

NEPHROS INC  
Form DEF 14A  
April 14, 2014

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**SCHEDULE 14A**

**Proxy Statement Pursuant to Section 14(a) of the**

**Securities Exchange Act of 1934**

Filed by the Registrant ..

Filed by a Party other than the Registrant ..

Check the appropriate box:

Preliminary Proxy Statement

**Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Under Rule 14a-12

**NEPHROS, INC.**

**(Name of Registrant as Specified In Its Charter)**

**(Name of Person(s) Filing Proxy Statement, if other than the Registrant)**

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

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.. Fee paid previously with preliminary materials.

Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

**Notice Date: April 11, 2014**

**Nephros, Inc.**

**41 Grand Avenue**

**River Edge, New Jersey 07661**

**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**

**To Be Held Friday, May 16, 2014**

**To The Stockholders of Nephros, Inc.:**

The Annual Meeting of Stockholders of Nephros, Inc., a Delaware corporation, will be held at the offices of Day Pitney LLP, One Jefferson Road, Parsippany, New Jersey, on Friday, May 16, 2014 at 10:00 a.m., Eastern Time, for the following purposes:

- to elect the two Directors named in this proxy statement to serve three-year terms expiring in 2017;
- to ratify the selection of Rothstein Kass as our independent registered public accounting firm for the fiscal year ending December 31, 2014;
- the approval of the compensation of our named executive officers on an advisory (non-binding) basis;
- the frequency of the advisory vote to approve the compensation of our named executive officers on an advisory (non-binding) basis; and
- to act upon such other matters as may properly come before the meeting or any adjournment thereof.

These matters are more fully described in the attached proxy statement.

The Board of Directors has fixed the close of business on April 8, 2014 as the record date for the determination of stockholders entitled to notice of and to vote at the meeting or any adjournment thereof. We cordially invite you to attend the meeting in person. However, to assure your representation at the meeting, please mark, sign, date and return the enclosed proxy as promptly as possible in the enclosed postage-prepaid envelope. If you attend the meeting, you

may vote in person even if you returned a proxy.

Our proxy statement and proxy are enclosed, along with our Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

**IMPORTANT — YOUR PROXY IS ENCLOSED**

**Whether or not you plan to attend the meeting, please execute and promptly return the enclosed proxy in the enclosed envelope. No postage is required for mailing in the United States.**

By Order of the Board of Directors

John C. Houghton  
*President, Chief Executive Officer  
and Acting Chief Financial Officer*

**IMPORTANT NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS FOR THE ANNUAL MEETING OF STOCKHOLDERS TO BE HELD ON MAY 16, 2014:** Copies of this proxy statement and our Annual Report on Form 10-K for the 2013 fiscal year are available at: <http://www.nephros.com/SEC.html>.

**Nephros, Inc.**

**41 Grand Avenue**

**River Edge, New Jersey 07661**

**PROXY STATEMENT**

**ANNUAL MEETING OF STOCKHOLDERS**

**FRIDAY, MAY 16, 2014**

**INFORMATION CONCERNING SOLICITATION AND VOTING**

The enclosed proxy is solicited by the Board of Directors of Nephros, Inc., a Delaware corporation, for use at our Annual Meeting of Stockholders to be held at the offices of Day Pitney LLP, One Jefferson Road, Parsippany, New Jersey, on Friday, May 16, 2014 at 10:00 a.m., Eastern Time, and any adjournment thereof.

The mailing address of our principal executive offices is 41 Grand Avenue, River Edge, New Jersey 07661.

**Stockholders Entitled to Vote**

Only the holders of record of our common stock at the close of business on the record date, April 8, 2014, are entitled to notice of and to vote at the meeting. On the record date, 25,225,704 shares of our common stock were outstanding. Stockholders are entitled to one vote for each share of common stock held on the record date.

## **Mailing of Proxy Statement and Form of Proxy**

This proxy statement and accompanying proxy card are being mailed to stockholders on or about April 15, 2014. This proxy statement contains important information for you to consider when deciding how to vote on matters brought before the meeting. Please read it carefully. Our Annual Report on Form 10-K for the 2013 fiscal year is being mailed to stockholders together with this proxy statement. When more than one holder of our common stock shares the same address, we may deliver only one annual report and one proxy statement to that address unless we have received contrary instructions from one or more of the stockholders.

## **Voting**

Our Board of Directors is asking for your proxy. Giving us your proxy means that you authorize us to vote your shares in the manner you direct in the proxy at our Annual Meeting of Stockholders to be held at the offices of Day Pitney LLP, One Jefferson Road, Parsippany, New Jersey, on Friday, May 16, 2014 at 10:00 a.m., Eastern Time, and any adjournment thereof.

You may vote for or withhold your vote from our director candidates. The election of the nominees for director requires a plurality of votes cast. Accordingly, abstentions and broker “non-votes” (that is, proxies from brokers or nominees indicating that such persons have not received instructions from the beneficial owner or other persons entitled to vote shares on a particular matter with respect to which brokers or nominees do not have discretionary power) will not affect the outcome of the election.

No broker may vote on the proposal to elect the director nominees named in this proxy statement without your specific instructions.

You may vote for or against or abstain from voting for the proposals to ratify the appointment by the Audit Committee of our independent registered public accounting firm for the fiscal year ending December 31, 2014 and to approve the compensation of our named executive officers. The affirmative vote of a majority of the shares of common stock represented and entitled to vote at the annual meeting is required for approval of these matters. For the proposal regarding the frequency of future advisory votes on executive compensation, the choice receiving the highest number of votes cast will be considered by the Board as the expected preference of stockholders. The vote for the approval of the compensation of our named executive officers and the vote for the frequency of future advisory votes on executive compensation is on an advisory basis and is therefore non-binding. On these matters, abstentions will have the same effect as a negative vote. However, because broker non-votes will not be treated as shares that are present and entitled to vote with respect to a specific proposal, broker non-votes will have no effect on the outcome of these matters.

When the enclosed proxy is properly executed and returned (and not subsequently properly revoked, as described below), the shares it represents will be voted in accordance with the directions indicated thereon, or, if no direction is indicated thereon, it will be voted:

- (1) FOR the election of the Class III Director nominees named herein;
- (2) FOR the ratification of the selection of Rothstein Kass as our independent registered public accounting firm for the fiscal year ending December 31, 2014;
- (3) FOR the approval of the compensation of our named executive officers;
- (4) 2 YEARS as the frequency with which we should conduct an advisory vote to approve the compensation of our named executive officers; and
- (5) in the discretion of the proxies, with respect to any other matters properly brought before the stockholders at the meeting.

#### **Quorum**

A majority of the voting power of the outstanding shares entitled to vote at the meeting shall constitute a quorum, whether present in person or by proxy. In accordance with Delaware law, broker non-votes, abstentions and votes withheld from any director will be counted for purposes of determining the presence or absence of a quorum for the transaction of business.

### **Record and Beneficial Shareholdings**

You may receive more than one proxy or voting card depending on how you hold your shares. Shares registered in your name are covered by one card. If you hold shares through someone else, such as a stockbroker, you may receive material from them asking how you want to vote those shares.

### **Solicitation of Proxies**

We will bear the cost of soliciting proxies. In addition to solicitation of proxies by mail, our employees, without extra remuneration, may solicit proxies personally or by telephone. We will reimburse brokerage firms and other custodians, nominees and fiduciaries for their reasonable out-of-pocket expenses for forwarding proxy materials to beneficial owners and seeking instruction with respect thereto.

### **Revoking a Proxy**

You may revoke your proxy by sending in a new proxy card with a later date or by sending written notice of revocation to our President, Chief Executive Officer and Acting Chief Financial Officer, John C. Houghton, at our principal executive offices. If you attend the meeting, you may revoke in writing previously submitted proxies and vote in person.

### **Attending in Person**

Only stockholders, their proxy holders and our guests may attend the meeting. If you want to vote in person at the annual meeting, and you hold your shares through a securities broker (that is, in “street name”), then you must obtain a proxy from your broker and bring that proxy to the meeting.



## **PROPOSAL NO. 1 — ELECTION OF DIRECTORS**

At the annual meeting, the director nominees named below will stand for election to serve a three-year term that will expire at the close of our annual meeting to be held during 2017. The shares represented by the enclosed proxy will be voted to elect as directors the nominees named below, unless a vote is withheld for such nominee or nominees. If a nominee cannot or will not serve as a director (which events are not anticipated), then the shares represented by the enclosed proxy may be voted for a substitute nominee named by the Board in the discretion of the holder of the proxies.

### **Director Classes**

Our Board of Directors is currently composed of five directors. Our Board of Directors is divided into three classes. Each year, one class is elected to serve for three years. The business address for each director for matters regarding our company is 41 Grand Avenue, River Edge, New Jersey 07661. On November 22, 2013, James S. Scibetta informed our Board of Directors of his resignation as director, effective December 31, 2013.

In connection with our September 2007 financing, we entered into an investor rights agreement with the 2007 investors pursuant to which we agreed to take such corporate actions as may be required, among other things, to entitle Lambda Investors (i) to nominate two individuals having reasonably appropriate experience and background to our Board to serve as directors until their respective successor(s) are elected and qualified, (ii) to nominate each successor to the Lambda Investors nominees, provided that any successor shall have reasonably appropriate experience and background, and (iii) to direct the removal from the Board of any director nominated under the foregoing clauses (i) or (ii). Under the investor rights agreement, we are required to convene meetings of the Board of Directors at least once every three months. If we fail to do so, a Lambda Investors director will be empowered to convene such meeting.

### **Board Nominees**

The Board of Directors has nominated Messrs. Daron Evans and Lawrence J. Centella for election as Class III directors. Messrs. Evans and Centella would serve three-year terms expiring at the close of our annual meeting to be held during 2017. Biographical information regarding Messrs. Evans and Centella is set forth below:

#### **Age**

<b>Name</b>	<b>(as of 4/1/14)</b>	<b>Director Since</b>	<b>Business Experience For Last Five Years</b>
Daron Evans	40	2013	<p>Mr. Evans is a life sciences executive with over 20 years of financial leadership and operational experience. Mr. Evans is currently a Partner at The Highland Group, an operational consulting practice that partners with industrial clients to deliver targeted results, and a Director on the Board of Zumbro Discovery, an early stage company developing a novel therapy for resistant hypertension. Mr. Evans was most recently Chief Financial Officer of Nile Therapeutics, Inc., from 2007 until its merger with Capricor, Inc. in November 2013. From 2006 to 2007, he was Director of Business Assessment for Vistakon, a division of Johnson &amp; Johnson Corp. From 2004 to 2006, he was Associate Director of Portfolio Management &amp; Business Analytics at Scios, Inc. after its acquisition by Johnson &amp; Johnson Corp. Mr. Evans was a co-founder of Applied Neuronal Network Dynamics, Inc. and served as its President from 2002 to 2004. From 1995 to 2002, Mr. Evans served in various roles at consulting firms Arthur D. Little and Booz Allen &amp; Hamilton. Mr. Evans is the author of four U.S. patents. Mr. Evans received his Bachelor of Science in Chemical Engineering from Rice University, his Master of Science in Biomedical Engineering from a joint program at the University of Texas at Arlington and Southwestern Medical School and his MBA from the Fuqua School of Business at Duke University.</p>

Name	Age (as of 4/1/14)	Director Since	Business Experience For Last Five Years
Lawrence J. Centella	73	2001	Lawrence J. Centella has served as a director of our company since January 2001. Mr. Centella serves as President of Renal Patient Services, LLC, a company that owns and operates dialysis centers, and has served in such capacity since June 1998. From 1997 to 1998, Mr. Centella served as Executive Vice President and Chief Operating Officer of Gambro Healthcare, Inc., an integrated dialysis company that manufactured dialysis equipment, supplied dialysis equipment and operated dialysis clinics. From 1993 to 1997, Mr. Centella served as President and Chief Executive Officer of Gambro Healthcare Patient Services, Inc. (formerly REN Corporation). Prior to that, Mr. Centella served as President of COBE Renal Care, Inc., Gambro Hospital, Inc., LADA International, Inc. and Gambro, Inc. Mr. Centella is also the founder of LADA International, Inc. Mr. Centella received a B.S. from DePaul University. Among other experience, qualifications, attributes and skills, Mr. Centella's extensive experience in managing companies engaged in the business of dialysis centers and equipment, led to the conclusion of our Board that he should serve as a director of our company in light of our business and structure.

**Vote Required**

Directors will be elected by plurality vote. No minimum vote is required for the nominees to be elected. If any other nominee is put forward at the meeting, the nominees receiving the highest number of affirmative votes of the shares present or represented and entitled to be voted at the meeting shall be elected as directors. Stockholders do not have cumulative voting rights. Your vote may be cast *for* or *withheld* from any individual nominee.

**Our Board of Directors has unanimously approved and recommends that stockholders vote “FOR”**

**the election of Messrs. Evans and Centella as our Class III directors (Item 1 of the enclosed proxy card).**

**Continuing Directors**

In addition to Messrs. Evans and Centella, who have been nominated for re-election to our Board and about whom information is provided in Proposal No. 1, our other directors whose terms do not expire at the annual meeting are listed below.

**Class I Director – Term Expiring 2015**

<b>Name</b>	<b>Age (as of 4/1/14)</b>	<b>Director Since</b>	<b>Business Experience For Last Five Years</b>
Arthur H. Amron	57	2007	Arthur H. Amron has served as a director of our company since September 2007. Mr. Amron is a Partner of Wexford Capital LP, an SEC-registered investment advisor and serves as its General Counsel. Mr. Amron also actively participates in various private equity transactions, particularly in the bankruptcy and restructuring areas, and has served on the boards and creditors' committees of a number of public and private companies in which Wexford has held investments. Mr. Amron has also served as a director of Rhino GP LLC, which is the general partner of Rhino Resource Partners LP, a publicly traded master limited partnership (NYSE - RNO), since October 2010. From 1991 to 1994, Mr. Amron was an Associate at Schulte Roth & Zabel LLP, specializing in corporate and bankruptcy law, and from 1984 to 1991, Mr. Amron was an Associate at Debevoise & Plimpton LLP specializing in corporate litigation and bankruptcy law. Mr. Amron holds a J.D. from Harvard University, a B.A. in Political Theory from Colgate University and is a member of the New York Bar. Among other experience, qualifications, attributes and skills, Mr. Amron's legal training and experience in the capital markets, as well as his experience serving on boards of directors of other public companies, led to the conclusion of our Board that he should serve as a director of our company in light of our business and structure.

**Class II Directors – Term Expiring 2016**

<b>Name</b>	<b>Age (as of 4/1/14)</b>	<b>Director Since</b>	<b>Business Experience For Last Five Years</b>
John C. Houghton	50	2012	Mr. Houghton has over 25 years of commercialization experience in the pharmaceutical and medical device fields. He has direct experience in building out global commercial organizations including marketing, sales, sales operations, customer service, business analytics and new product development and has also been directly responsible for successfully licensing products and

leading joint ventures and partnerships. Mr. Houghton most recently served as President and CEO of CorMedix Inc. (NYSE-Amex: CRMD), a pharmaceutical company focused on therapeutic products for the treatment of cardio-renal disease. While President and CEO, Mr. Houghton led the acquisition of the company's product candidates and the completion of its initial public offering. Prior to assuming the role of President and CEO, he was the Chief Business Officer for CorMedix. Before joining CorMedix, Mr. Houghton established the global sales and marketing infrastructure for the Biotech division of Stryker Corp. (NYSE: SYK). Prior to Stryker, he worked with Aventis (NYSE: SNY) and predecessor companies for more than 14 years. During his time at Aventis he led the global marketing of Nasacort, served as commercial lead on the Aventis-Millennium inflammation collaboration, and functioned as the global new products commercialization head for respiratory, inflammation, cardiovascular, and metabolism products. Mr. Houghton received his B.Sc. from Liverpool John Moores University, United Kingdom. Mr. Houghton's extensive experience in leadership roles in connection with sales and marketing in the pharmaceutical and medical device fields, as well as his management experience, led to the conclusion of our Board that he should serve as a director of our company in light of our business and structure.

Name	Age (as of 4/1/14)	Director Since	Business Experience For Last Five Years
Paul A. Mieyal	44	2007	<p>Paul A. Mieyal has served as a director of our company since September 2007. Dr. Mieyal has been a Vice President of Wexford Capital LP since October 2006. From January 2000 through September 2006, he was Vice President in charge of healthcare investments for Wechsler &amp; Co., Inc., a private investment firm and registered broker-dealer. Dr. Mieyal is also a director of Nile Therapeutics, Inc., which is a publicly traded company. Dr. Mieyal received his Ph.D. in Pharmacology from New York Medical College, a B.A. in Chemistry and Psychology from Case Western Reserve University, and is a Chartered Financial Analyst. Dr. Mieyal served as our Acting Chief Executive Officer from April 6, 2010 until April 20, 2012. Among other experience, qualifications, attributes and skills, Dr. Mieyal's pharmacology and chemistry education, his experience in investment banking in the healthcare industry, as well as his experience serving on boards of directors of other public companies, led to the conclusion of our Board that he should serve as a director of our company in light of our business and structure.</p>

**PROPOSAL NO. 2 —**

**RATIFICATION OF SELECTION OF INDEPENDENT**

**REGISTERED PUBLIC ACCOUNTING FIRM**

The Audit Committee of the Board of Directors has selected the firm of Rothstein Kass to serve as our independent registered public accounting firm for the fiscal year ending December 31, 2014. The Board of Directors has ratified this selection and recommends that the stockholders ratify this selection. If the selection of Rothstein Kass is not ratified by the stockholders, the Audit Committee will reconsider, but might not change, its selection.

Rothstein Kass has audited our consolidated accounts since July 2007, and has advised us that it does not have, and has not had, any direct or indirect financial interest in our company in any capacity other than that of serving as independent registered public accounting firm. Representatives of Rothstein Kass are expected to attend the annual meeting. They will have an opportunity to make a statement, if they desire to do so, and will also be available to respond to appropriate questions.

**Summary of Auditor Fees and Pre-Approval Policy**

In accordance with its charter, the Audit Committee approves in advance all audit and non-audit services to be provided by our registered independent public accounting firm. Although the Audit Committee does not have formal pre-approval policies and procedures in place, it pre-approved all of the services performed by Rothstein Kass during fiscal years 2013 and 2012.

**Audit Fees**

Fees billed for audit services by Rothstein Kass totaled approximately \$126,000 and \$119,000 in connection with statutory and regulatory filings for the fiscal years ended December 31, 2013 and 2012, respectively. Such fees include fees associated with the annual audit.

**Audit-Related Fees**

During the fiscal year ended December 31, 2013, we were billed approximately \$17,000 by Rothstein Kass for audit-related services in connection with the annual audit and for the reviews of our Form S-1 filings. During the fiscal year ended December 31, 2012, we were billed approximately \$24,500 by Rothstein Kass for audit-related services in connection with the annual audit and for the reviews of our Form S-1 filings.

Our Audit Committee has considered whether, and determined that, the provision of the non-audit services rendered to us during 2013 and 2012 was compatible with maintaining the independence of Rothstein Kass.

#### **Tax Fees**

There were no tax services provided by Rothstein Kass for the fiscal years ended December 31, 2013 and 2012.

#### **All Other Fees**

We did not engage Rothstein Kass to provide any information technology services or any other services during the fiscal years ended December 31, 2013 and 2012.

#### **Vote Required**

The affirmative vote of the holders of a majority of the shares of our common stock present or represented and voting on this proposal at the meeting shall constitute ratification of the appointment of Rothstein Kass. Abstentions will have the same effect as a vote against Proposal No. 2. However, broker non-votes will have no effect on the outcome of this matter.

**Our Board of Directors has unanimously approved and recommends a vote “FOR”**

**the ratification of the selection of Rothstein Kass as our independent registered public**

**accounting firm for the fiscal year ending December 31, 2014 (Item 2 on the enclosed proxy card).**



**PROPOSAL NO. 3 —**

**ADVISORY VOTE ON EXECUTIVE COMPENSATION**

We are asking our stockholders to cast an advisory vote to approve the compensation of our named executive officers as disclosed in our proxy statement under “Compensation Matters”, and in the tabular and accompanying narrative disclosure regarding named executive officer compensation.

As required by Section 14A(a)(1) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), our stockholders are entitled to vote at the annual meeting to approve the compensation of our named executive officers, as disclosed in this proxy statement pursuant to Item 402 of Regulation S-K, at least once every three years.

Our executive compensation arrangements are designed to enhance stockholder value on an annual and long-term basis. Through the use of base pay as well as annual and long-term incentives, we seek to compensate our named executive officers for their contributions to our profitability and success. Please read “Compensation Matters” beginning on page 17 of this proxy statement for additional details about our executive compensation arrangements, including information about the fiscal year 2013 compensation of our named executive officers. We are asking our stockholders to indicate their support for our compensation arrangements as described in this proxy statement.

For the reasons discussed above, the Board recommends that stockholders vote in favor of the following resolution:

“**RESOLVED**, that the compensation paid to the company's named executive officers, as disclosed in this proxy statement pursuant to Item 402 of Regulation S-K under the heading “Compensation Matters”, including the compensation tables and narrative discussion, is hereby APPROVED.”

**Vote Required**

The affirmative vote of a majority of votes cast is required to approve the compensation of our named executive officers. Because your vote is advisory, however, it will not be binding upon or overrule any decisions of the Board, nor will it create any additional fiduciary duty on the part of the Board. This advisory vote also does not seek to have the Board or Compensation Committee take any specific action. However, the Board and the Compensation Committee value the view expressed by our stockholders in their vote on this proposal and will take into account the outcome of the vote when considering executive compensation matters in the future. In considering the outcome of this advisory vote, the Board will review and consider all shares voted in favor of the proposal and not in favor of the

proposal. Broker non-votes will have no impact on the outcome of this advisory vote.

**Our Board of Directors has unanimously approved and recommends a vote “FOR”  
the approval of the compensation of the named executive officers as disclosed in this proxy  
statement pursuant to Item 402 of Regulation S-K (Item 3 on the enclosed proxy card).**

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**PROPOSAL NO. 4 —**

**ADVISORY VOTE ON THE FREQUENCY OF THE**

**ADVISORY VOTE ON EXECUTIVE COMPENSATION**

In this advisory vote, we are asking stockholders to indicate whether we should conduct an advisory vote on the compensation of our named executive officers once every year, once every two years, or once every three years (i.e., on an annual, biennial or triennial basis). Alternatively, stockholders may abstain from casting a vote on this matter.

After careful consideration, our Board of Directors has determined that an advisory vote on executive compensation every two years is the most appropriate alternative for us. By providing an advisory vote on executive compensation every two years, our stockholders will be able to provide us with direct input on our compensation policies and practices as disclosed in the proxy statement. We understand that our stockholders may have different views as to what is the best approach for us.

Based on these considerations, the Board is recommending that stockholders vote that an advisory vote on executive compensation should be held once every two years, but it is important to note that the proxy card provides for four choices (every one, two, or three years, or abstain) and that stockholders are not voting to approve or disapprove the Board's recommendation.

**Vote Required**

Because your vote is advisory, it will not be binding upon the Board, nor will it create any additional fiduciary duty on the part of the Board. However, the Board will take into account the outcome of the vote when determining how frequently an advisory vote on executive compensation should be conducted in the future. The frequency that receives the highest number of votes cast by stockholders will be considered by the Board as the frequency that has been elected by stockholders.

Legislation requires that our stockholders be given the opportunity, at least once every six years, to cast an advisory vote regarding how frequently we should conduct this advisory vote on executive compensation. In the future, the Board may, in its discretion, decide to hold an advisory vote on the frequency of future advisory votes on executive compensation more often than once every six years.

**Our Board of Directors has unanimously approved and recommends a vote for “2 Years” as the frequency for future non-binding stockholder votes on the compensation of the named executive officers as required by Section 14A(a)(1) of the Exchange Act (Item 4 on the enclosed proxy card).**

## **CORPORATE GOVERNANCE**

### **Board of Director Meetings**

Our business is under the general oversight of the Board of Directors as provided by the laws of Delaware and our bylaws. During the fiscal year ended December 31, 2013, the Board of Directors held ten meetings and took action by unanimous written consent in lieu of a meeting two times. Each person who was a director during 2013 attended at least 75% of the Board of Directors meetings and the meetings of the committees on which he served.

Each of our directors is encouraged to be present at the annual meeting of our stockholders absent exigent circumstances that prevents his attendance. Where a director is unable to attend the annual meeting in person but is able to do so by electronic conferencing, we will arrange for the director's participation by means where the director can hear, and be heard by, those present at the meeting. Two of our then four directors attended the 2013 annual meeting.

### **Selection of Nominees for the Board of Directors**

The entire Board is responsible for nominating members for election to the Board and for filling vacancies on the Board that might occur between annual meetings of the stockholders. The Board is also responsible for identifying, screening, and recommending candidates for prospective Board membership. When formulating its membership recommendations, the Board also considers any qualified candidate for an open Board position timely submitted by our stockholders in accordance with our established procedures.

The Board will evaluate and recommend candidates for membership on the Board consistent with criteria, including: personal qualities and characteristics, accomplishments, and reputation in the business community; financial, regulatory, and business experience; current knowledge and contacts in the industry in which we do business; ability and willingness to commit adequate time to Board and committee matters; fit of the individual's skills with those of other directors and potential directors in building a Board that is effective and responsive to our needs; independence; and any other factors the Board deems relevant, including diversity of viewpoints, background, experience, and other demographics. In addition, prior to nominating an existing director for re-election, the Board will consider and review an existing director's Board and committee attendance and performance; length of Board service; experience, skills, and contributions that the existing director brings to the Board; and independence.

To identify nominees, the Board will rely on personal contacts as well as its knowledge of persons in our industry. We have not previously used an independent search firm to identify nominees.

The Board will consider stockholder recommendations of candidates when the recommendations are properly submitted. Stockholder recommendations should be submitted to us under the procedures discussed in “Procedures For Security Holder Submission of Nominating Recommendations” which is available on our website at [www.nephros.com](http://www.nephros.com), by clicking on the Investor Relations link, then the Corporate Governance link. Written notice of any nomination must be timely delivered to Nephros, Inc., 41 Grand Avenue, River Edge, New Jersey 07661, Attention: Board of Directors, c/o President, Chief Executive Officer and Acting Chief Financial Officer.

The Board uses a variety of methods for identifying and evaluating non-incumbent candidates for director. The Board regularly assesses the appropriate size and composition of the Board, the needs of the Board and the respective committees of the Board as well as the qualifications of candidates in light of these needs. The Board will solicit recommendations for nominees from persons that the Board believes are likely to be familiar with qualified candidates, including members of the Board, our management or a professional search firm. The evaluation of these candidates may be based solely upon information provided to the Board or may also include discussions with persons familiar with the candidate, an interview of the candidate or other actions the Board deems appropriate, including the use of third parties to review candidates.

## **Director Independence**

Our Board of Directors has determined that all of the directors are “independent” within the meaning of the Nasdaq independence standards other than Mr. Houghton.

## **Committees**

Our Board of Directors has established an Audit Committee and a Compensation Committee. These committees are each governed by a specific charter, each of which is available on our website at [www.nephros.com](http://www.nephros.com), by clicking on the Investor Relations link, and then the Corporate Governance link. All members of these committees are independent directors.

The Board of Directors does not currently have a Nominating and Corporate Governance Committee given that the entire Board participates in discussions and decisions regarding identifying qualified individuals to become Board members, determining the composition of the Board and its committees, in monitoring a process to assess Board effectiveness and developing and implementing corporate procedures and policies.

### *Audit Committee*

The Audit Committee is composed of Daron Evans (Chairman) and Lawrence J. Centella, neither of whom is our employee and each of whom has been determined by the Board of Directors to be independent under the Nasdaq listing standards. The purpose of the Audit Committee is to: (i) oversee accounting, auditing, and financial reporting processes; (ii) assess the integrity of our financial statements; (iii) ensure that our internal controls and procedures are designed to promote compliance with accounting standards and applicable laws and regulations; and (iv) appoint and evaluate the qualifications and independence of our independent registered public accounting firm. The Audit Committee held four meetings in 2013.

The Board of Directors has determined that all Audit Committee members are financially literate under the current listing standards of Nasdaq. The Board also determined that Mr. Evans qualifies as an “audit committee financial expert” as defined by the Securities and Exchange Commission, or SEC, rules adopted pursuant to the Sarbanes-Oxley Act of 2002 based on his extensive experience previously outlined.

*Compensation Committee*

The Compensation Committee is composed of directors Lawrence J. Centella (Chairman) and Paul A. Mieyal. Neither gentleman is our employee; however, Dr. Mieyal served as Acting Chief Executive Officer from April 6, 2010 until April 20, 2012. The purpose of the Compensation Committee is to: (i) assist the Board in discharging its responsibilities with respect to compensation of our executive officers and directors; (ii) evaluate the performance of our executive officers; (iii) assist the Board in developing succession plans for executive officers; and (iv) administer our stock and incentive compensation plans and recommend changes in such plans to the Board as needed. The Compensation Committee establishes the compensation of senior executives on an annual basis. The Compensation Committee held one meeting in 2013.

The Compensation Committee reviews and approves, on an annual basis, the corporate goals and objectives with respect to the compensation of our executive officers. The Compensation Committee evaluates, at least once a year, our executive officers' performance in light of these established goals and objectives, and, based upon these evaluations, recommends to the full Board the annual compensation of such executive officers, including salary, bonus, incentive, and equity compensation. In reviewing and recommending the compensation of the executive officers, the Compensation Committee may consider the compensation awarded to officers of similarly situated companies, our performance, the individuals' performance, compensation given to our executive officers in past years or any other fact that the Compensation Committee deems appropriate. The Chief Executive Officer does not participate in the discussions and processes concerning his own compensation and is not present during any discussions regarding his own compensation. The Compensation Committee also reviews and recommends to the full Board appropriate director compensation programs for service as directors and committee members. The Compensation Committee has the authority to delegate any of its responsibilities to subcommittees as the Committee may deem appropriate.



Lawrence J. Centella and Paul A. Mieyal served as members of our Compensation Committee during all of 2013. Neither of these individuals was at any time during 2013 or at any other time an officer or employee of our company. Although Dr. Mieyal served as our Acting Chief Executive Officer until April 20, 2012, he received no employee compensation or employee benefits from us. No interlocking relationship exists between any member of our Compensation Committee and any member of any other company's Board of Directors or Compensation Committee.

### **Board Leadership Structure and Oversight of Risk**

The Board of Directors is responsible for providing oversight of our affairs. Until December 31, 2013, our Board leadership structure consisted of different persons serving the roles of Chairman of the Board and Chief Executive Officer. The Chairman of the Board, among other responsibilities, works with the Chief Executive Officer and the Board to prepare Board meeting agendas and schedules, acts as liaison to other members of the Board, and, in conjunction with our Chief Executive Officer, presides at Board meetings.

We believe that this Board leadership structure is an appropriate structure for us and our stockholders at this time. This structure allows the Chief Executive Officer to focus his energy on strategy and management of the company and the Board to focus on oversight of strategic planning and risk management of the company.

In fiscal year 2013, James S. Scibetta served as the Chairman of the Board. On November 22, 2013, Mr. Scibetta informed our Board of Directors of his resignation as a director, effective December 31, 2013. Our Board of Directors has not yet appointed a Chairman of the Board to replace Mr. Scibetta.

As explained above, our Board of Directors has two committees—the Audit Committee and the Compensation Committee. Our Audit Committee is responsible for overseeing certain accounting related aspects of our risk management processes while our full Board of Directors focuses on overall risk management. The Audit Committee and the full Board of Directors focus on what they believe to be the most significant risks facing us and our general risk management strategy, and also attempt to ensure, together with the Chief Executive Officer, that risks undertaken by us are consistent with the Board's appetite for risk. While the Board of Directors oversees our risk management, our management is responsible for day-to-day risk management processes. We believe this division of responsibilities at the present time is an appropriate approach for addressing the risks facing our company and that our Board leadership structure supports this approach. We can offer no assurance that this structure, or any other structure, will be effective in all circumstances.

### **Stockholder Communication with the Board**

Stockholders may communicate with the Board of Directors, members of particular committees or to individual directors, by sending a letter to such persons in care of our President, Chief Executive Officer and Acting Chief Financial Officer at our principal executive offices. The President, Chief Executive Officer and Acting Chief Financial Officer has the authority to disregard any inappropriate communications or to take other appropriate actions with respect to any inappropriate communications. If deemed an appropriate communication, the President, Chief Executive Officer and Acting Chief Financial Officer will submit the correspondence to the Board of Directors or to any committee or specific director to whom the correspondence is directed. Procedures for sending communications to the Board of Directors can be found on our website at [www.nephros.com](http://www.nephros.com), by clicking on the Investor Relations link, then the Corporate Governance link. Please note that all such communications must be accompanied by a statement of the type and amount of our securities that the person holds; any special interest, meaning an interest that is not derived from the proponent's capacity as a stockholder, of the person in the subject matter of the communication; and the address, telephone number and e-mail address, if any, of the person submitting the communication.

### **Code of Business Conduct and Code of Ethics**

During the fiscal year ended December 31, 2004, we adopted a Code of Ethics and Business Conduct, which was amended and restated on April 2, 2007, for our employees, officers and directors that complies with SEC regulations. The Code of Ethics is available free of charge on our website at [www.nephros.com](http://www.nephros.com), by clicking on the Investor Relations link, then the Corporate Governance link. We intend to timely disclose any amendments to, or waivers from, our code of ethics and business conduct that are required to be publicly disclosed pursuant to rules of the SEC by filing such amendment or waiver with the SEC.

## **Executive Officer**

We currently have no executive officers other than John C. Houghton.

On May 29, 2013, Gerald J. Kochanski, Chief Financial Officer, Treasurer and Corporate Secretary of Nephros, Inc., resigned effective June 15, 2013. In connection with the resignation of Gerald J. Kochanski as the Company's Chief Financial Officer, on August 9, 2013, the Board of Directors of the Company appointed John C. Houghton, President and Chief Executive Officer, to also serve as the Company's Acting Chief Financial Officer and Principal Financial and Accounting Officer.

From April 6, 2010 until April 20, 2012, Paul A. Mieyal, a member of the Board of Directors, served as the Acting Chief Executive Officer. Upon the appointment of John C. Houghton, effective April 20, 2012, Paul A. Mieyal resigned as Acting Chief Executive Officer, but remains a member of the Board of Directors of the Company. Dr. Mieyal is a Vice President of Wexford Capital LP, the managing member of Lambda Investors LLC, which, as of April 1, 2014, beneficially owned approximately 48% of our outstanding common stock, representing approximately 60% on a fully-diluted basis.

## **Audit Committee Report**

The Audit Committee has reviewed and discussed our consolidated audited financial statements for fiscal year 2013 with management. The Audit Committee has discussed with Rothstein Kass, our independent registered public accounting firm, the matters required to be discussed by Statement on Auditing Standards No. 61, as amended. The Audit Committee has received the written disclosures and the letter from Rothstein Kass required by the Public Company Accounting Oversight Board regarding communications with the Audit Committee regarding independence, and has discussed with Rothstein Kass its independence. Based on the review and discussions described above, among other things, the Audit Committee recommended to the Board of Directors that the consolidated audited financial statements be included in our Annual Report on Form 10-K for fiscal year 2013.

Submitted by: The Audit Committee  
Daron Evans, Chairman

Lawrence J. Centella

This Audit Committee Report shall not be deemed to be filed with the SEC or incorporated by reference into any of our previous or future filings with the SEC, except as otherwise explicitly specified by us in any such filing.



**Stock Ownership of Management and Principal SHAREHOLDERS**

The following table sets forth the beneficial ownership of our common stock as of April 1, 2014, by (i) each person known to us to own beneficially more than five percent (5%) of our common stock, based on such persons' or entities' filings with the SEC as of that date; (ii) each director, director nominee and executive officer; and (iii) all directors, director nominees and executive officers as a group:

Name and Address of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percentage of Class <sup>(1)</sup>	
Lambda Investors LLC <sup>(2)</sup>	26,524,427	60	%
Southpaw Asset Management LP <sup>(3)</sup>	1,145,278	3	%
Arthur H. Amron <sup>(4)</sup>	107,778	*	
Lawrence J. Centella <sup>(5)</sup>	174,017	*	
John C. Houghton <sup>(6)</sup>	620,844	1	%
Daron Evans <sup>(7)</sup>	34,772	*	
Paul A. Mieyal <sup>(8)</sup>	107,778	*	
Gerald J. Kochanski <sup>(9)</sup>	-0-	*	
All executive officers and directors as a group <sup>(4) - (9)</sup>	1,045,189	4	%

\* Represents less than 1% of the outstanding shares of our common stock.

Applicable percentage ownership is based on 25,225,704 shares of common stock outstanding as of April 1, 2014, after giving effect to the 1:20 reverse stock split effected March 11, 2011, together with applicable options and warrants for each stockholder. Beneficial ownership is determined in accordance with the rules of the SEC, based (1) on factors including voting and investment power with respect to shares. Common stock subject to options and warrants exercisable on or within 60 days after April 1, 2014 are deemed outstanding for the purpose of computing the percentage ownership of the person holding those options or warrants, but not for computing the percentage ownership of any other person.

(2) Based in part on information provided Form 4 filed on March 18, 2014. The shares beneficially owned by Lambda Investors may be deemed beneficially owned by Wexford Capital LP, which is the managing member of Lambda Investors, Wexford GP LLC, which is the General Partner of Wexford Capital LP, by Charles E. Davidson in his capacity as Chairman and managing member of Wexford Capital LP and by Joseph M. Jacobs in his capacity as President and managing member of Wexford Capital LP. The address of each of Lambda Investors LLC, Wexford Capital LP, Mr. Davidson and Mr. Jacobs is c/o Wexford Capital LP, 411 West Putnam Avenue, Greenwich, CT 06830. Each of Wexford Capital LP, Wexford GP LLC, Mr. Davidson and Mr. Jacobs disclaims beneficial ownership of the shares of Common Stock owned by Lambda Investors except, in the case of Mr. Davidson and Mr. Jacobs, to the extent of their respective interests in each member of Lambda Investors. Includes 14,524,677 shares issuable upon exercise of warrants held by Lambda Investors having an exercise price of \$0.40 per share. Lambda Investors is controlled by Wexford Capital LP. Arthur H. Amron, one of our directors, is a Partner and General Counsel of Wexford Capital LP. Paul A. Mieyal, one of our directors, is a Vice President of Wexford

Capital LP.

Based in part on information provided in Schedule 13D/A filed on May 30, 2013. The shares beneficially owned by Southpaw Asset Management LP may be deemed beneficially owned by Southpaw Holdings LLC, which is the General Partner of Southpaw Asset Management LP, and by each of Kevin Wyman and Howard Golden, who are principals of Southpaw Holdings LLC, and Southpaw Credit Opportunity Master Fund LP, of which Southpaw Asset Management LP is the investment manager. The address of each of Southpaw Asset Management LP, (3) Southpaw Holdings LLC, Kevin Wyman, Howard Golden, and Southpaw Credit Opportunity Master Fund LP, is 2 Greenwich Office Park, Greenwich, CT 06831. Each of Southpaw Asset Management LP, Southpaw Holdings LLC, Kevin Wyman and Howard Golden disclaims beneficial ownership of 664,298 shares of common stock and 480,980 shares issuable upon the exercise of warrants beneficially owned by Southpaw Credit Opportunity Master Fund LP having an exercise price of \$0.40.

Mr. Amron's address is c/o Wexford Capital LP, 411 West Putnam Avenue, Greenwich, CT 06830. The shares identified as being beneficially owned by Mr. Amron consist of: (i) 48,496 shares of restricted stock granted under (4) the 2004 Stock Incentive Plan; and (ii) 59,282 shares issuable upon exercise of options granted under the 2004 Stock Incentive Plan. Does not include 21,066 shares issuable upon the exercise of options which have been granted under our Stock Incentive Plans but will not vest within 60 days of April 1, 2014.

Mr. Centella's address is the company address: 41 Grand Avenue, River Edge, New Jersey 07661. The shares identified as being beneficially owned by Mr. Centella consist of: (i) 37,239 shares of common stock; (ii) 48,496 (5) shares of restricted stock granted under the 2004 Stock Incentive Plan; and (iii) 88,282 shares issuable upon exercise of options granted under the 2004 Stock Incentive Plan. Does not include 21,066 shares issuable upon the exercise of options which have been granted under our Stock Incentive Plans but will not vest within 60 days of April 1, 2014.

Mr. Houghton's address is the company address: 41 Grand Avenue, River Edge, New Jersey 07661. The shares identified as being beneficially owned by Mr. Houghton consist of: (i) 66,254 shares of restricted stock granted (6) under the 2004 Stock Incentive Plan; and (ii) 554,590 shares issuable upon exercise of options granted under the 2004 Stock Incentive Plan. Does not include 524,460 shares issuable upon the exercise of options which have been granted under our Stock Incentive Plans but will not vest within 60 days of April 1, 2014.

Mr. Evans' address is the company address: 41 Grand Avenue, River Edge, New Jersey 07661. The shares identified as being beneficially owned by Mr. Evans consist of: (i) 9,651 shares of common stock; and (ii) 25,121 (7) shares issuable upon exercise of options granted under the 2004 Stock Incentive Plan. Does not include 50,240 shares issuable upon the exercise of options which have been granted under our Stock Incentive Plans but will not vest within 60 days of April 1, 2014.

Dr. Mieyal's address is c/o Wexford Capital LP, 411 West Putnam Avenue, Greenwich, CT 06830. The shares identified as being beneficially owned by Dr. Mieyal consist of: (i) 48,496 shares of restricted stock granted under (8) the 2004 Stock Incentive Plan; and (ii) 59,282 shares issuable upon exercise of options granted under the 2004 Stock Incentive Plan. Does not include 21,066 shares issuable upon the exercise of options which have been granted under our Stock Incentive Plans but will not vest within 60 days of April 1, 2014.