MAP Pharmaceuticals, Inc.
Form 10-Q
July 27, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2012

OR

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

FOR THE TRANSITION PERIOD FROM TO

Commission File Number 001-33719

MAP PHARMACEUTICALS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**20-0507047**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
2400 Bayshore Parkway, Suite 200	
Mountain View, California	**94043**
(Address of principal executive offices)	**(Zip code)**

(650) 386-3100

(Registrant s telephone number, including area code)

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

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

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

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

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

As of July 20, 2012, the registrant had outstanding 30,748,261 shares of Common Stock.

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PART I FINANCIAL INFORMATION

Item 1 Financial Statements

MAP PHARMACEUTICALS, INC.

(a development stage enterprise)

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

(Unaudited)

	June 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$ 68,419	$ 98,816
Accounts receivable	229	636
Prepaid expenses and other current assets	743	763
Total current assets	69,391	100,215
Property and equipment, net	6,720	6,786
Other assets	27	27
Restricted investment	310	310
Total assets	$ 76,448	$ 107,338
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,063	$ 3,860
Accrued liabilities	6,750	6,933
Current portion of deferred revenue	3,512	3,349
Total current liabilities	11,325	14,142
Deferred revenue, less current portion	51,512	53,581
Other liabilities		63
Total liabilities	62,837	67,786
Commitments and contingencies (Note 6)		
Stockholders equity:		
Common stock	302	300
Additional paid-in capital	316,947	311,755
Deficit accumulated during the development stage	(303,638)	(272,503)
Total stockholders equity	13,611	39,552
Total liabilities and stockholders equity	$ 76,448	$ 107,338

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

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MAP PHARMACEUTICALS, INC.

(a development stage enterprise)

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands, except per share amounts)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,		Period from July 3, 2003 (Inception) to June 30,
	2012	2011	2012	2011	2012
Collaboration revenue	$ 878	$ 837	$ 1,906	$ 1,395	$ 79,141
Operating expenses:					
Research and development	7,773	7,259	18,735	18,827	269,867
Sales, general and administrative	6,399	4,796	14,308	9,639	99,282
Total operating expenses	14,172	12,055	33,043	28,466	369,149
Loss from operations	(13,294)	(11,218)	(31,137)	(27,071)	(290,008)
Interest income	1	22	1	52	6,469
Interest expense		(106)		(273)	(7,309)
Other income (expense), net	1		1	(10)	(773)
Net loss	(13,292)	(11,302)	(31,135)	(27,302)	(291,621)
Cumulative stock dividend attributed to preferred stockholders					(13,925)
Net loss attributed to common stockholders	$ (13,292)	$ (11,302)	$ (31,135)	$ (27,302)	$ (305,546)
Net loss per share attributed to common stockholders basic and diluted	$ (0.43)	$ (0.37)	$ (1.02)	$ (0.90)	
Weighted average shares outstanding used in calculating net loss per share attributed to common stockholders basic and diluted	30,698	30,333	30,659	30,272	
Total comprehensive loss	$ (13,292)	$ (11,302)	$ (31,135)	$ (27,302)	$ (305,546)

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

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MAP PHARMACEUTICALS, INC.

(a development stage enterprise)

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Six Months Ended June 30,		Cumulative Period from July 3, 2003 (Date of Inception) to June 30,
	2012	2011	2012
Cash flows from operating activities:			
Net loss	$ (31,135)	$ (27,302)	$ (291,621)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization	919	609	8,247
Accretion of investment discounts, net			(1,595)
Accretion of debt payment premium		55	999
Stock-based compensation	4,321	3,772	29,506
Loss on disposal of equipment and other non-cash items	398	10	2,682
Changes in operating assets and liabilities:			
Accounts receivable	407	(384)	(229)
Prepaid expenses and other current assets	20	128	(968)
Other assets		3	113
Accounts payable	(2,208)	(263)	918
Accrued liabilities	(185)	(4,116)	6,668
Deferred revenue	(1,906)	58,605	55,024
Other liabilities	(61)	(12)	2
Net cash provided by (used in) operating activities	(29,430)	31,105	(190,254)
Cash flows from investing activities:			
Purchase of intangible assets and in-process research and development			(412)
Purchase of property and equipment	(1,840)	(1,490)	(16,205)
Purchase of short-term investments			(169,497)
Sales and maturities of short-term investments			171,411
Purchase of restricted investment			(310)
Net cash used in investing activities	(1,840)	(1,490)	(15,013)
Cash flows from financing activities:			
Proceeds from issuance of convertible notes payable			4,300
Proceeds from issuance of debt			31,006
Net proceeds from issuance of common stock through equity plans	873	1,758	7,584
Repayment of debt		(3,921)	(32,105)
Proceeds from issuance of common stock resulting from drawdown of equity line of credit, net of issuance costs			19,653
Proceeds from issuance of common stock in equity offering, net of issuance costs		2	140,820
Proceeds from issuance of convertible preferred stock, net of issuance costs			102,428

Net cash provided by (used in) financing activities	873	(2,161)	273,686
Net increase (decrease) in cash and cash equivalents	(30,397)	27,454	68,419
Cash and cash equivalents at beginning of period	98,816	76,007	
Cash and cash equivalents at end of period	$ 68,419	$ 103,461	$ 68,419
Supplemental disclosures of non-cash investing activities			
Purchase of property and equipment through accounts payable	$ 116	$ 198	$ 116

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

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MAP PHARMACEUTICALS, INC.

(a development stage enterprise)

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. THE COMPANY

MAP Pharmaceuticals, Inc., incorporated in the state of Delaware, originally was formed as a limited liability company on July 3, 2003 and converted to a corporation on December 11, 2003. Our goal is to enhance the therapeutic benefits and commercial attractiveness of proven drugs in the field of neurology, while minimizing risk by capitalizing on their known safety, efficacy and commercialization history, by applying our proprietary formulation and inhalation technologies. Our current focus is to advance the development of our product candidate, LEVADEX®, formerly known as MAP0004, a proprietary orally inhaled version of dihydroergotamine for the potential treatment of migraine. We are in the development stage and since inception have devoted substantially all of our efforts to research and development, raising capital and recruiting personnel.

We have incurred losses and negative cash flow since our inception in July 2003. We will continue to incur losses until we generate sufficient revenue to offset our expenses, and we anticipate that we may continue to incur net losses for the next several years. We will need substantial additional capital in the future in connection with the development and potential commercialization of LEVADEX and to fund the development and potential commercialization of any future product candidates. Prior to achieving profitable operations, we intend to continue to fund operations through public or private financings, strategic partnerships or other arrangements. Such funding, if needed, may not be available on favorable terms, if at all. In the event we are unable to obtain additional capital, we may delay or reduce the scope of our current research and development programs and other expenses.

On March 26, 2012, we received a Complete Response letter, in which the U.S. Food and Drug Administration, or FDA, described the reasons it was unable to approve our New Drug Application, or NDA, and identified issues that we need to address in order to obtain FDA approval of LEVADEX. Specifically, the FDA requested that we address issues relating to the chemistry, manufacturing and controls, or CMC, of LEVADEX. The FDA also stated that manufacturing deficiencies identified during a recent facility inspection of one of our third party manufacturers need to be resolved to the FDA s satisfaction. The FDA also indicated that it had not been able to complete its review of inhaler usability information requested late in the review cycle by the FDA. We continue to work to address the issues identified in the Complete Response letter and recently completed an End-of-Review meeting with the FDA to discuss our proposed plan for responding to the Complete Response letter. Based upon the meeting with the FDA, we are in the process of addressing the issues in the Complete Response letter, and we plan to resubmit to the FDA in the late third quarter/early fourth quarter 2012 timeframe.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

We have prepared the accompanying interim condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these financial statements and accompanying notes do not include all of the information and disclosures required by generally accepted accounting principles for complete financial statements. The financial statements include all adjustments (consisting of normal recurring adjustments) that management believes are necessary for the fair statement of the balances and results for the periods presented. These interim financial statement results are not necessarily indicative of the results to be expected for the full fiscal year or any future interim period.

The year-end condensed consolidated balance sheet at December 31, 2011 was derived from audited financial statements, and does not include all the disclosures required by accounting principles generally accepted in the United States. The financial statements and related disclosures have been prepared with the presumption that users of the interim financial statements have read or have access to the audited financial statements for the preceding fiscal year. Accordingly, these financial statements should be read in conjunction with the audited financial

statements and notes thereto contained in our Form 10-K for the year ended December 31, 2011.

Reclassifications

Certain prior period amounts in the condensed consolidated statements of cash flows have been reclassified to conform to current period presentation. Such reclassification did not impact our net loss or financial position.

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Revenue Recognition

We recognize revenue when all of the following criteria are met: persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; the fee is fixed or determinable; and collectability is reasonably assured. Collaboration revenue, which is earned under license agreements with third parties, may include nonrefundable license fees, cost reimbursements and contingent milestones.

Before January 1, 2011, we evaluated license arrangements with multiple elements in accordance with Accounting Standards Codification, or ASC, 605-25 *Revenue Recognition Multiple-Element Arrangements*. In October 2009, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update, or ASU, 2009-13 *Revenue Arrangements with Multiple Deliverables,* or ASU 2009-13, which amended the accounting standards for certain multiple element revenue arrangements to:

- provide updated guidance on whether multiple elements exist, how the elements in an arrangement should be separated, and how the arrangement consideration should be allocated to the separate elements;
- require an entity to allocate arrangement consideration to each element based on a selling price hierarchy, also called the relative selling price method, where the selling price for an element is based on vendor-specific objective evidence (VSOE), if available; third-party evidence (TPE), if available and VSOE is not available; or the best estimate of selling price (ESP), if neither VSOE nor TPE is available; and
- eliminate the use of the residual method and require an entity to allocate arrangement consideration using the selling price hierarchy.

The revenue allocated to each element is then recognized when the basic revenue recognition criteria are met for that element.

On January 1, 2011, we adopted ASU 2009-13 on a prospective basis. The new accounting standard for revenue recognition, if applied in the same manner to the year ended December 31, 2010, would not have any impact to total revenue and deferred revenue for that fiscal year as we did not have any collaboration revenue in fiscal 2010 or any deferred revenue as of December 31, 2010. The new accounting guidance for revenue recognition is not expected to have a significant effect on total net revenue in periods after initial adoption, although the impact on the timing of revenue will vary depending on the evaluation of the elements of any new arrangements.

VSOE is based on the price charged when the element is sold separately and is the price actually charged for that deliverable. We typically are not able to establish VSOE for the elements of a license arrangement because each arrangement is unique, an arrangement typically consists of multiple elements and we have limited history of entering into license arrangements.

When VSOE cannot be established, we attempt to establish the selling price of the elements of a license arrangement based on TPE. TPE is determined based on a competitor s price for similar deliverables when sold separately. We typically are not able to determine TPE for license arrangements, as they contain a significant level of differentiation such that the comparable pricing of a competitor s license arrangement with similar functionality cannot be obtained, and we are therefore unable to reliably determine what a similar competitor s license arrangement s selling price would be on a standalone basis.

When we are unable to establish the selling price of an element using VSOE or TPE, we use the ESP in our allocation of the upfront payment. The objective of the ESP is to determine the price at which we would transact a sale if the element of the license arrangement were sold on a standalone basis.

Our process for determining ESPs involves management s judgment. Our process considers multiple factors such as discounted cash flows, estimated direct expenses and other costs and available data, which may vary over time, depending upon the circumstances, and relate to each deliverable. If the estimated obligation period of one or more deliverables should change, the future amortization of the revenue would also change. We regularly review ESP and maintain internal controls over the establishment and updates of the estimates.

We entered into a Collaboration Agreement with Allergan, Inc. in January 2011 which requires us to provide multiple deliverables, including: a license to commercialize LEVADEX, clinical and regulatory work necessary for FDA approval of the first indication for LEVADEX (acute treatment of migraine in adults), manufacturing process development for LEVADEX, an option to include Canada in the territory in which Allergan can promote LEVADEX, and participation in various committees jointly with Allergan throughout the term of the Collaboration Agreement. These deliverables are non-contingent in nature. We received an upfront cash payment of $60.0 million from Allergan upon execution of the Collaboration Agreement. In accordance with ASU 2009-13, we evaluated whether there is standalone value for each of the various non-contingent deliverables. We have determined that the license delivered by us and other non-contingent deliverables do not have standalone value separate from each other, based on contractual limitations in the Collaboration Agreement that restrict Allergan from using the license for its intended purpose without other non-contingent deliverables from us.

We believe that since the license does not have standalone value, it must be combined with all the remaining non-contingent deliverables because the license would not be fully delivered for its intended purpose unless we continue to perform our obligation to participate in the various committees jointly with Allergan. Accordingly, all of the non-contingent deliverables are treated as a single unit of accounting, and we have combined the delivered license with the remaining non-contingent deliverables for accounting

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purposes. As a result, revenue relating to the $60.0 million upfront cash payment was deferred and will be recognized on a straight-line basis over the term of the Collaboration Agreement through 2028, which represents the estimated obligation period of the participation in the various joint committees, the non-contingent deliverable with the longest term.

The Collaboration Agreement also contains contingent deliverables that do not relate to the non-contingent deliverables identified above. For example, we will collaborate and share expenses with Allergan to develop LEVADEX for additional indications separate from and in addition to the first indication. Any reimbursements from Allergan to us for shared expenses relating to contingent deliverables are recorded in our financial statements in the quarters in which the cost sharing occurs.

Milestone payments relating to contingent deliverables, such as the acceptance for filing by the FDA of our New Drug Application for LEVADEX, are recognized as revenue in their entirety upon our achievement of a substantive milestone and when the respective revenue recognition criteria are met. A milestone is substantive if the consideration earned from the achievement of the milestone (i) is consistent with performance required to achieve the milestone or the increase in value to the delivered item, (ii) relates solely to past performance and (iii) is reasonable relative to all of the other deliverables and payments within the arrangement.

Stock-Based Compensation

Effective January 1, 2006, we adopted ASC 718 *Compensation Stock Compensation,* or ASC 718, using the prospective transition method, which requires the measurement and recognition of compensation expense for all stock-based payment awards granted, modified and settled to our employees and directors after January 1, 2006. ASC 718 requires companies to estimate the fair value of the stock-based payment awards on the date of grant using an option-pricing model. Our financial statements reflect the impact of ASC 718. We chose the straight-line attribution method for allocating compensation costs and recognized the fair value of each stock option on a straight-line basis over the requisite service period.

For RSUs with time-based vesting, the fair value is based on the closing price of our common stock on the date of grant. We measure compensation expense for these RSUs at fair value on the date of grant and recognize the expense over the expected vesting period, after considering the estimated forfeitures.

For RSUs with performance-based vesting, the fair value is based on the closing price of our common stock on the date of grant. A probability assessment that performance goals will be achieved is made quarterly. The compensation expense is recognized over the vesting period, and is adjusted periodically for forfeiture rate and any changes to our probability assessment of the number of performance-based RSUs expected to vest as a result of our achievement of the performance goals.

Concentration of Credit Risk and Other Risks and Uncertainties

We invest cash that is not currently being used for operational purposes in accordance with our investment policy. The policy allows for the purchase of debt securities such as those issued by the U.S. government and its agencies and subject to certain concentration limits by corporations. We also strive to limit risk by specifying a minimum credit quality for corporate debt securities of A1/P1 for commercial paper and AAA for other securities. The maximum maturity for these securities does not exceed 12 months. We believe our established guidelines for investment of our excess cash maintains safety and liquidity through our policies on diversification and investment maturity. Our cash and cash equivalent balances can be in excess of federally insured amounts.

At June 30, 2012, Allergan accounted for 100% of our accounts receivable. For the three and six months ended June 30, 2012 and 2011, Allergan accounted for 100% of our collaboration revenue.

We do not own or operate manufacturing facilities for clinical or commercial manufacture of our product candidates, which includes drug substance and drug packaging, including the components of the TEMPO inhaler, the device used to administer certain of our drug candidates, including LEVADEX. If our contract manufacturers fail to deliver the required commercial quantities of finished product on a timely basis and at commercially reasonable prices and we are unable to find one or more replacement manufacturers capable of production at a substantially equivalent cost, in substantially equivalent volumes and quality and on a timely basis, we would likely be unable to meet demand for our products and we would lose potential revenue. It may take a significant period of time to establish an alternative source of supply for our product

candidates.

Our product candidates require approval from the U.S. Food and Drug Administration or other international regulatory agencies prior to commencing commercial sales. There can be no assurance that our product candidates will receive any of these required approvals. If we are denied such approvals or such approvals are delayed, our results of operations, financial position and future cash flows may be materially adversely affected.

Net Loss per Share

Basic net loss per share is computed by dividing net loss attributed to common stockholders by the weighted average number of common shares outstanding during the period. Our potential dilutive shares, which include common stock options, restricted stock units, or RSUs, with time-based vesting, common stock issuable pursuant to the Employee Stock Purchase Plan, or ESPP, warrants to

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purchase common stock and RSUs with performance-based vesting have not been included in the computation of diluted net loss per share for all the periods as the result would be anti-dilutive. Such potentially dilutive shares are excluded when the effect would be to reduce a net loss per share.

The numerator and denominator used in the calculation of basic and diluted net loss per share were as follows (in thousands, except share and per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Numerator				
Net loss attributed to common stockholders	$ (13,292)	$ (11,302)	$ (31,135)	$ (27,302)
Denominator				
Weighted average common shares outstanding	30,698,208	30,333,126	30,658,900	30,272,271
Basic and diluted net loss per share	$ (0.43)	$ (0.37)	$ (1.02)	$ (0.90)

The following outstanding common stock options, RSUs with time-based vesting, common stock issuable pursuant to the ESPP, and warrants to purchase common stock were excluded from the computation of diluted net loss per share for the periods presented because including them would have had an anti-dilutive effect. The RSUs with performance-based vesting were also excluded from the computation of diluted net loss per share because they were contingently issuable shares.

	June 30,	
	2012	2011
Options to purchase common stock	5,065,251	4,391,696
RSUs with time-based vesting	308,898	128,242
Common stock issuable pursuant to the ESPP	61,747	37,297
Warrants to purchase common stock	26,903	26,903
RSUs with performance-based vesting	38,000	81,000

New Accounting Standard Recently Adopted

Effective January 1, 2012, we adopted revised guidance related to the presentation of comprehensive income that increases comparability between U.S. GAAP and International Financial Reporting Standards. This guidance eliminates the current option to report other comprehensive income, or OCI, and its components in the statement of changes in stockholders equity. We adopted this guidance during the first quarter of 2012 and elected to disclose OCI in a single continuous statement during interim reporting periods.

NOTE 3. LICENSE AND SUPPLY AGREEMENTS

Agreement with Allergan

On January 28, 2011, we entered into a Collaboration Agreement (the Collaboration Agreement) and a Co-Promotion Agreement (the Co-Promotion Agreement, and together with the Collaboration Agreement, the Allergan Agreements) with Allergan, Inc., Allergan USA, Inc. and Allergan Sales, LLC (collectively, Allergan). Pursuant to the terms of the Allergan Agreements, we have granted Allergan a co-exclusive license (the Allergan License) to market and co-promote LEVADEX®, our proprietary novel migraine therapy for delivery by inhalation, to neurologists and pain specialists in the United States in collaboration with us.

In July 2011, Allergan exercised its option to expand the Collaboration Agreement to include commercialization to neurologists and pain specialists in Canada. Under the Allergan Agreements, we retain the right to market and co-promote LEVADEX to other physicians within the United States and Canada and also retain all rights to LEVADEX in all other countries.

Under the Allergan Agreements, we are solely responsible for payment of all remaining costs of obtaining regulatory approval of LEVADEX for the acute treatment of migraine in adults, except that if the FDA notifies us that additional development or manufacturing activities costing in excess of a certain threshold amount will be required for such regulatory approval, the parties will share any such excess costs.

Contingent upon FDA approval of LEVADEX for the initial indication (the acute treatment of migraine), the parties will collaborate in the development of LEVADEX for the treatment of pediatric migraine and for at least one other indication. The parties generally share equally all other costs of developing LEVADEX under the Allergan Agreements, except that neither party shall be obligated for more than a certain threshold amount in a given year, or for more than a certain threshold amount in the aggregate, for development or manufacturing costs or expenses incurred by us for such activities. We may develop LEVADEX for certain other indications independently of the collaboration if Allergan does not agree to develop LEVADEX for such indications pursuant to the Allergan Agreements.

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We are responsible for manufacturing and distributing LEVADEX, if approved by the FDA, and anticipate booking product revenues from sales of LEVADEX resulting from the parties collaboration. The parties will each provide sales representatives and other sales support for marketing and promotional efforts. The Allergan Agreements specify minimum annual sales detail requirements to be provided by each party, and establish maximum annual amounts of detailing costs that each party will be obligated to incur pursuant to a commercialization plan. Shared commercialization costs are those costs and expenses directly related to the commercialization of LEVADEX and are agreed upon periodically by both parties. The parties share profits and losses resulting from the collaboration equally.

The Collaboration Agreement may be terminated (i) by Allergan, at will, after first commercial sale of LEVADEX in the United States, upon 180 days prior written notice, (ii) by Allergan, upon written notice to us, if we receive a complete response letter or equivalent communication from the FDA, that Allergan determines will extend potential approval beyond a certain date or requires a certain minimum level of additional investment, (iii) by us, upon written notice to Allergan, if Allergan commercializes a competing product in the United States or Canada and (iv) by us, upon written notice to Allergan, if Allergan challenges or opposes patent rights licensed to Allergan pursuant to the Collaboration Agreement. Additionally, either party may terminate the Collaboration Agreement in the event of an uncured material breach. The Co-Promotion Agreement will terminate upon termination of the Collaboration Agreement.

In February 2011, Allergan paid us an upfront payment of $60.0 million, out of which we have recognized $0.9 million and $1.9 million, respectively, for the three and six months ended June 30, 2012, compared to $0.8 million and $1.4 million, respectively, for the same periods in 2011. We have recognized $5.0 million for the cumulative period from July 3, 2003 (date of inception) to June 30, 2012. As of June 30, 2012, $55.0 million of the initial $60.0 million remained unrecognized and will be amortized as collaboration revenue through the end date of the non-contingent deliverable in the Collaboration Agreement with the longest term. Our participation in joint committees with Allergan has the longest obligation period, requiring our participation throughout the term of the Collaboration Agreement. The term of the Collaboration Agreement is the later of (a) December 31, 2025, and (b) the date that our last patent right covering LEVADEX in the United States expires. The date that our last patent right covering LEVADEX in the United States expires is 2028. As a result, we will amortize the remaining $55.0 million of the initial $60.0 million through 2028.

During the third quarter ended September 30, 2011, the FDA accepted for filing our LEVADEX NDA. As a result, pursuant to the terms of the Allergan Agreements, Allergan paid us a milestone payment of $20.0 million. We have determined that the achievement of this contingent milestone was substantive and we recorded the $20.0 million as collaboration revenue on our consolidated statements of operations for the year ended December 31, 2011. In addition to the $20.0 million milestone described above, under the terms of the Collaboration Agreement, we may also receive up to an additional $77.0 million in milestone payments, including $50.0 million for the first commercial sale of LEVADEX associated with the initial indication (the acute treatment of migraine), up to $25.0 million for the achievement of certain FDA-approved product labeling in the United States and $2.0 million for regulatory approval of the initial indication for LEVADEX in Canada.

We agreed with Allergan, subsequent to the effective date of the Collaboration Agreement, to begin commercialization activities relating to the initial indication prior to initial approval of LEVADEX, and that those costs would be shared equally between the parties. Any reimbursements from Allergan for shared expenses relating to contingent deliverables are recorded in our financial statements in the quarters in which the cost sharing occurs. Sales, general and administrative expenses for the three and six months ended June 30, 2012 were net of $0.2 million and $0.5 million, respectively, compared to $0.4 million and $0.4 million, respectively, for the same periods of 2011, of costs reimbursed or reimbursable by Allergan under cost-sharing provisions in the Allergan Agreements. Sales, general and administrative expenses for the cumulative period from July 3, 2003 (date of inception) to June 30, 2012 were net of $1.9 million of costs reimbursed or reimbursable by Allergan under cost-sharing provisions in the Allergan Agreements.

Agreement with Nektar

Under our June 2004 agreement, as amended, with Nektar Therapeutics UK Limited, or the Nektar Agreement, we were granted a worldwide, exclusive license, with a right to sublicense, under Nektar patents and know-how, to develop and commercialize any formulation of a form of dihydroergotamine for administration by inhalation using a device. We also agreed to pay royalties at specified rates based on net sales.

We paid $0 for both the three and six months ended June 30, 2012, compared to $0 and $1.0 million, respectively, for the same periods in 2011. We paid $3.6 million for the cumulative period from July 3, 2003 (date of inception) to June 30, 2012. Either party may terminate the Nektar Agreement upon a material, uncured default of the other party. We may terminate the Nektar Agreement, with or without cause, at any time upon six months prior written notice.

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NOTE 4. FAIR VALUE MEASUREMENTS

We adopted ASC 820, *Fair Value Measurements,* as it relates to financial assets and financial liabilities. ASC 820 defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements.

ASC 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This standard is now the single source in GAAP for the definition of fair value, except for the fair value of leased property as defined in ASC 840 *Accounting for Leases,* which establishes a fair value hierarchy that distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity s own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy under ASC 820 are described below:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.

Level 2: Directly or indirectly observable inputs as of the reporting date through correlation with market data, including quoted prices for similar assets and liabilities in active markets and quoted prices in markets that are not active. Level 2 also includes assets and liabilities that are valued using models or other pricing methodologies that do not require significant judgment since the input assumptions used in the models, such as interest rates and volatility factors, are corroborated by readily observable data from actively quoted markets for substantially the full term of the financial instrument.

Level 3: Unobservable inputs that are supported by little or no market activity and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management s estimates of market participant assumptions.

In determining fair value, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, as well as consider counterparty credit risk in our assessment of fair value.

The following is a summary of our cash, cash equivalents and restricted investment as of June 30, 2012 and December 31, 2011, respectively (in thousands):

	As of June 30, 2012		
	Amortized Cost	Unrealized Gain (Loss)	Estimated Fair Value
Cash	$ 3,168	$	$ 3,168
Certificates of deposit	310		310
Money market funds	65,251		65,251
	$ 68,729	$	$ 68,729
Reported as:			
Cash and cash equivalents			$ 68,419
Restricted investment			310
			$ 68,729

	As of December 31, 2011		
	Amortized Cost	Unrealized Gain (Loss)	Estimated Fair Value
Cash	$ 3,569	$	$ 3,569
Certificates of deposit	310		310
Money market funds	95,247		95,247
	$ 99,126	$	$ 99,126
Reported as:			
Cash and cash equivalents			$ 98,816
Restricted investment			310
			$ 99,126

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Our investment instruments are classified within Level 1 or Level 2 of the fair value hierarchy because they are valued using quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. The types of instruments that are generally classified within Level 1 of the fair value hierarchy include money market securities. The types of investments that are generally classified within Level 2 of the fair value hierarchy include U.S. government and agency securities, corporate debt securities and certificates of deposit.

As of June 30, 2012 and December 31, 2011, financial assets measured and recognized at fair value on a recurring basis and classified under the appropriate level of the fair value hierarchy as described above were as follows, respectively (in thousands):

As of June 30, 2012	Level 1	Level 2	Level 3	Total
Certificates of deposit	$	$ 310	$	$ 310
Money market funds	65,251			65,251
Total	$ 65,251	$ 310	$	$ 65,561

As of December 31, 2011	Level 1	Level 2	Level 3	Total
Certificates of deposit	$	$ 310	$	$ 310
Money market funds	95,247			95,247
Total	$ 95,247	$ 310	$	$ 95,557

Our investments in money market funds are measured at fair value on a recurring basis. Our money market funds comply with Rule 2a-7 of the Investment Company Act of 1940 and are required to be priced and have a fair value of $1.00 net asset value per share. These money market funds are actively traded and reported daily through a variety of sources. Due to the structure and valuation required by the Investment Company Act of 1940 regarding Rule 2a-7 funds, the fair value of the money market fund investments is classified as Level 1.

The fair value of the certificates of deposit is classified as Level 2 due to the nature of a contractual restriction in our lease agreement which limits our ability to liquidate the investment.

NOTE 5. BALANCE SHEET COMPONENTS

Accrued Liabilities

Accrued liabilities consist of the following (in thousands):

	June 30, 2012	December 31, 2011
Research and development	$ 2,048	$ 1,367
Payroll and related expenses	3,965	4,888
Professional services	703	596
Other	34	82

	$ 6,750	$ 6,933

NOTE 6. COMMITMENTS AND CONTINGENCIES

Operating Leases

In June 2004, we entered into a lease agreement for laboratory and office facilities in Mountain View, California, or the Lease. The Lease was subsequently amended in August 2006, March 2008 and September 2008. In November 2011, we further amended the Lease, providing for additional square footage in a separate building. The amended lease will expire in June 2013 and contains certain renewal options. Under the Lease, we pay operating costs, including property taxes, insurance and maintenance, in addition to monthly rent. Rent is subject to an annual increase for the duration of the Lease, which we recognize on a straight-line basis.

Rent expense was approximately $0.4 million and $0.8 million, respectively, for the three and six months ended June 30, 2012, compared to $0.3 million and $0.6 million, respectively, for the same periods in 2011. Rent expense was approximately $7.9 million for the cumulative period from July 3, 2003 (date of inception) to June 30, 2012.

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As of June 30, 2012, future minimum lease payments are as follows (in thousands):