the tables below may include changes in fair value that were attributable to both observable (e.g., changes in market interest rates) and unobservable (e.g., changes in historical company data) inputs.

The following table summarizes the valuation of the Company's derivative liabilities and accrued compensation by the above fair value hierarchy levels as of June 30, 2016 and December 31, 2015 using quoted prices in active markets for identical assets (Level 1), significant other observable inputs (Level 2), and significant unobservable inputs (Level 3):

	Total	Quoted Prices In Active Markets for Identical Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Accrued compensation	\$ 104,431	\$ -	\$ -	\$ 104,431
Derivative liability	<u>3,508,850</u>	<u>-</u>	<u>-</u>	<u>3,508,850</u>
Balance - June 30, 2016	<u>\$ 3,613,281</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,613,281</u>
Accrued compensation	\$ 60,000	\$ -	\$ -	\$ 60,000
Derivative liability	<u>3,279,600</u>	<u>-</u>	<u>-</u>	<u>3,279,600</u>
Balance - December 31, 2015	<u>\$ 3,339,600</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,339,600</u>

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 4 - Fair Value – Continued

Financial assets are considered Level 3 when their fair values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. The Company's Level 3 liabilities shown in the above table consist of warrants with "down-round protection", as the Company is unable to determine if it will have sufficient authorized common stock to settle such arrangements, warrants deemed to be derivative liabilities according to the Company's sequencing policy in accordance with ASC 815-40-35-12, the conversion option of convertible notes payable and accrued obligations to issue a warrant and common stock.

Assumptions utilized in the valuation of Level 3 liabilities are described as follows:

	For the Three Months		For the Six Months Ended	
	Ended		June 30,	
	2016	2015	2016	2015
Risk-free interest rate	0.26% - 0.86%	1.01% - 1.63%	0.21% - 1.04%	1.01% - 1.63%
Expected term (years)	0.04 - 4.19	3.33 - 4.37	0.04 - 5.00	3.33 - 4.62
Expected volatility	152%	166% - 172%	152% - 159%	166% - 172%
Expected dividends	0.00%	0.00%	0.00%	0.00%

The expected term used is the contractual life of the instrument being valued. Since the Company's stock has not been publicly traded for a sufficiently long period of time or with significant volume, the Company is utilizing an expected volatility based on a review of the historical volatilities, over a period of time, equivalent to the expected life of the instrument being valued, of similarly positioned public companies within its industry. The risk-free interest rate was determined from the implied yields from U.S. Treasury zero-coupon bonds with a remaining term consistent with the expected term of the instrument being valued.

The following table provides a summary of the changes in fair value, including net transfers in and/or out, of all Level 3 liabilities measured at fair value on a recurring basis using unobservable inputs during the six months ended June 30, 2016:

	Accrued Compensation	Derivative Liability	Total
Balance - December 31, 2015	\$ 60,000	\$ 3,279,600	\$ 3,339,600
Change in fair value	(674)	(370,850)	(371,524)
Issuance of warrants and conversion options	-	600,100	600,100
Accrual of obligations	45,105	-	45,105
Balance - June 30, 2016	<u>\$ 104,431</u>	<u>\$ 3,508,850</u>	<u>\$ 3,613,281</u>

The Company's significant financial instruments such as cash, other current assets, accounts payable, accrued expenses and notes payable were deemed to approximate fair value due to their short term nature.

See Note 6 – Notes Payable for details associated with the issuance of warrants and conversion options which were deemed to be derivative liabilities.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 5 – Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses consisted of the following:

	June 30, 2016	December 31, 2015
	(unaudited)	
Accrued research and development	\$ 117,949	\$ 186,815
Accrued legal fees	194,940	216,956
Accrued other professional fees	100,502	75,164
Accrued director compensation	12,000	12,000
Accrued Scientific Advisory Board compensation	57,000	31,000
Accrued interest, current portion	130,660	25,139
Other accrued expenses	114,007	39,411
Accounts payable and accrued expenses, current portion	727,058	586,485
Non-current portion of accrued interest	15,384	4,474
Total accounts payable and accrued expenses	<u>\$ 742,442</u>	<u>\$ 590,959</u>

Note 6 – Notes Payable

Non-Convertible Notes

On March 8, 2016, the Company issued six-month notes payable in the aggregate principal amount of \$600,000 which bear interest at a rate of 10% per annum. In connection with the note issuances, the Company issued immediately vested warrants to purchase an aggregate of 300,000 shares of common stock at an exercise price of \$0.75 per share with an issuance date fair value of \$93,400, which were recorded as a debt discount. In connection with the Company's sequencing policy, the warrants were determined to be derivative liabilities. See Note 4 – Fair Value for additional details. The warrants contain a provision that provides the Company with an option, prior to the expiration date, to redeem all of the warrants then outstanding upon not less than thirty (30) days nor more than (60) days notice to the applicable holder, at a redemption price of \$0.01 per share, subject to the conditions that: (i) there is an effective registration statement covering the resale of the underlying shares of common stock and (ii) the common stock has traded for twenty (20) consecutive days with a closing price of at least \$2.50 per share with an average trading volume of 100,000 shares per day. The warrants expire on March 25, 2019.

On April 4, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000, originally dated May 15, 2015, from December 31, 2015 to June 30, 2016. See Note 11 – Subsequent Events – Notes Payable for details related to the subsequent extension of this note.

On April 6, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000, originally dated March 26, 2015, from March 26, 2016 to June 27, 2016. See Note 11 – Subsequent Events – Notes Payable for details related to the subsequent extension of this note.

On April 6, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000, originally dated March 26, 2015, from March 26, 2016 to June 26, 2016. See Note 11 – Subsequent Events – Notes Payable for details related to the subsequent extension of this note.

On May 10, 2016, the Company issued a six-month note payable in the principal amount of \$53,000 which bears interest at 6% per annum, payable at maturity.

See Note 8 – Related Parties for details related to non-convertible notes held by the Company's Chief Executive Officer ("CEO") and a director of the Company. See Note 11 – Subsequent Events – Notes Payable for details related to the issuance and extension of notes payable subsequent to June 30, 2016.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 6 – Notes Payable – Continued

Convertible Notes

Other Convertible Notes

In January 2016, the Company issued a convertible note payable in the principal amount of \$250,000 to an investor who advanced the funds to the Company in January 2015. The note matures on July 27, 2016 and bears interest at a rate of 10% per annum, beginning from the date the funds were advanced. The note shall be automatically converted into shares of the Company's common stock upon the earlier of (i) the closing of an offering of equity securities pursuant to which the Company receives an aggregate of at least \$5,000,000 in gross proceeds ("Qualified Financing"); or (ii) the maturity date. In the event the note is converted upon the occurrence of a Qualified Financing (the "QF Conversion Shares"), the conversion price of the note shall be the lesser of (i) seventy percent (70%) of the price per share or per unit (assuming the unit includes one share of common stock or the price per unit divided by the number of shares of common stock underlying such unit) at which the Company sells its securities in a Qualified Financing; or (ii) the quotient obtained by dividing \$35,000,000 by the aggregate number of outstanding shares of the common stock, measured on a fully-diluted basis, excluding certain shares, on the date immediately preceding the Qualified Financing. The QF Conversion Shares shall be subject to a prohibition from any sale, pledge or transfer for a period of six (6) months from the date of the closing on which the Company generates aggregate gross proceeds under the Qualified Financing of at least \$5,000,000. In addition, upon conversion of the note following the occurrence of a Qualified Financing, the holder shall automatically receive five-year warrants to purchase that number of shares of common stock into which the note is convertible and such warrants shall have an exercise price equal to the lesser of (i) seventy percent (70%) of the price per share or per unit (assuming the unit includes one share of common stock or the price per unit divided by the number of shares of common stock underlying such unit) at which the Company sells its securities in a Qualified Financing; or (ii) \$0.75. In the event the note is automatically converted upon the maturity date, the conversion price of the note shall be equal to the quotient obtained by dividing \$20,000,000 by the aggregate number of outstanding shares of the common stock, measured on a fully-diluted basis, excluding certain shares, on the date immediately preceding the maturity date (the "Maturity Conversion Price"). In addition, in the event of an automatic conversion of the note upon the maturity date, the holder shall automatically receive five-year warrants to purchase that number of common stock into which the note is convertible and such warrants shall have an exercise price equal to the Maturity Conversion Price. In connection with the Company's sequencing policy, the conversion option of the note was determined to be a derivative liability. The \$179,000 issuance date fair value was recorded as a debt discount and will be amortized over the term of the note. See Note 4 – Fair Value for additional details.

10% Convertible Note Offering

During the six months ended June 30, 2016, the Company closed on an aggregate of \$390,000 in principal amount of convertible notes to investors (the "10% Convertible Notes"). The 10% Convertible Notes bear interest at a rate of 10% per annum and are payable eighteen (18) months from the date of issuance (the "Maturity Date"). The 10% Convertible Notes shall be automatically converted into shares of the Company's common stock upon the earlier of (i) the closing of an offering of equity securities pursuant to which the Company receives an aggregate of at least \$5,000,000 in gross proceeds ("Qualified Financing"); (ii) the closing of a strategic transaction (including but not limited to the Company's entry into a joint venture or partnership agreement or the sublicensing of the Company's intellectual property) pursuant to which the Company, directly or indirectly, receives, or expects to receive within eighteen months, cash, assets or other consideration with a total aggregate value of at least \$4,000,000 ("Strategic Transaction"); or (iii) the Maturity Date of the 10% Convertible Notes.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 6 – Notes Payable – Continued

Convertible Notes - Continued

10% Convertible Note Offering – Continued

In the event the 10% Convertible Notes are converted upon the occurrence of a Qualified Financing (the “QF Conversion Shares”), the conversion price of the 10% Convertible Notes shall be the lesser of (i) seventy percent (70%) of the price per share or per unit (assuming the unit includes one share of common stock or the price per unit divided by the number of shares of common stock underlying such unit) at which the Company sells its securities in a Qualified Financing; or (ii) \$0.75. The QF Conversion Shares shall be subject to a prohibition from any sale, pledge or transfer for a period of six (6) months from the date of the closing on which the Company generates aggregate gross proceeds under the Qualified Financing of at least \$5,000,000. In the event the 10% Convertible Notes are converted upon the occurrence of a Strategic Transaction (the “ST Conversion Shares”), the conversion price of the 10% Convertible Notes shall be equal to \$0.75. In addition, upon conversion of the 10% Convertible Notes following the occurrence of a Qualified Financing or a Strategic Transaction, each holder of a 10% Convertible Note shall automatically receive five-year warrants to purchase that number of shares of common stock into which the 10% Convertible Notes are convertible and such warrants shall have an exercise price equal to one hundred ten percent (110%) of the per-share or per unit (assuming the unit includes one share of common stock or the price per unit divided by the number of shares of common stock underlying such unit) at which the Company sells its securities in a Qualified Financing or \$0.825 in the case of a Strategic Transaction, as applicable. The ST Conversion Shares shall be subject to a prohibition from any sale, pledge or transfer for a period of six (6) months from the date of the closing of a Strategic Transaction. In the event the 10% Convertible Notes are automatically converted upon the Maturity Date, the conversion price of the 10% Convertible Notes shall be equal to the quotient obtained by dividing \$15 million by the aggregate number of outstanding shares of the common stock, measured on a fully-diluted basis, excluding certain shares, on the date immediately preceding the Maturity Date (the “Maturity Conversion Price”). In addition, in the event of an automatic conversion of the 10% Convertible Notes upon the Maturity Date, the holder shall automatically receive five-year warrants to purchase that number of common stock into which the 10% Convertible Notes are convertible and such warrants shall have an exercise price equal to the Maturity Conversion Price.

In connection with the Company’s sequencing policy, the conversion options of the notes were determined to be derivative liabilities. The \$327,700 aggregate issuance date fair value was recorded as a debt discount and will be amortized over the term of the notes. See Note 4 – Fair Value for additional details.

Summary

During the three and six months ended June 30, 2016, the Company recorded interest expense related to notes payable of \$55,232 and \$118,557, respectively. During the three and six months ended June 30, 2015, the Company recorded interest expense related to notes payable of \$5,277 and \$6,756, respectively.

During the three and six months ended June 30, 2016, the Company recorded amortization of debt discount of \$325,288 and \$598,676, respectively. During the three and six months ended June 30, 2015, the Company recorded amortization of debt discount of \$77,100 and \$79,500, respectively.

Note 7 – Advances Payable

See Note 6 – Notes Payable – Convertible Notes – Other Convertible Notes for details associated with the issuance of a note that previously was classified as an advance payable.

Note 8 – Related Parties

For the three and six months ended June 30, 2016, the Company recorded a charge to operations of \$199,000 and \$399,000, respectively, related to its research and license agreement with Yeda. For the three and six months ended June 30, 2015, the Company recorded a charge to operations of \$200,000 and \$400,000, respectively, related to its research and license agreement with Yeda. As of June 30, 2016 and December 31, 2015, approximately \$200,000 and \$208,000 has been accrued and is payable to Yeda, respectively.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 8 – Related Parties – Continued

On March 29, 2016, the Company exercised its option pursuant to an October 3, 2011 exclusive option agreement with Yeda, as amended, such that the Company is now in the process of negotiating an agreement with Yeda whereby the Company would exclusively license certain organ regeneration technology from Yeda. As a result of exercising the option, the Company will fund research with Yeda in the additional amount of \$100,000 per annum commencing during the third quarter of 2016. In addition, the Company shall pay Yeda an option initiation fee of \$200,000 (the “Option Initiation Fee”) on or before the date on which the Company shall have received, beginning from October 11, 2011, an aggregate investment in the amount of \$10,000,000.

During the six months ended June 30, 2016, the Company repaid a note payable in the principal amount of \$50,000 to the Company’s CEO.

On April 4, 2016, the Company extended the maturity date of a note payable to the Company’s CEO in the principal amount of \$50,000, originally dated November 26, 2014, from June 30, 2016 to September 30, 2016.

As of June 30, 2016 and December 31, 2015, there were outstanding notes payable to the Company’s CEO in the aggregate principal amount of \$50,000 and \$100,000, respectively. As of June 30, 2016 and December 31, 2015, there was an outstanding note payable to a director of the Company in the principal amount of \$100,000.

Note 9 – Commitments and Contingencies

Litigation

Certain conditions may exist as of the date the condensed consolidated financial statements are issued, which may result in a loss to the Company, but which will only be resolved when one or more future events occur or fail to occur. The Company assesses such contingent liabilities, and such assessment inherently involves an exercise of judgment. In assessing loss contingencies related to legal proceedings that are pending against the Company, or unasserted claims that may result in such proceedings, the Company evaluates the perceived merits of any legal proceedings or unasserted claims, as well as the perceived merits of the amount of relief sought or expected to be sought therein.

If the assessment of a contingency indicates that it is probable that a material loss has been incurred and the amount of the liability can be estimated, then the estimated liability would be accrued in the Company’s condensed consolidated financial statements. If the assessment indicates that a potentially material loss contingency is not probable, but is reasonably possible, or is probable but cannot be estimated, then the nature of the contingent liability and an estimate of the range of possible losses, if determinable and material, would be disclosed.

Loss contingencies considered remote are generally not disclosed, unless they involve guarantees, in which case the guarantees would be disclosed. There can be no assurance that such matters will not materially and adversely affect the Company’s business, financial position, and results of operations or cash flows. As of June 30, 2016 and December 31, 2015, the Company has not accrued any amounts for contingencies.

CELL SOURCE, INC. AND SUBSIDIARY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 10 – Stockholders' Deficiency

Stock-Based Compensation

During the three and six months ended June 30, 2016, the Company recognized \$23,092 and \$91,962 of stock-based compensation expense related to warrants. During the three and six months ended June 30, 2015, the Company recognized \$(23,500) and \$(33,400) of stock-based compensation expense related to warrants. As of June 30, 2016, there was \$92,686 of unrecognized stock-based compensation expense that will be recognized over approximately 1.0 years.

Note 11 – Subsequent Events

The Company evaluates events that have occurred after the balance sheet date but before the condensed consolidated financial statements are issued. Based upon the evaluation, the Company did not identify any recognized or non-recognized subsequent events that would require adjustment or disclosure in the condensed consolidated financial statements.

Notes Payable

Issuances

Subsequent to June 30, 2016, the Company issued six-month notes payable in the aggregate principal amount of \$300,000 which bear interest at a rate of 10% per annum, payable at maturity. In connection with the note issuances, the Company issued to the purchasers immediately-vested, five-year warrants to purchase an aggregate of 225,000 shares of common stock at an exercise price of \$0.75 per share.

Extensions

On July 20, 2016, the Company extended the maturity date of a note payable to a director of the Company in the principal amount of \$100,000 from July 20, 2016 to January 24, 2017. In connection with the extension, the Company issued to the holder an immediately vested, three-year warrant to purchase 50,000 shares of common stock at an exercise price of \$0.75 per share. In addition, in connection with the terms of the original note, because the principal amount of the note was not repaid by July 20, 2016, the Company issued to the holder an immediately vested, three-year warrant to purchase 10,000 shares of common stock at an exercise price of \$0.75 per share and shall pay a cash penalty of \$5,000 to the holder.

On July 22, 2016, the Company extended the maturity date of convertible notes payable in the aggregate principal amount of \$145,000 from July 24, 2016 to January 24, 2017. In connection with the extension, the Company issued immediately vested, three-year warrants to purchase an aggregate of 72,500 shares of common stock at an exercise price of \$0.75 per share.

On August 10, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000 from June 30, 2016 to September 30, 2016. In connection with the extension, the Company issued to the holder 250,000 shares of immediately vested common stock.

On August 10, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000 from June 27, 2016 to September 26, 2016. In connection with the extension, the Company issued to the holder 250,000 shares of immediately vested common stock. The note will become payable in full in the event that the Company raises \$2.5 million or more of funding in its private placement. Furthermore, in the event the Company raises \$3.0 million or more of funding, the holder's note issued in October 2015 in the original principal amount of \$125,000 shall become payable in full.

On August 10, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000 from June 26, 2016 to September 26, 2016. In connection with the extension, the Company issued to the holder 250,000 shares of immediately vested common stock. The note will become payable in full in the event that the Company raises \$2.5 million or more of funding in its private placement. Furthermore, in the event the Company raises \$3.0 million or more of funding, the advance of \$100,000 made to the Company by the investor in January 2015 shall become payable in full as well as at least \$15,000 of interest.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of the consolidated results of operations and financial condition of Cell Source, Inc. ("CSI", "Cell Source" or the "Company") as of June 30, 2016 and December 31, 2015 and for the three and six months ended June 30, 2016 and 2015 should be read in conjunction with our condensed consolidated financial statements and the notes thereto that are included elsewhere in this Quarterly Report on Form 10-Q. References in this Management's Discussion and Analysis of Financial Condition and Results of Operations to "us," "we," "our," and similar terms refer to CSI. This Quarterly Report contains forward-looking statements as that term is defined in the federal securities laws. The events described in forward-looking statements contained in this Quarterly Report may not occur. Generally these statements relate to business plans or strategies, projected or anticipated benefits or other consequences of our plans or strategies, projected or anticipated benefits from acquisitions to be made by us, or projections involving anticipated revenues, earnings or other aspects of our operating results. The words "may," "will," "expect," "believe," "anticipate," "project," "plan," "intend," "estimate," and "continue," and their opposites and similar expressions, are intended to identify forward-looking statements. We caution you that these statements are not guarantees of future performance or events and are subject to a number of uncertainties, risks and other influences, many of which are beyond our control, which may influence the accuracy of the statements and the projections upon which the statements are based. Factors that may affect our results include, but are not limited to, the risks and uncertainties discussed in Item 1A ("Risk Factors") of our Annual Report on Form 10-K for the year ended December 31, 2015 filed with the Securities and Exchange Commission (the "SEC") on April 14, 2016.

Overview

Our wholly-owned subsidiary, Cell Source Israel was founded in 2011 as a privately held company located in Tel Aviv, Israel. Our business is based on over ten (10) years of prominent research at the Weizmann Institute from whom we license patented and patent pending technology. Our exclusive, world-wide license provides us with access to certain discoveries, inventions and other intellectual property generated by Professor Yair Reisner, formerly Head of the Immunology Department at the Weizmann Institute, together with others. Professor Reisner leads a team at the Weizmann Institute to continue the development of these technologies in order to facilitate the transition of those technologies from the laboratory to clinical trials. Our Scientific Advisory Board is chaired by Dr. Terry Strom, Professor of Medicine and Surgery at Harvard Medical School and Director of The Transplant Institute at Beth Israel Deaconess Medical Center, the founding President of the American Society of Transplantation, from which he received a Lifetime Achievement Award, and past President of the Clinical Immunology Society. Its other members include Dr. Robert Negrin, Director of Bone and Marrow Transplantation and Professor of Medicine at Stanford University who is a past President of the American Society of Bone and Marrow Transplantation and the International Society of Cellular Therapy; Dr. Steven Burakoff, Director of the Tisch Cancer Institute at Mount Sinai Medical Center, Professor of Cancer Medicine at the Icahn School of Medicine, past Professor of Medicine at Harvard Medical School and Director of the NYU Cancer Institute, who won the American Association of Immunologists Lifetime Achievement Award; Dr. Herman Waldman, Department Head and Professor Emeritus of Pathology and Head of the Therapeutic Immunology Group at Oxford Medical School, former Cambridge Immunology Professor and SCRIP Lifetime Achievement Award winner; and Dr. Hermann Einsele, Professor and Director of Internal Medicine at Julius Maximilian University, Würzburg, Germany, a former visiting professor at the Fred Hutchinson Cancer Research Center in Seattle, Director of the German and member of the European Blood and Marrow Transplantation Groups.

Our lead prospective product is our patented Veto Cell immune system management technology, which is an immune tolerance biotechnology that enables the selective blocking of immune responses. The Company's target indications include: lymphoma, multiple myeloma and BCLL (a form of leukemia), facilitating transplantation acceptance (initially bone marrow transplantation and subsequently organ transplantation), and ultimately treating a variety of non-malignant diseases.

Cell Source, under its exclusive license with Yeda Research & Development Ltd., the commercial arm of the Weizmann Institute of Science, has recently filed two new provisional patent applications that extend the usage of Veto Cell technology as a critical enabler for other cell therapy treatments. One patent application highlights, based on preclinical data, the ability of Veto Cells to accompany other cell therapy treatments and help them overcome rejection and avoid Graft vs. Host Disease (GvHD) in an allogeneic (using a third party donor) treatment setting. The other patent application involves a genetically modified Veto Cell that can have sustained survival in the patient's body while avoiding rejection and GvHD. Both of these applications holds the potential to make CAR-T cells, which to date been effective primarily in an autologous (patient's own cells) setting, succeed in an allogeneic setting.

Cell Source is actively exploring collaborations with larger biopharmaceutical firms where Veto Cell technology can significantly enhance the efficacy of cell therapy treatments for a variety of indications. This may allow Cell Source to complement the development of its own treatment candidates with parallel development with partners, thus multiplying the potential impact of this technology in the clinic.

Prior to commercializing its products, the Company must conduct human clinical trials and obtain FDA approval and/or approvals from comparable foreign regulatory authorities.

Generally speaking, as a preclinical biotechnology firm, Cell Source needs to go through several necessary steps in order to commercialize its products and commence revenue generation. These steps are per product, but can run in parallel for multiple products, which are each in different stages of the development “pipeline”, so that, for example, when a certain product is already in a human clinical trial, another product may still be in preclinical development and a third may be awaiting regulatory approval to commence human trials. These can also take place in parallel, and varied stages, for the same product in different geographic jurisdictions. The typical steps per product (and range of time frame for each) are:

1. Complete development of human treatment protocol (2-5 years)
2. Apply for and receive approval to commence human trials (9-18 months)
3. Recruit patients (1-6 months)
4. Conduct Phase I trials showing safety of product (1-2 years)
5. Apply for and receive approval to conduct trials showing product efficacy (6-12 months)
6. Data collecting and analysis (6-12 months)
7. Conduct Phase II efficacy trials (2-3 years)
8. Data collecting and analysis (6-12 months)
9. Apply for and receive approval to conduct trials showing efficacy in larger numbers of patients (6-12 months)
10. Conduct Phase III efficacy trials with larger numbers of patients (2-4 years)
11. Data collecting and analysis (6-12 months)
12. Apply for and receive approval for production scale manufacturing facilities (6-12 months)
13. Contract third party or establish own production facilities (6-30 months)
14. Contract third party or establish own distribution platform (6-18 months)
15. Commence manufacturing and distribution (6-12 months)

Please note that steps 12-15 can be conducted in parallel with some of the steps above. In the case of Cell Source and other firms that treat terminal patients with either rare diseases or those for which there is currently no effective treatment, or where preclinical studies indicate a reasonable expectation to increase life expectancy and survival rates by a substantive margin, several of these steps can be combined and or shortened, subject to regulatory discretion. For example, Phase I and II (safety and efficacy) can be combined in a single concurrent step; approvals for subsequent steps can be accelerated; in some countries patients can already be treated commercially after the end of Phase II, foregoing the requirement for Phase III data as a prerequisite.

Although we have provided estimated timeframes for each step above, no assurances can be made that such timeframes are accurate or that they would not be delayed for one or more reasons. At any stage of a human clinical trial, there could be problems with either safety or efficacy of treatment. In these instances the Company could be required to reformulate the treatment and proceed with additional patients, which could involve a delay of months or years, depending on whether we would have to seek approval from the very beginning of the approval process. There can also be a delay of up to 1 to 2 years between phases of a human clinical trial, as the regulator may wish to take additional time to review the approval of a subsequent stage. Furthermore, if a significant modification to the treatment is required, the application process begins again from the very first stage. If the treatment is not effective at all or if it’s harmful to patients, even after modifications are made, it is possible that the trials may be halted completely and the product candidates permanently withdrawn. While the timescales presented here are representative of the typical experience, there is no assurance that there will not be significant delays at any stage or step in the process or a complete failure of trials.

The specific detailed next steps the Company must take to get the treatments or products to market include the following:

We have not submitted any drug applications to the FDA and do not have anything pending for approval with the FDA. Cell Source itself has not had any contact with any regulator anywhere regarding treatment approvals or clinical trials associated with regulatory approvals. We are aware that a hospital in Italy in May, 2014 independently requested and in September, 2014 received approval to conduct a trial with the same protocol that we plan to use, but we are not mentioned in the application nor in the approval. However, we may indirectly benefit from the outcome of the trial, if successful, although we are not the sponsor of this trial. There are no written or verbal agreements between the hospital and Cell Source regarding the use of the technology. That said, Cell Source is aware and in favor of the hospital plans to use the technology and would of course find a positive initial outcome encouraging. Since the treatment is being done on compassionate grounds as a non-commercial clinical trial, there is no legal requirement for the hospital to obtain approval to use the treatment protocol. The hospital has successfully treated a cancer patient using the Megadose Drug Combination technology that Cell Source exclusively licenses from Yeda Research & Development Ltd., commercial arm of the Weizmann Institute of Science. While Cell Source is not a sponsor of the trial, the results provide a positive initial indication with respect to the technology. The patient received a bone marrow transplantation from a haploidentical or “mismatched” donor under a reduced intensity conditioning regimen (i.e., a relatively low level of immune suppression treatment). There was successful initial engraftment of the transplantation in the absence of GVHD.

For the Veto Cell application for reducing rejection in Bone Marrow Transplants, Cell Source expects to commence Phase I/II human clinical trials in the US and EU starting sometime in 2017. Cell Source anticipates that Phase I/II studies will last until 2019 or 2020. These would be followed by completion of Phase II and Phase III, which would last another 2-3 years each, so that full approval, if successful, would be expected sometime in 2025. In Germany there is a possibility of approval for commercial use on a “compassionate grounds” basis at the end of Phase II, which could take place by 2023. In the US, Cell Source plans to commence the IND approval process with the FDA in 2017, which could last until between 2021 and 2024. Cell Source also aspires to enter into a collaboration with respect to combining CAR-T cell therapy with Veto Cell therapy and commence pre-clinical proof of concept trials in 2016. If successful, this could lead to a commencement of a combined FDA trial in 2017 or 2018 and could last until 2025 or 2026.

It is possible that Cell Source treatments could qualify for any or all of Fast Track, Breakthrough Therapy, Accelerated Approval and Priority Review designation under the FDA, which would hasten their approval if successful.

The costs for each step of development, in terms of clinical trials, are delineated below:

Cell Source estimates the cost of clinical trials alone to be up to \$5-10 million in each of the coming two years and another \$25-50 million in order to reach commercialization for both the Anti-rejection Veto Cell and the Veto Cell + CAR-T cell products. This would mean that Cell Source will need to secure one or more significant capital infusions in order to reach the point that meaningful revenues could be generated.

Cell Source will require additional financing for any and all of the steps described above.

Recent Developments

On May 10, 2016, the Company issued a six-month notes payable in the principal amount of \$53,000 which bears interest at 6% per annum, payable at maturity. The foregoing description of the six-month promissory note does not purport to be complete and is qualified in its entirety by reference to the complete text of the note which is filed as Exhibit 10.1 hereto, which is incorporated herein by reference.

Subsequent to June 30, 2016, the Company issued six-month notes payable in the aggregate principal amount of \$300,000 which bear interest at a rate of 10% per annum, payable at maturity. In connection with the note issuances, the Company issued to the purchasers immediately-vested, five-year warrants to purchase an aggregate of 225,000 shares of common stock at an exercise price of \$0.75 per share.

On July 20, 2016, the Company extended the maturity date of a note payable to a director of the Company in the principal amount of \$100,000 from July 20, 2016 to January 24, 2017. In connection with the extension, the Company issued to the holder an immediately vested, three-year warrant to purchase 50,000 shares of common stock at an exercise price of \$0.75 per share. In addition, in connection with the terms of the original note, because the principal amount of the note was not repaid by July 20, 2016, the Company issued to the holder an immediately vested, three-year warrant to purchase 10,000 shares of common stock at an exercise price of \$0.75 per share and shall pay a cash penalty of \$5,000 to the holder.

On July 22, 2016, the Company extended the maturity date of convertible notes payable in the aggregate principal amount of \$145,000 from July 24, 2016 to January 24, 2017. In connection with the extension, the Company issued immediately vested, three-year warrants to purchase an aggregate of 72,500 shares of common stock at an exercise price of \$0.75 per share.

On August 10, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000 from June 30, 2016 to September 30, 2016. In connection with the extension, the Company issued to the holder 250,000 shares of immediately vested common stock.

On August 10, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000 from June 27, 2016 to September 26, 2016. In connection with the extension, the Company issued to the holder 250,000 shares of immediately vested common stock. The note will become payable in full in the event that the Company raises \$2.5 million or more of funding in its private placement. Furthermore, in the event the Company raises \$3.0 million or more of funding, the holder’s note issued in October 2015 in the original principal amount of \$125,000 shall become payable in full.

On August 10, 2016, the Company extended the maturity date of a note payable in the principal amount of \$250,000 from June 26, 2016 to September 26, 2016. In connection with the extension, the Company issued to the holder 250,000 shares of immediately vested common stock. The note will become payable in full in the event that the Company raises \$2.5 million or more of funding in its private placement. Furthermore, in the event the Company raises \$3.0 million or more of funding, the advance of \$100,000 made to the Company by the investor in January 2015 shall become payable in full as well as at least \$15,000 of interest.

Consolidated Results of Operations

Three Months Ended June 30, 2016 Compared to Three Months Ended June 30, 2015

The following table presents selected items in our unaudited condensed consolidated statements of operations for the three months ended June 30, 2016 and 2015, respectively:

	For The Three Months Ended June 30,	
	2016	2015
Revenues	\$ -	\$ -
Operating Expenses		
Research and development	110,167	124,472
Research and development - related party	198,820	200,000
Selling, general and administrative	221,179	243,261
Total Operating Expenses	<u>530,166</u>	<u>567,733</u>
Loss From Operations	<u>(530,166)</u>	<u>(567,733)</u>
Other Income (Expense)		
Change in fair value of derivative liabilities	209,900	79,200
Interest expense	(55,232)	(5,277)
Amortization of debt discount	(325,288)	(77,100)
Total Other Expense	<u>(170,620)</u>	<u>(3,177)</u>
Net Loss	<u>\$ (700,786)</u>	<u>\$ (570,910)</u>

Research and Development

Research and development expense remained relatively unchanged as compared to the prior period, as it was \$308,987 and \$324,472 for the three months ended June 30, 2016 and 2015, respectively, a decrease of \$15,485, or 5%.

Selling, General and Administrative

Selling, general and administrative expense was \$221,179 and \$243,261 for the three months ended June 30, 2016 and 2015, respectively, a decrease of \$22,082, or 9%. The decrease was primarily due to a reduction in payroll due to reduced headcount as compared to the prior period.

Change in Fair Value of Derivative Liability

The change in fair value of derivative liability for the three months ended June 30, 2016 and 2015 was a gain of \$209,900 and \$79,200, respectively, which represents the change in fair value of the warrants that were deemed to be derivative liabilities during the respective periods.

Interest Expense

Interest expense was \$55,232 and \$5,277 for the three months ended June 30, 2016 and 2015, respectively, an increase of \$49,955, or 947%. The increase was due to the issuance of new notes payable subsequent to June 30, 2015 with interest rates ranging from 6% - 10%.

Amortization of Debt Discount

Amortization of debt discount was \$325,288 and \$77,100 for the three months ended June 30, 2016 and 2015, respectively, an increase of \$248,188 or 322%. The increase was primarily due to costs associated with warrants and conversion options issued in connection with notes payable and the costs incurred in connection with our debt offerings.

Six Months Ended June 30, 2016 Compared to Six Months Ended June 30, 2015

The following table presents selected items in our unaudited condensed consolidated statements of operations for the six months ended June 30, 2016 and 2015, respectively:

	For The Six Months Ended June 30,	
	2016	2015
Revenues	\$ -	\$ -
Operating Expenses		
Research and development	223,588	177,219
Research and development - related party	398,820	400,000
Selling, general and administrative	<u>552,437</u>	<u>576,778</u>
Total Operating Expenses	<u>1,174,845</u>	<u>1,153,997</u>
Loss From Operations	<u>(1,174,845)</u>	<u>(1,153,997)</u>
Other Income (Expense)		
Change in fair value of derivative liabilities	370,850	112,700
Interest expense	(118,557)	(6,756)
Amortization of debt discount	<u>(598,676)</u>	<u>(79,500)</u>
Total Other (Expense) Income	<u>(346,383)</u>	<u>26,444</u>
Net Loss	<u>\$ (1,521,228)</u>	<u>\$ (1,127,553)</u>

Research and Development

Research and development expense was \$622,408 and \$577,219 for the six months ended June 30, 2016 and 2015, respectively, an increase of \$45,189, or 8%, primarily associated with increased expenses associated with key patents.

Selling, General and Administrative

Selling, general and administrative expense was \$552,437 and \$576,778 for the six months ended June 30, 2016 and 2015, respectively, a decrease of \$24,341, or 4%.

Change in Fair Value of Derivative Liability

The change in fair value of derivative liability for the six months ended June 30, 2016 and 2015 was a gain of \$370,850 and \$112,700, respectively, which represents the change in fair value of the warrants that were deemed to be derivative liabilities during the respective periods.

Interest Expense

Interest expense was \$118,557 and \$6,756 for the six months ended June 30, 2016 and 2015, respectively, an increase of \$111,801, or 1,655%. The increase was due to the issuance of new notes payable subsequent to June 30, 2015 with interest rates ranging from 6% - 10%.

Amortization of Debt Discount

Amortization of debt discount was \$598,676 and \$79,500 for the six months ended June 30, 2016 and 2015, respectively, an increase of \$519,176 or 653%. The increase was primarily due to costs associated with warrants and conversion options issued in connection with notes payable and the costs incurred in connection with our debt offerings.

Liquidity and Going Concern

We measure our liquidity in a number of ways, including the following:

	June 30, 2016 (unaudited)	December 31, 2015
Cash	\$ 3,736	\$ 6,944
Working capital deficiency	\$ (7,068,800)	\$ (5,711,374)

We have not generated any revenues since our inception, we have recurring net losses, we have a working capital deficiency as of June 30, 2016 of approximately \$7,069,000 and we have used cash in operations of approximately \$952,000 and \$1,114,000 during the six months ended June 30, 2016 and 2015, respectively. These conditions raise substantial doubt about our ability to continue as a going concern. Based on our current resources, we will not be able to continue to operate without additional immediate funding.

Our ability to continue our operations is dependent on the execution of management's plans, which include the raising of capital through the debt and/or equity markets, until such time that funds provided by operations are sufficient to fund working capital requirements. We may need to incur additional liabilities with certain related parties to sustain our existence. If we were not to continue as a going concern, we would likely not be able to realize our assets at values comparable to the carrying value or the fair value estimates reflected in the balances set out in the preparation of our financial statements.

There can be no assurances that we will be successful in generating additional cash from equity or debt financings or other sources to be used for operations. Should we not be successful in obtaining the necessary financing to fund our operations, we would need to curtail certain or all operational activities and/or contemplate the sale of our assets, if necessary.

During the six months ended June 30, 2016 and 2015, our sources and uses of cash were as follows:

Net Cash Used in Operating Activities

We experienced negative cash flows from operating activities for the six months ended June 30, 2016 and 2015 in the amounts of \$951,633 and \$1,114,304, respectively. The net cash used in operating activities for the six months ended June 30, 2016 was primarily due to cash used to fund a net loss of \$1,521,228, adjusted for net non-cash expenses in the aggregate amount of \$320,218, partially offset by \$249,377 of net cash provided by changes in the levels of operating assets and liabilities. The net cash used in operating activities for the six months ended June 30, 2015 was primarily due to cash used to fund a net loss of \$1,127,553, adjusted for net non-cash credits in the aggregate amount of \$66,170, partially offset by \$79,419 of net cash provided by changes in the levels of operating assets and liabilities.

Net Cash Provided by Financing Activities

Net cash provided by financing activities for the six months ended June 30, 2016 and 2015 was \$948,425 and \$1,200,000, respectively. The net cash provided by financing activities during the six months ended June 30, 2016 was attributable to \$1,043,000 of proceeds from the issuance of notes payable, partially offset by repayments of \$50,000 of notes payable and \$44,575 of debt issuance costs. The net cash provided by financing activities during the six months ended June 30, 2015 was attributable to \$750,000 of proceeds from the issuance of notes payable and \$450,000 of proceeds received in connection with a convertible note offering prior to closing.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements.

Critical Accounting Policies and Estimates

There are no material changes from the critical accounting policies set forth in "Management's Discussion and Analysis of Financial Condition and Results of Operations" of our Annual Report on Form 10-K which was filed with the Securities and Exchange Commission ("SEC") on April 14, 2016. Please refer to that document for disclosures regarding the critical accounting policies related to our business.

Recent Accounting Standards

In March 2016, the Financial Accounting Standards Board issued Accounting Standard Update No. 2016-09, "Compensation – Stock Compensation (Topic 718)" ("ASU 2016-09"). ASU 2016-09 requires an entity to simplify several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, with early adoption permitted. We are currently evaluating ASU 2016-09 and its impact on our condensed consolidated financial statements or disclosures.

We have evaluated all new accounting standards that are in effect and may impact our condensed consolidated financial statements and do not believe that there are any other new accounting standards that have been issued that might have a material impact on our financial position or results of operations.

Item 3. Quantitative And Qualitative Disclosures About Market Risk.

Not applicable.

Item 4. Controls and Procedures.

Disclosure Controls and Procedures

Disclosure controls are procedures that are designed with the objective of ensuring that information required to be disclosed in our reports filed under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), such as this Quarterly Report, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls are also designed with the objective of ensuring that such information is accumulated and communicated to our management, including the Principal Executive and Financial Officer, Itamar Shimrat, as appropriate to allow timely decisions regarding required disclosure. Internal controls are procedures which are designed with the objective of providing reasonable assurance that (1) our transactions are properly authorized, recorded and reported; and (2) our assets are safeguarded against unauthorized or improper use, to permit the preparation of our condensed consolidated financial statements in conformity with United States generally accepted accounting principles.

In connection with the preparation of this Quarterly Report on Form 10-Q for the quarter ended June 30, 2016, management, with the participation of our Principal Executive and Financial Officer, Itamar Shimrat, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e) and 15d-15(e)). Based upon that evaluation, our Principal Executive and Financial Officer concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective.

Changes in Internal Controls

There have been no changes in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Rule 13a-15 or 15d-15 under the Exchange Act that occurred during the quarter ended June 30, 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Limitations of the Effectiveness of Control

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations of any control system, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings.

We are not currently a party to any material legal proceedings.

Item 1A. Risk Factors.

There have been no material changes to the risk factors discussed in Item 1A. Risk Factors in our Annual Report on Form 10-K which was filed with the Securities and Exchange Commission on April 14, 2016.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

None.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

The information contained in Part II. Item 2. above is incorporated herein by reference.

Item 6. Exhibits.

Exhibit Number		Description
10.1	*	Form of May 2016 Note
31.1	*	Certificate of the Chief Executive Officer
31.2	*	Certificate of the Chief Financial Officer
32	**	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS	*	XBRL Instance Document
101.SCH	*	XBRL Schema Document
101.CAL	*	XBRL Calculation Linkbase Document
101.DEF	*	XBRL Definition Linkbase Document
101.LAB	*	XBRL Label Linkbase Document
101.PRE	*	XBRL Presentation Linkbase Document

* Filed herewith

** This certification is being furnished and shall not be deemed "filed" with the SEC for purposes of Section 18 of the Exchange Act, or otherwise be subject to the liability of that section, and shall not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent that the registrant specifically incorporates it by reference.

SIGNATURES

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

CELL SOURCE, INC.

Dated: August 15, 2016

By: /s/ Itamar Shimrat
Name: Itamar Shimrat
Title: Chief Executive Officer and
Chief Financial Officer (Principal
Executive, Financial and Accounting
Officer)

PROMISSORY NOTE

US\$53,000

May 10, 2016

All references in this Note to monies are to U.S. Dollars

1. **Promise to Pay.** In exchange for the sum of \$53,000 (net of wire transfer fees) which CELL SOURCE INC., a Nevada Corporation ("Maker") received from Main Street Restaurant Associates Inc. ("Holder") on the date hereof, Maker promises to pay as set forth in this Promissory Note ("Note") Holder, the principal sum of \$53,000 (the "Principal Amount").

2. **Payment.** All amounts payable here under shall be paid in lawful money of the United States by certified check or wire transfer. Maker may repay all or any portion of the unpaid principal amount of this Note without any premium or penalty. The unpaid principal and accrued interest under this Note shall become all due and payable on November 10, 2016 (the "Maturity Date"). This Note shall bear interest at the rate of 6% per annum.

3. **Notices.** Any demand, notice or other communication to be given in connection with this Note shall be given in writing and shall be given by personal delivery, by registered mail or by electronic means of communication addressed to the recipient as follows:

To the Holder: Main Street Restaurant Associates Inc.
244 Main Street
Worcester MA, Bnei Brak, 01608-1202
Email: ligorsubash@gmail.com

To Maker: Cell Source, Inc.
5 Kineret Street
Bnei Brak, Israel 5126237
Attention: Itamar Shimrat
Email: ishimrat@cell-source.com

or to such other address, individual or electronic communication number as may be designated by notice given by either party to the others in accordance herewith. Any demand, notice or other communication given by personal delivery shall be conclusively deemed to have been given on the day of actual delivery thereof and, if given by registered mail, on the 5th day following the deposit thereof in the mail and, if given by electronic communication, on the day of transmittal (with receipt confirmed) thereof. If the party giving any demand, notice or other communication knows or ought reasonably to know of any difficulties with the postal system which might affect the delivery of mail, any such demand, notice or other communication shall not be mailed but shall be given by personal delivery or by electronic communication.

4. **Amendments.** Any provision of this Note may be amended only with the written consent of Maker and the Holder. Any amendment effected in accordance with this Section 4 shall be binding upon Maker and the Holder and their permitted assigns and successors.

5. **No Right of Set Off.** Maker shall have no right of set off or counterclaim with respect to the monies owing hereunder, and Maker hereby waive presentment; protest and notice of every kind and waives any defenses based upon indulgences, which may be granted by the Holder to Maker.

7. **Jury Waiver.** The Holder and Maker hereby waive the right to any jury trial in any action, proceeding, or counterclaim brought by either Holder or Maker against the other.

8. **Governing Law.** This Note will be governed by the laws of the State of New York without regard to its conflicts of law provisions.

MAKER:

HOLDER:

CELL SOURCE, INC.

MAIN STREET RESTAURANT ASSOCIATES INC.

By: _____
Name: Itamar Shimrat
Title: CEO

By: _____
Name: Ligor Shubashi
Title: Secretary

CERTIFICATIONS UNDER SECTION 302

I, Itamar Shimrat, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Cell Source, Inc.;
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(s) 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - 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(s) 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: August 15, 2016

/s/ Itamar Shimrat

Itamar Shimrat
Chief Executive Officer and Chief Financial Officer
(Principal Executive Officer)

CERTIFICATIONS UNDER SECTION 302

I, Itamar Shimrat, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Cell Source, Inc.;
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(s) 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - 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(s) 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: August 15, 2016

/s/ Itamar Shimrat

Itamar Shimrat
Chief Executive Officer and Chief Financial Officer
(Principal Financial Officer)

CERTIFICATIONS UNDER SECTION 906

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), each of the undersigned officers of Cell Source, Inc., a Nevada corporation (the “Company”), does hereby certify, to such officer’s knowledge, that:

The Quarterly Report for the quarter ended June 30, 2016 (the “Form 10-Q”) of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 15, 2016

By: /s/ Itamar Shimrat
Itamar Shimrat
Chief Executive Officer and Chief Financial Officer
(Principal Executive and Financial Officer)
