RIGEL PHARMACEUTICALS INC
Form 10-Q
November 05, 2013
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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 SEPTEMBER 30, 2013

OR

o 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 0-29889

Rigel Pharmaceuticals, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**94-3248524**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1180 Veterans Blvd. South San Francisco, CA	**94080**
(Address of principal executive offices)	(Zip Code)

(650) 624-1100

(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 o

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 o

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.

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

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

As of October 30, 2013, there were 87,430,342 shares of the registrant s Common Stock outstanding.

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RIGEL PHARMACEUTICALS, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2013

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

RIGEL PHARMACEUTICALS, INC.

CONDENSED BALANCE SHEETS

(In thousands, except share and per share amounts)

	September 30, 2013 (unaudited)	December 31, 2012 (1)
Assets		
Current assets:		
Cash and cash equivalents	$ 16,031	$ 33,484
Available-for-sale securities	214,851	264,757
Prepaid expenses and other current assets	2,131	4,217
Total current assets	233,013	302,458
Property and equipment, net	4,938	5,826
Other assets	1,586	1,759
	$ 239,537	$ 310,043
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 1,025	$ 1,697
Accrued compensation	2,874	6,775
Accrued research and development	2,679	2,124
Other accrued liabilities	652	942
Deferred rent - current portion	1,073	666
Total current liabilities	8,303	12,204
Long-term portion of deferred rent	7,752	8,647
Other long-term liabilities	80	96
Commitments and contingencies		
Stockholders equity:		
Preferred stock		
Common stock	87	87
Additional paid-in capital	1,055,599	1,049,174
Accumulated other comprehensive income	129	82
Accumulated deficit	(832,413)	(760,247)
Total stockholders equity	223,402	289,096
	$ 239,537	$ 310,043

(1) The balance sheet at December 31, 2012 has been derived from the audited financial statements included in Rigel s Annual Report on Form 10-K for the year ended December 31, 2012.

See accompanying Notes.

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RIGEL PHARMACEUTICALS, INC.

CONDENSED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Contract revenues from collaborations	$	$	$ 1,400	$ 2,250
Costs and expenses:				
Research and development	17,574	20,186	57,282	59,014
General and administrative	4,677	5,383	14,964	16,997
Restructuring charges	1,679		1,679	
Total costs and expenses	23,930	25,569	73,925	76,011
Loss from operations	(23,930)	(25,569)	(72,525)	(73,761)
Interest income	106	113	359	393
Net loss	$ (23,824)	$ (25,456)	$ (72,166)	$ (73,368)
Net loss per share, basic and diluted	$ (0.27)	$ (0.36)	$ (0.83)	$ (1.03)
Weighted average shares used in computing net loss per share, basic and diluted	87,430	71,636	87,240	71,505

See accompanying Notes.

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RIGEL PHARMACEUTICALS, INC.

CONDENSED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Net loss	$ (23,824)	$ (25,456)	$ (72,166)	$ (73,368)
Other comprehensive income:				
Unrealized gain on available-for-sale securities	112	69	47	100
Comprehensive loss	$ (23,712)	$ (25,387)	$ (72,119)	$ (73,268)

See accompanying Notes.

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RIGEL PHARMACEUTICALS, INC.

CONDENSED STATEMENTS OF CASH FLOWS

(In thousands)

(unaudited)

	Nine Months Ended September 30,	
	2013	**2012**
Operating activities		
Net loss	$ (72,166)	$ (73,368)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,941	1,797
Stock-based compensation expense	5,603	9,354
Changes in assets and liabilities:		
Prepaid expenses and other current assets	2,086	(141)
Other assets	173	165
Accounts payable	(672)	(168)
Accrued compensation	(3,901)	(1,872)
Accrued research and development	555	203
Other accrued liabilities	(290)	493
Deferred rent and other long term liabilities	(504)	(101)
Net cash used in operating activities	(67,175)	(63,638)
Investing activities		
Purchases of available-for-sale securities	(276,328)	(282,813)
Maturities of available-for-sale securities	309,802	354,826
Sales of available-for-sale securities	16,479	
Capital expenditures	(1,053)	(2,776)
Net cash provided by investing activities	48,900	69,237
Financing activities		
Net proceeds from issuances of common stock	822	2,569
Net cash provided by financing activities	822	2,569
Net (decrease) increase in cash and cash equivalents	(17,453)	8,168
Cash and cash equivalents at beginning of period	33,484	18,633
Cash and cash equivalents at end of period	$ 16,031	$ 26,801

See accompanying Notes.

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Rigel Pharmaceuticals, Inc.

Notes to Condensed Financial Statements

(unaudited)

In this report, Rigel, we, us and our refer to Rigel Pharmaceuticals, Inc.

1. Nature of Operations

We were incorporated in the state of Delaware on June 14, 1996. We are engaged in the discovery and development of novel, small-molecule drugs for the treatment of inflammatory and autoimmune diseases, as well as muscle disorders.

2. Basis of Presentation

Our accompanying unaudited condensed financial statements have been prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP), for interim financial information and pursuant to the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities Act of 1933, as amended (Securities Act). Accordingly, they do not include all of the information and notes required by U.S. GAAP for complete financial statements. These unaudited condensed financial statements include only normal and recurring adjustments that we believe are necessary to fairly state our financial position and the results of our operations and cash flows. Interim-period results are not necessarily indicative of results of operations or cash flows for a full-year or any subsequent interim period. The balance sheet at December 31, 2012 has been derived from audited financial statements at that date, but does not include all disclosures required by U.S. GAAP for complete financial statements. Because all of the disclosures required by U.S. GAAP for complete financial statements are not included herein, these interim unaudited condensed financial statements and the notes accompanying them should be read in conjunction with our audited financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2012.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ from these estimates.

3. Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, that requires an organization to present the effects on the line items of net income of significant amounts reclassified out of Accumulated Other Comprehensive Income, but only if the item reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. ASU No. 2013-02 is effective for fiscal years

beginning after December 15, 2012. We adopted ASU No. 2013-02 on January 1, 2013 on a prospective basis. The adoption had no material effect on our financial position or results of operations.

4. Net loss per share

Basic net loss per share is computed by dividing net loss by the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per share is computed by dividing net earnings by the weighted-average number of shares of common stock outstanding during the period and the number of additional shares of common stock that would have been outstanding if potentially dilutive securities had been issued. Potentially dilutive securities include warrant and stock options and shares issuable under our employee stock purchase plan (Purchase Plan). The dilutive effect of these potentially dilutive securities is reflected in diluted earnings per share by application of the treasury stock method. Under the treasury stock method, an increase in the fair market value of our common stock can result in a greater dilutive effect from potentially dilutive securities.

During the periods presented, we had securities which could potentially dilute basic loss per share, but were excluded from the computation of diluted net loss per share, as their effect would have been antidilutive. These securities consist of the following (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Outstanding options	15,473	13,596	15,473	13,596
Warrant	200	200	200	200
Purchase Plan	52	26	52	36
	15,725	13,822	15,725	13,832

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5. Stock Award Plans

Total stock-based compensation expense related to all of our stock-based awards that we recognized was as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Research and development	$ 1,035	$ 1,866	$ 3,060	$ 5,213
General and administrative	789	1,379	2,304	4,141
Restructuring charges	239		239	
Total stock-based compensation expense	$ 2,063	$ 3,245	$ 5,603	$ 9,354

In September 2013, we announced that we had reduced our workforce by 18% or 30 positions in connection with efforts to prioritize projects and conserve our working capital. As part of the severance arrangement we offered the terminated employees, we extended the date to which the terminated employees had to exercise their vested options to June 30, 2014, rather than 90 days from the termination date as was stipulated under the employee s option agreements pursuant to our equity incentive plan. In addition, we also accelerated the vesting period of certain unvested stock options for one terminated employee. As a result of these modifications, we recorded non-cash stock-based compensation expense of $239,000 in the third quarter of 2013. See Note 11 for further discussion regarding this reduction in our workforce.

The fair value of each option award is estimated on the date of grant using the Black-Scholes option pricing model. We have segregated option awards into the following three homogenous groups for the purposes of determining fair values of options: officers and directors, all other employees, and consultants.

We determined weighted-average valuation assumptions separately for each of these groups as follows:

- Volatility We estimated volatility using the historical share price performance over the expected life of the option up to the point where we have historical market data. We also considered other factors, such as implied volatility, our current clinical trials and other company activities that may affect the volatility of our stock in the future. We determined that at this time historical volatility is more indicative of our expected future stock performance than implied volatility.

- Expected term For options granted to consultants, we use the contractual term of the option, which is generally 10 years, for the initial valuation of the option and the remaining contractual term of the option for the succeeding periods. We worked with various historical data to determine the applicable expected term for each of the other option groups. This data included: (1) for exercised options, the term of the options from option grant date to exercise date; (2) for cancelled options, the term of the options from option grant date to cancellation date, excluding unvested option forfeitures; and (3) for options that remained outstanding at the balance sheet date, the term of the options from option grant date to the end of the reporting period and the estimated remaining term of the options. The consideration and calculation of the above data gave us reasonable estimates of the expected term for each employee group. We also considered the vesting schedules of the options granted and factors surrounding exercise behavior of the option groups, our current market price and company activity that may affect our market price. In addition, we considered the optionee type (i.e., officers and directors or all other employees) and other factors that may affect the expected term of the option.

- Risk-free interest rate The risk-free interest rate is based on U.S. Treasury constant maturity rates with similar terms to the expected term of the options for each option group.

- Dividend yield The expected dividend yield is 0% as we have not paid and do not expect to pay dividends in the future.

Pursuant to FASB ASC 718, we are required to estimate the amount of expected forfeitures when calculating compensation costs. We estimated the forfeiture rate using our historical experience with pre-vesting options. We adjust our stock-based compensation expense as actual forfeitures occur, review our estimated forfeiture rates each quarter and make changes to our estimate as appropriate.

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The following table summarizes the weighted-average assumptions relating to options granted pursuant to our equity incentive plans for the three and nine months ended September 30, 2013 and 2012:

	Equity Incentive Plans Three Months Ended September 30,		Equity Incentive Plans Nine Months Ended September 30,	
	2013	2012	2013	2012
Risk-free interest rate	1.5%	0.7%	1.0%	0.9%
Expected term (in years)	5.0	5.0	5.4	5.5
Dividend yield	0.0%	0.0%	0.0%	0.0%
Expected volatility	69.5%	83.9%	72.5%	81.6%

The exercise price of stock options is at the market price of our common stock on the date immediately preceding the date of grant. Options become exercisable at varying dates and generally expire 10 years from the date of grant. We granted options to purchase 3,034,456 shares of common stock during the nine months ended September 30, 2013, with a grant-date weighted-average fair value of $3.40 per share. We granted options to purchase 2,135,016 shares of common stock during the nine months ended September 30, 2012, with a grant-date weighted-average fair value of $5.44 per share. As of September 30, 2013, there was approximately $8.3 million of total unrecognized stock-based compensation cost, net of estimated forfeitures, related to unvested options granted under our equity incentive plans. At September 30, 2013, there were 9,104,761 shares of common stock available for future grant under our equity incentive plans and no options to purchase shares were exercised during the nine months ended September 30, 2013.

Employee Stock Purchase Plan

The fair value of awards granted under our Purchase Plan is estimated on the date of grant using the Black-Scholes option pricing model, which uses weighted-average assumptions. Our Purchase Plan provides for a twenty-four month offering period comprised of four six-month purchase periods with a look-back option. A look-back option is a provision in our Purchase Plan under which eligible employees can purchase shares of our common stock at a price per share equal to the lesser of 85% of the fair market value on the first day of the offering period or 85% of the fair market value on the purchase date. Our Purchase Plan also includes a feature that provides for a new offering period to begin when the fair market value of our common stock on any purchase date during an offering period falls below the fair market value of our common stock on the first day of such offering period. This feature is called a reset. Participants are automatically enrolled in the new offering period. We had a reset on July 1, 2013 because the fair market value of our stock on June 28, 2013 was lower than the fair market value of our stock on January 2, 2013, the first day of the offering period. We applied modification accounting in accordance with ASC Topic No. 718, *Stock Compensation*, to determine the incremental fair value associated with this Purchase Plan reset and will recognize the related stock-based compensation expense according to FASB ASC Subtopic No. 718-50, *Employee Share Purchase Plan*. The total incremental fair value for the above Purchase Plan reset was approximately $682,000 that is being amortized from July 1, 2013 to June 30, 2015.

As of September 30, 2013, there were approximately 178,037 shares reserved for future issuance under the Purchase Plan. The following table summarizes the weighted-average assumptions related to our Purchase Plan for the nine months ended September 30, 2013 and 2012. Expected volatilities for our Purchase Plan are based on the historical volatility of our stock. Expected term represents the weighted-average of the purchase periods within the offering period. The risk-free interest rate for periods within the expected term is based on U.S. Treasury constant maturity rates.

	Employee Stock Purchase Plan Nine Months Ended September 30,	
	2013	2012
Risk-free interest rate	0.2%	0.2%
Expected term (in years)	1.4	1.2
Dividend yield	0.0%	0.0%
Expected volatility	64.4%	47.3%

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6. Revenue Recognition

We present revenue from our collaboration arrangements under the FASB ASC 808, *Collaboration Arrangements*. Our revenue arrangements with multiple elements are evaluated under FASB ASC 605-25, *Multiple-Element Arrangements* (as amended by ASU No. 2009-13), and are divided into separate units of accounting if certain criteria are met, including whether the delivered element has standalone value to the customer, whether the arrangement includes a general right of return relative to the delivered element and whether delivery or performance of the undelivered element is considered probable and substantially under our control. The consideration we receive under collaboration arrangements is allocated among the separate units of accounting based on the selling price hierarchy, and the applicable revenue recognition criteria is applied to each of the separate units. Advance payments received in excess of amounts earned are classified as deferred revenue until earned.

Revenues associated with substantive, at-risk milestones pursuant to collaborative agreements are recognized upon achievement of the milestones. We consider a milestone to be substantive at the inception of the arrangement if it is commensurate with either our performance to achieve the milestone or the enhancement of the value of the delivered item as a result of a specific outcome resulting from our performance to achieve the milestone, it relates solely to past performance and it is reasonable relative to all of the deliverables and payment terms within the arrangement. Non-refundable contingent future amounts receivable in connection with future events specified in collaboration agreements that are not considered milestones will be recognized as revenue when payments are earned from our collaborators through their completion or achievement of any underlying events, the amounts are fixed or determinable and collectability is reasonably assured.

7. Research and Development Accruals

We have various contracts with third parties related to our research and development activities. Costs that are incurred but not billed to us as of the end of the period are accrued. We make estimates of the amounts incurred in each period based on the information available to us and our knowledge of the nature of the contractual activities generating such costs. Clinical trial contract expenses are accrued based on units of activity reported by third parties. Expenses related to other research and development contracts, such as research contracts, toxicology study contracts and manufacturing contracts are estimated to be incurred generally on a straight-line basis over the duration of the contracts. Raw materials and study materials purchased for us by third parties are expensed at the time of purchase.

8. Sponsored Research and License Agreements

We conduct research and development programs independently and in connection with our corporate collaborators. We currently do not have significant active collaborations.

AstraZeneca

Fostamatinib

In February 2010, we entered into an exclusive worldwide license agreement with AstraZeneca AB (AZ) for the development and commercialization of our oral spleen tyrosine kinase (SYK) inhibitors for the treatment of human diseases other than those primarily involving respiratory or pulmonary dysfunction. The agreement included a license of rights to fostamatinib, our late-stage investigational product candidate for the treatment of rheumatoid arthritis (RA) and other indications. AZ was responsible for conducting and funding all future development, regulatory filings, manufacturing and global commercialization of products containing most of our oral SYK inhibitors. The agreement became effective on March 26, 2010, and we received an upfront payment from AZ of $100.0 million in April 2010. In September 2010, we earned $25.0 million from AZ for completing the transfer of the fostamatinib long-term open label extension study to AZ and for their initiation of Phase 3 clinical trials in the fostamatinib program by AZ.

In June 2013, based on the totality of the results of the OSKIRA Phase 3 program in patients with RA, AZ informed us that it would not proceed with regulatory filings and, instead would return the rights to the compound to us. AZ is solely responsible for all costs and expenses incurred by both parties in connection with the transfer of responsibilities up to December 4, 2013.

In September 2013, we announced that we would not continue further development of fostamatinib for the treatment of RA or lymphoma due to insufficient efficacy findings from recent clinical trials and the competitive landscape in those indications.

Other Agreements

We have several active collaborations with additional several partners. Under these collaborations, which we enter into in the ordinary course of business, we received or may be entitled to receive upfront cash payments, progress dependent contingent payments and royalties on any net sales of products under the agreements. Total future contingent payments to us under all of these current collaborations could exceed $160.0 million if all potential product candidates achieved all of the

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payment triggering events under all of our current collaborations (based on a single product candidate under each agreement). Of this amount, up to $68.9 million relates to the achievement of development events, up to $53.6 million relates to the achievement of regulatory events and up to $37.5 million relates to the achievement of commercial or launch events.

Since we do not control the research, development or commercialization of the product candidates generated under these collaborations, we are not able to reasonably estimate when, if at all, any contingent payments may be payable to us. As such, the contingent payments we could receive thereunder involve a substantial degree of risk to achieve and may never be received. Accordingly, we do not expect, and investors should not assume, that we will receive all of the potential contingent payments provided for under these collaborations and it is possible that we may never receive any additional significant contingent payments under these collaborations.

In June 2012, we entered into an exclusive worldwide license agreement with AZ for the development and commercialization of our program, R256, an inhaled janus kinase (JAK) inhibitor shown to inhibit interleukin (IL)-13 and IL-4 signaling, which is being investigated as a treatment for moderate to severe chronic asthma. AZ will be responsible for beginning the first-in-human clinical studies for R256, and for designing and conducting the clinical development of the compound. AZ will also have exclusive rights to commercialize R256 around the world. AZ paid us an upfront payment of $1.0 million in July 2012. Under the agreement, we were obligated to provide the following deliverables: (i) granting a license of rights to our program, and (ii) delivery of a small batch of compound to AZ. We concluded that these deliverables should be accounted for as separate units of accounting. As our obligations with respect to the deliverables were achieved by June 30, 2012, we recognized revenue of $1.0 million in the second quarter of 2012.

In June 2011, we entered into an exclusive license agreement with BerGenBio AS (BerGenBio) for the development and commercialization of an oncology program. BerGenBio is responsible for all activities it wishes to perform under the license we granted to it. In July 2012, we received a payment of $500,000 from BerGenBio which we recognized as revenue in the second quarter of 2012.

In August 2002, we entered into a collaboration agreement with Daiichi Sankyo (Daiichi) to pursue research related to a specific target from a novel class of drug targets called ligases that control cancer cell proliferation through protein degradation. In April 2013, we received a $1.4 million payment from Daiichi related to the filing of an IND for an oncology compound. In January 2012, we received a $750,000 payment from Daiichi related to an oncology compound in pre-clinical testing at Daiichi. We have earned, to date, payments under this arrangement totaling $7.9 million and may earn additional payments in connection with the achievement of certain clinical events. The research phase of this three-year collaboration expired in August 2005. Under the terms of the collaboration agreement, we retain the rights to co-develop and co-promote certain products resulting from this collaboration in North America, while Daiichi retains co-development and promotion rights in the remainder of the world. Future events that may trigger payments to us under the Daiichi agreement are based solely on Daiichi s future efforts and achievements of specified events.

9. Cash, Cash Equivalents and Available-For-Sale Securities

Cash, cash equivalents and available-for-sale securities consisted of the following (in thousands):

	September 30, 2013	December 31, 2012

Checking account	$	94	$	251
Money market funds		14,437		23,936
U. S. treasury bills		2,104		
Government-sponsored enterprise securities		80,867		77,047
Corporate bonds and commercial paper		133,380		197,007
	$	230,882	$	298,241
Reported as:				
Cash and cash equivalents	$	16,031	$	33,484
Available-for-sale securities		214,851		264,757
	$	230,882	$	298,241

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Cash equivalents and available-for-sale securities include the following securities with unrealized gains and losses (in thousands):

September 30, 2013	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U. S. treasury bills	$ 2,102	$ 2	$	$ 2,104
Government-sponsored enterprise securities	80,809	60	(2)	80,867
Corporate bonds and commercial paper	133,311	75	(6)	133,380
Total	$ 216,222	$ 137	$ (8)	$ 216,351

December 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Government-sponsored enterprise securities	$ 77,041	$ 37	$ (31)	$ 77,047
Corporate bonds and commercial paper	196,931	98	(22)	197,007
Total	$ 273,972	$ 135	$ (53)	$ 274,054

As of September 30, 2013, the contractual maturities of our cash equivalents and available-for-sale securities were (in thousands):

	Years to Maturity	
	Within One Year	After One Year Through Two Years
U. S. treasury bills	$	$ 2,104
Government-sponsored enterprise securities	53,203	27,664
Corporate bonds and commercial paper	129,885	3,495
	$ 183,088	$ 33,263

As of September 30, 2013, our cash equivalents and available-for-sale securities had a weighted average time to maturity of 218 days. We view our investment portfolio as available for use in current operations. Accordingly, we have classified all of our investments as available-for-sale securities on our balance sheet even though the stated maturity date of these securities may be more than one year from the current balance sheet date. In the second quarter of 2013, we sold certain available-for-sale securities at their approximate carrying values prior to maturity and received proceeds of $16.5 million. The cost of securities we sell is determined based on the specific identification method. At each of September 30, 2013 and December 31, 2012, we had no investments that had been in a continuous unrealized loss position for more than 12 months. As of September 30, 2013, a total of 14 individual securities had been in an unrealized loss position for 12 months or less and the losses were determined to be temporary.

The following table shows the fair value and gross unrealized losses of our investments in individual securities that are in an unrealized loss position, aggregated by investment category (in thousands):

September 30, 2013	Fair Value	Unrealized Losses
Government-sponsored enterprise securities	$ 2,998	$ (2)

Corporate bonds and commercial paper		28,265		(6)
Total	$	31,263	$	(8)

10. Fair Value

Under FASB ASC 820, *Fair Value Measurements and Disclosures*, fair value is defined as the price at which an asset could be exchanged or a liability transferred in a transaction between knowledgeable, willing parties in the principal or most advantageous market for the asset or liability. Where available, fair value is based on observable market prices or parameters or derived from such prices or parameters. Where observable prices or parameters are not available, valuation models are applied.

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Assets and liabilities recorded at fair value in our financial statements are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Hierarchical levels directly related to the amount of subjectivity associated with the inputs to fair valuation of these assets and liabilities, are as follows:

Level 1 Inputs are unadjusted, quoted prices in active markets for identical assets at the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

The fair valued assets we hold that are generally included under this Level 1 are money market securities where fair value is based on publicly quoted prices.

Level 2 Are inputs, other than quoted prices included in Level 1, that are either directly or indirectly observable for the asset or liability through correlation with market data at the reporting date and for the duration of the instrument s anticipated life.

The fair valued assets we hold that are generally assessed under Level 2 included government-sponsored enterprise securities and corporate bonds and commercial paper. We utilize third party pricing services in developing fair value measurements where fair value is based on valuation methodologies such as models using observable market inputs, including benchmark yields, reported trades, broker/dealer quotes, bids, offers and other reference data. We use quotes from external pricing service providers and other on-line quotation systems to verify the fair value of investments provided by our third party pricing service providers. We review independent auditor s reports from our third party pricing service providers particularly regarding the controls over pricing and valuation of financial instruments and ensure that our internal controls address certain control deficiencies, if any, and complementary user entity controls are in place.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities and which reflect management s best estimate of what market participants would use in pricing the asset or liability at the reporting date. Consideration is given to the risk inherent in the valuation technique and the risk inherent in the inputs to the model.

We do not have fair valued assets classified under Level 3.

Fair Value on a Recurring Basis

Financial assets measured at fair value on a recurring basis are categorized in the tables below based upon the lowest level of significant input to the valuations (in thousands):

	Assets at Fair Value as of September 30, 2013			
	Level 1	**Level 2**	**Level 3**	**Total**

Money market funds	$ 14,437	$	$	$ 14,437
U. S. treasury bills		2,104		2,104
Government-sponsored enterprise securities		80,867		80,867
Corporate bonds and commercial paper		133,380		133,380
Total	$ 14,437	$ 216,351	$	$ 230,788

	Assets at Fair Value as of December 31, 2012			
	Level 1	Level 2	Level 3	Total
Money market funds	$ 23,936	$	$	$ 23,936
Government-sponsored enterprise securities		77,047		77,047
Corporate bonds and commercial paper		197,007		197,007
Total	$ 23,936	$ 274,054	$	$ 297,990

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11. Restructuring Charges

In September 2013, we announced that we had reduced our workforce by 30 positions, mostly from the drug discovery area, as a consequence of prioritizing projects and looking to conserve our working capital. We recorded restructuring charges in the third quarter of 2013 of approximately $1.7 million within Restructuring Charges, which included $1.5 million of costs paid or to be paid in cash, and $239,000 of non-cash stock-based compensation expense primarily as a result of the modification of certain stock options (see Note 5). At September 30, 2013, the remaining accrued restructuring costs consists of $171,000 related to COBRA benefits for the fourth quarter of 2013. This accrued liability is classified under accrued compensation on the balance sheet.

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

This discussion and analysis should be read in conjunction with our financial statements and the accompanying notes included in this report and the audited financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2012. Operating results for the three and nine months ended September 30, 2013 are not necessarily indicative of results that may occur in future interim periods or for the full fiscal year.

This Quarterly Report on Form 10-Q contains statements indicating expectations about future performance and other forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Exchange Act, that involve risks and uncertainties. We usually use words such as may, will, should, could, expect, plan, anticipate, believe, estimate, predict, intend, or the negative of these terms or similar expressions to identify these forward-looking statements. These statements appear throughout this Quarterly Report on Form 10-Q and are statements regarding our current expectation, belief or intent, primarily with respect to our operations and related industry developments. Examples of these statements include, but are not limited to, statements regarding the following: our business and scientific strategies; the progress of our and our collaborators product development programs, including clinical testing, and the timing of results thereof; the potential impact of our cost reduction plans and reduction in workforce, our corporate collaborations and revenues that may be received from our collaborations and the timing of those potential payments; our expectations with respect to regulatory submissions and approvals; our drug discovery technologies; our research and development expenses; protection of our intellectual property; sufficiency of our cash and capital resources and the need for additional capital; and our operations and legal risks. You should not place undue reliance on these forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including as a result of the risks and uncertainties discussed under the heading Risk Factors in Item 1A of Part II of this Quarterly Report on Form 10-Q. Any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for us to predict which factors will arise. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Overview

We are a clinical-stage drug development company that discovers and develops novel, small-molecule drugs for the treatment of inflammatory and autoimmune diseases, as well as muscle disorders. Our pioneering research focuses on intracellular signaling pathways and related targets that are critical to disease mechanisms. We currently have five product candidates in development: fostamatinib, an oral SYK inhibitor for ITP that we expect to commence Phase 3 clinical trials; R348, a topical JAK/SYK inhibitor for dry eye in Phase 2 clinical trials; R118, an AMPK activator entering Phase 1 in early 2014; and two oncology product candidates in Phase 1 development with partners BerGenBio AS and Daiichi Sankyo.

Since inception, we have financed our operations primarily through the sale of equity securities, contract payments under our collaboration agreements and equipment financing arrangements. Our research and development activities, including preclinical studies and clinical trials, consume substantial amounts of capital. As of September 30, 2013, we had approximately $230.9 million in cash, cash equivalents and available-for-sale securities. We believe that our existing capital resources will be sufficient to support our current and projected funding requirements through at least the next 12 months. Unless and until we are able to generate a sufficient amount of product, royalty or milestone revenue, we expect to finance future cash needs through public and/or private offerings of equity securities, debt financings or collaboration and licensing arrangements, as well as through interest income earned on the investment of our cash balances and short-term investments. With the exception of contingent and royalty payments that we may receive under our existing collaborations, we do not currently have any commitments for future funding.

Product Development Programs

Our product development portfolio features multiple novel, small-molecule drug candidates whose specialized mechanisms of action are intended to provide therapeutic benefit for a range of inflammatory and autoimmune diseases, as well as muscle disorders.

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Clinical Stage Programs

Fostamatinib - Immune Thrombocytopenic Purpura

Disease background. Chronic ITP affects approximately 100,000 people, with the majority of these cases being in women. ITP is a blood disorder in which the immune system attacks and destroys the body s own blood platelets, which have an important role in the clotting and healing process. ITP patients can suffer bruising, bleeding and fatigue as a result of their low blood platelet counts. Currently marketed therapies aim to raise blood platelet counts, but do not address the etiology of the disorder.

Orally-available SYK inhibitor program. Platelet destruction from ITP is mediated by IgG signaling, and fostamatinib is a potent inhibitor of IgG signaling. The results of our Phase 2 study of fostamatinib to evaluate its safety and initial efficacy in chronic ITP patients, published in *Blood (volume 113, number 14)*, showed that fostamatinib may be effective in treating this rare autoimmune disorder. In this clinical trial, fostamatinib was orally administered in varying doses for 30 or more days and demonstrated that it can improve platelet counts in highly refractory patients.

In October 2013, we met with the U.S. Food and Drug Administration (FDA) for an end-of-Phase 2 meeting for fostamatinib in ITP. We expect to initiate two pivotal Phase 3 studies in the first half of 2014. Each of these trials is expected to enroll approximately 75 patients who would be treated for six months and have the option to enroll in an extension study. These trials will be randomized, placebo-controlled and will enroll verified ITP patients with platelet counts below 30,000 platelets per microliter of blood. The goal of the trials will be to achieve a durable platelet count increase to over 50,000 platelets per microliter of blood. We expect top line data from these studies in 2015.

Fostamatinib Rheumatoid Arthritis

Disease background. RA is a systemic autoimmune inflammatory disease that causes damage to the joints and other organs, affecting approximately 1 in 100 people in the United States. It is a major cause of disability and is also associated with reduced life expectancy, especially if it is not adequately treated.

In September 2013, we announced that we would not continue further development of fostamatinib for the treatment of RA or lymphoma due to insufficient efficacy findings from recent clinical trials and the competitive landscape in those indications.

OSKIRA

The (Oral SYK Inhibition in Rheumatoid Arthritis) OSKIRA program was designed to investigate fostamatinib as a potential new oral treatment option for RA and an alternative to injectable therapies for patients with an inadequate response to conventional disease modifying

anti-rheumatic drugs (DMARDs). OSKIRA-1 was a 12-month study with approximately 900 patients, examining the effect of fostamatinib compared with placebo over a 24 week period, in patients responding inadequately to MTX. OSKIRA-1 had co-primary endpoints of American College of Rheumatology (ACR)20 scores and mTSS (x-ray endpoint assessing structural progression) at 24 weeks. OSKIRA-2 was a 12-month study with approximately 900 patients, examining the effect of fostamatinib compared with placebo over a 24 week period, in patients responding inadequately to DMARDs. OSKIRA-2 had a primary endpoint of ACR20 at 24 weeks. OSKIRA-3 was a six-month study of approximately 320 patients assessing the effect of fostamatinib compared with placebo in patients responding inadequately to TNF- antagonist therapy. The primary endpoint of OSKIRA-3 was ACR20 at 24 weeks.

In June 2013, AZ announced the topline results from OSKIRA-2 and OSKIRA-3, two pivotal Phase 3 clinical trials investigating fostamatinib, the first oral SYK inhibitor in development for RA. In the OSKIRA-2 study of patients inadequately responding to DMARDs, fostamatinib in combination with DMARDs showed statistically significant improvements in ACR20 response rates at 24 weeks compared to placebo. In the OSKIRA-3 study of patients inadequately responding to MTX and a single TNF-alpha antagonist, fostamatinib in combination with MTX showed statistically significant improvements in ACR20 response rates at 24 weeks in the 100mg twice daily group but not in the group given 100mg twice daily for four weeks followed by 150mg once daily compared to placebo. The safety and tolerability findings for fostamatinib observed in the OSKIRA Phase 3 program were generally consistent with those previously reported in earlier studies. The most commonly reported adverse events in the OSKIRA program include hypertension, diarrhea, nausea, headache and nasopharyngitis (common cold).

Based on the totality of the results of the OSKIRA Phase 3 program in patients with RA, in June 2013, AZ informed us that it would not proceed with regulatory filings and, instead would return the rights to the compound to us. AZ is solely responsible for all costs and expenses incurred by both parties in connection with the transfer of responsibilities within 180 days from the date of written notice of termination, which was June 7, 2013.

In April 2013, AZ announced top-line results of OSKIRA-1, a Phase 3 study to assess the efficacy and safety of fostamatinib. OSKIRA-1 had two primary endpoints: assessing signs and symptoms of RA as measured by ACR20 response

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rates, and an X-ray endpoint known as mTSS (modified Total Sharp Score). In the OSKIRA-1 study, fostamatinib achieved a statistically significant improvement in ACR 20 response rate at 24 weeks compared to placebo. Fostamatinib did not demonstrate a statistically significant difference in mTSS compared to placebo at 24 weeks. The safety and tolerability findings for fostamatinib observed in the OSKIRA-1 study were generally consistent with those previously reported for the *TASKi* Phase 2 program. The most commonly reported adverse events were typical of those seen in earlier studies, including hypertension, diarrhea, nausea, headache and nasopharyngitis (common cold).

Fostamatinib Other Indications

In addition to RA, fostamatinib had been studied in patients with other immune disorders and some cancers. AZ commenced Phase 2 clinical trials to investigate the effect of fostamatinib on hematological malignancies in the first quarter of 2012. The randomized double-blind Phase 2 clinical trial was designed to evaluate the effectiveness of two doses of fostamatinib (100mg twice daily and 200mg twice daily) in patients with worsening or unmanageable diffuse large B-cell lymphoma. As discussed above, we have decided not to continue further development of fostamatinib for the treatment of lymphoma.

R343 Asthma

Disease background. Allergic asthma is a chronic inflammatory disorder of the airways. Asthma affects the lower respiratory tract and is marked by episodic flare-ups, or attacks, that can be life threatening. In some patients, allergens, such as pollen, trigger the production of immunoglobulin E (IgE) antibodies, which then bind to mast cells and cause an intracellular signal that results in the release of various chemical mediators. When this process occurs repeatedly over time, it creates persistent inflammation of the airway passages, resulting in the chronic congestion and airway obstruction associated with allergic rhinitis and asthma, respectively.

Inhaled SYK inhibitor program. R343 is a potent SYK inhibitor that blocks IgE receptor signaling. Mast cells play important roles in both early and late phase allergic reactions, and SYK inhibitors could potentially prevent both phases. Based on its mechanism of action, this inhaled SYK inhibitor may provide a new treatment paradigm for the largest group of patients with allergic asthma whose symptoms range from acute to chronic phases of the disease.

In 2005, we announced a collaborative research and license agreement with Pfizer, Inc. (Pfizer) for the development of inhaled products for the treatment of allergic asthma. The collaboration was focused on our preclinical small-molecule compounds, which inhibit SYK. R343 was the oral SYK inhibitor small molecule at the center of this collaboration. Pfizer completed the Phase 1a clinical trial of an inhaled formulation of R343, which commenced in December 2007 and resulted in a payment of $5.0 million to us. Pfizer also completed an initial Phase 1b allergen challenge clinical trial. In 2011, we assumed development of R343 after Pfizer returned full rights to the R343 program to us as a result of its decision to exit research and development in the allergy and respiratory therapeutic area, and the collaborative research and license agreement was terminated.

SITAR. In August 2013, we announced that R343, an inhaled SYK inhibitor being evaluated as a potential therapeutic for patients with allergic asthma, did not meet the primary or secondary endpoints in a recently completed Phase 2 clinical study. The primary endpoint was the change in pre-bronchodilator FEV1 (a measure of lung function) from baseline to dosing completion at Week 8, comparing active doses to placebo. R343 was shown to be relatively safe and well tolerated at both doses. The Phase 2 clinical study, called SITAR (SYK Inhibition for Treatment

of Asthma with R343), was designed to randomize approximately 270 adults with allergic asthma into the three arms of the study for eight weeks of treatment with either of two different doses of the study agent or placebo. R343 is being delivered directly into the lungs via a dry powder inhalation device. In light of these overall findings, we have decided not to move forward with R343.

R333 Discoid Lupus Erythematosus (DLE)

Disease background. DLE is an autoimmune disease of the skin characterized by disc-shaped sores with inflammation, swelling, scaling, scarring, pigment discoloration and hair loss. The lesions most commonly appear in sun exposed areas, predominantly on the face, chest and scalp. This disease has an acute phase, which research has connected to SYK signaling within the immune cascade. There is also a chronic phase of the disease due to the abundance of JAK signaling. Current treatments for DLE have either poor efficacy or significant toxicities.

Topical Dermatological JAK/SYK inhibitor program. R333 is a topical dermatological JAK/SYK inhibitor, which may be useful in treating both the acute and chronic phases of DLE. We completed the Phase 1 clinical study of its topical agent to test its application in treating acute and chronic phases of DLE in the first half of 2012.

SKINDLE. In October 2013, we announced that R333, which was being evaluated as a potential therapeutic for active skin lesions in patients with DLE in a Phase 2 clinical study, called SKINDLE (SYK Kinase Inhibition for DLE), did not meet the primary endpoint in a recently completed Phase 2 clinical study. The primary endpoint was the proportion of

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patients who achieved at least a 50% decrease from baseline in the total combined Erythema and Scaling score of all treated lesions at Week 4. R333 was shown to be relatively safe and well tolerated. In light of these overall findings, we have decided not to pursue this indication further with R333.

R348 Keratoconjunctivitis Sicca

Disease background. Chronic dry eye, or keratoconjunctivitis sicca, an inflammatory disease that often affects the lacrimal (tear producing) glands of the eye. Over five million Americans suffer with this disorder, and many patients with chronic dry eye may also suffer with autoimmune conditions, including systemic lupus erythematosus and rheumatoid arthritis. Chronic dry eye is an irritating and painful disease that may be destructive to the cornea if not well controlled.

Topical Ophthalmic JAK/SYK inhibitor program. Since both JAK and SYK are important components in the body s immune and inflammatory responses, R348 s combined JAK/SYK inhibition is expected to offer relief directly to the eye. A recently completed Phase 1 study of R348 in patients with dry eye disease showed that the drug candidate is well tolerated. In July 2013, we initiated a Phase 2 study, called DROPS (Dry Eye Rigel Ophthalmic Phase 2 Study). This multi-center, randomized, double-masked study, will evaluate two doses of R348 versus placebo administered twice a day over a three-month period in approximately 210 patients with dry eye disease. The efficacy endpoints will include change from baseline in corneal staining, tear production and dry eye symptom scores. Results of this Phase 2 study are expected in the second half of 2014.

Research/Preclinical Programs

We are conducting proprietary research in the broad disease areas of inflammation/immunology and muscle wasting/muscle endurance. Within each disease area, our researchers are investigating mechanisms of action as well as screening compounds against potential novel targets and optimizing those leads that appear to have the greatest potential.

We have active small molecule discovery programs in muscle wasting. Excessive loss of muscle in the context of illness can contribute significantly to both morbidity and mortality rates. Many conditions that have been associated with muscle atrophy, or the loss of muscle mass, including cancer, chronic heart failure, chronic kidney disease, mechanical ventilation and aging (sarcopenia), have significant patient populations that may benefit from therapeutics that counter such muscle loss.

In the area of muscle atrophy and muscle endurance, we are focusing on several signaling pathways that are important for muscle homeostasis. Patients with chronic illnesses such as chronic heart failure, chronic obstructive pulmonary disease (COPD), or diabetes, often experience a decrease in strength and increase in fatigue due to muscle myopathy. We are conducting preclinical studies of an oral activator of adenosine monophosphate (AMP)-activated protein kinase (AMPK) to examine whether it can improve the body s energy utilization and restore muscle endurance in chronically ill subjects. Our focus for this program is to evaluate its potential treatment in patients with peripheral vascular disease who exhibit exercise intolerance. We expect to enter into the clinic with this program in the beginning of 2014.

Corporate Collaborations

We conduct research and development programs independently and in connection with our corporate collaborators. We currently do not have significant active collaborations.

AstraZeneca

Fostamatinib

In February 2010, we entered into an exclusive worldwide license agreement with AZ for the development and commercialization of our oral SYK inhibitors for the treatment of human diseases other than those primarily involving respiratory or pulmonary dysfunction. The agreement included a license of rights to fostamatinib, our late-stage investigational product candidate for the treatment of RA and other indications. AZ was responsible for conducting and funding all future development, regulatory filings, manufacturing and global commercialization of products containing most of our oral SYK inhibitors. The agreement became effective on March 26, 2010, and we received an upfront payment from AZ of $100.0 million in April 2010. In September 2010, we earned $25.0 million from AZ for completing the transfer of the fostamatinib long-term open label extension study to AZ and for the initiation of Phase 3 clinical trials in the fostamatinib program by AZ.

In June 2013, based on the totality of the results of the OSKIRA Phase 3 program in patients with RA, AZ informed us that it would not proceed with regulatory filings and, instead would return the rights to the compound to us. AZ is solely responsible for all costs and expenses incurred by both parties in connection with the transfer of responsibilities up to December 4, 2013.

In September 2013, we announced that we would not continue further development of fostamatinib for the treatment of RA or lymphoma due to insufficient efficacy findings from recent clinical trials and the competitive landscape in those indications.

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Other Agreements

We have several active collaborations with additional partners. Under these collaborations, which we enter into in the ordinary course of business, we received or may be entitled to receive upfront cash payments, progress dependent contingent payments and royalties on any net sales of products under the agreements. Total future contingent payments to us under all of these current collaborations could exceed $160.0 million if all potential product candidates achieved all of the payment triggering events under all of our current collaborations (based on a single product candidate under each agreement). Of this amount, up to $68.9 million relates to the achievement of development events, up to $53.6 million relates to the achievement of regulatory events and up to $37.5 million relates to the achievement of commercial or launch events.

Since we do not control the research, development or commercialization of the product candidates generated under these collaborations, we are not able to reasonably estimate when, if at all, any contingent payments may be payable to us. As such, the contingent payments we could receive thereunder involve a substantial degree of risk to achieve and may never be received. Accordingly, we do not expect, and investors should not assume, that we will receive all of the potential contingent payments provided for under these collaborations and it is possible that we may never receive any additional significant contingent payments under these collaborations.

In June 2012, we entered into an exclusive worldwide license agreement with AZ for the development and commercialization of our program, R256, an inhaled JAK inhibitor shown to inhibit IL-13 and IL-4 signaling, which is being investigated as a treatment for moderate to severe chronic asthma. AZ will be responsible for beginning the first-in-human clinical studies for R256, and for designing and conducting the clinical development of the compound. AZ will also have exclusive rights to commercialize R256 around the world. AZ paid us an upfront payment of $1.0 million in July 2012. Under the agreement, we were obligated to provide the following deliverables: (i) granting a license of rights to our program, and (ii) delivery of a small batch of compound to AZ. We concluded that these deliverables should be accounted for as separate units of accounting. As our obligations with respect to the deliverables were achieved by June 30, 2012, we recognized revenue of $1.0 million in the second quarter of 2012.

In June 2011, we entered into an exclusive license agreement with BerGenBio for the development and commercialization of an oncology program. BerGenBio is responsible for all activities it wishes to perform under the license we granted to it. In July 2012, we received a payment of $500,000 from BerGenBio due to us 12 months from June 29, 2011, the effective date of the agreement. We recognized the payment as revenue in the second quarter of 2012.

In August 2002, we entered into a collaboration agreement with Daiichi to pursue research related to a specific target from a novel class of drug targets called ligases that control cancer cell proliferation through protein degradation. In April 2013, we received a $1.4 million payment from Daiichi related to the filing of an investigational new drug (IND) application for an oncology compound. In January 2012, we received a $750,000 payment from Daiichi related to an oncology compound in pre-clinical testing at Daiichi. We have earned, to date, payments under this arrangement totaling $7.9 million and may earn additional payments in connection with the achievement of certain clinical events. The research phase of this three-year collaboration expired in August 2005. Under the terms of the collaboration agreement, we retain the rights to co-develop and co-promote certain products resulting from this collaboration in North America, while Daiichi retains co-development and promotion rights in the remainder of the world. Future events that may trigger payments to us under the Daiichi agreement are based solely on Daiichi s future efforts and achievements of specified events.

Research and Development Expenses

Our research and development expenditures include costs related to preclinical and clinical trials, scientific personnel, supplies, equipment, consultants, sponsored research, stock-based compensation, and allocated facility costs.

We do not track fully-burdened research and development costs separately for each of our drug candidates. We review our research and development expense by focusing on three categories: research, development, and other. Our research team is focused on creating a portfolio of product candidates that can be developed into small-molecule therapeutics in our own proprietary programs or with potential collaborative partners and utilizes our robust discovery engine to rapidly discover and validate new product candidates in our focused range of therapeutic indications. Research expenses relate primarily to personnel expenses, lab supplies, fees to third party research consultants and compounds. Our development group leads the implementation of our clinical and regulatory strategies and prioritizes disease indications in which our compounds may be studied in clinical trials. Development expenses relate primarily to clinical trials, personnel expenses, lab supplies and fees to third party research consultants. Other expenses primarily consist of allocated facilities costs and allocated stock-based compensation expense relating to personnel in research and development groups.

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In addition to reviewing the three categories of research and development expense described in the preceding paragraph, we principally consider qualitative factors in making decisions regarding our research and development programs, which include enrollment in clinical trials and the results thereof, the clinical and commercial potential for our drug candidates and competitive dynamics. We also make our research and development decisions in the context of our overall business strategy, which includes the evaluation of potential collaborations for the development of our drug candidates.

The following table presents our total research and development expense by category (in thousands).

	Three Months Ended September 30,		Nine Months Ended September 30,		From January 1, 2007*
Categories:	**2013**	**2012**	**2013**	**2012**	**to September 30, 2013**
Research	$ 5,336	$ 6,165	$ 18,142	$ 18,547	$ 152,001
Development	6,802	7,822	22,975	22,545	220,627
Other	5,436	6,199	16,165	17,922	167,951
	$ 17,574	$ 20,186	$ 57,282	$ 59,014	$ 540,579

* We started tracking research and development expense by category on January 1, 2007.

Other expenses mainly represent allocated facilities costs of approximately $4.4 million and $4.3 million for the three months ended September 30, 2013 and 2012, respectively, and allocated stock-based compensation expenses of approximately $1.0 million and $1.9 million for the three months ended September 30, 2013 and 2012, respectively. For the nine months ended September 30, 2013 and 2012, allocated facilities costs were approximately $13.1 million and $12.7 million, respectively, and allocated stock-based compensation expenses were approximately $3.1 million and $5.2 million, respectively.

For the three and nine months ended September 30, 2013 and 2012, a major portion of our total research and development expense were associated with the salaries of our research and development personnel, research and development expense for our asthma program, topical ophthalmic JAK/SYK inhibitor program, topical JAK/SYK inhibitor program and AMPK activator program, as well as allocated facilities costs.

The scope and magnitude of future research and development expense are difficult to predict given the number of clinical trials that we will need to conduct for any of our potential products, as well as our limited capital resources. Preclinical testing and clinical development are long, expensive and uncertain processes. In general, biopharmaceutical development involves a series of steps, beginning with identification of a potential target and including, among others, proof of concept in animals and Phase 1, 2 and 3 clinical trials in humans. Each of these steps is typically more expensive than the previous step. Success in early stages of development often results in increasing expenditures for a given product candidate. Significant delays in clinical testing could materially impact our product development costs and timing of completion of the clinical trials. We do not know whether planned clinical trials will begin on time, will need to be halted or revamped or will be completed on schedule, or at all. Clinical trials can be delayed for a variety of reasons, including delays in obtaining regulatory approval to commence a trial, delays from scale up, delays in reaching agreement on acceptable clinical trial agreement terms with prospective clinical sites, delays in obtaining institutional review board approval to conduct a clinical trial at a prospective clinical site or delays in recruiting subjects to participate in a clinical study.

We currently do not have reliable estimates of total costs for a particular drug candidate to reach the market. Our potential products are subject to a lengthy and uncertain regulatory process that may involve unanticipated additional clinical trials and may not result in receipt of the necessary regulatory approvals. Failure to receive the necessary regulatory approvals would prevent us from commercializing the product candidates affected. In addition, clinical trials of our potential products may fail to demonstrate safety and efficacy, which could prevent or significantly delay regulatory approval. We do not have a reasonable basis to determine when or if material net cash inflows from the commercialization and sale of our drug candidates will occur. Commercialization of our product candidates depends upon successful completion of extensive preclinical studies and clinical trials to demonstrate their safety and efficacy for humans. We do not know whether we, or any of our current or potential future collaborative partners, will undertake clinical trials of potential products beyond the trials already concluded and the trials currently in process. It will take us, or our current or potential future collaborative partners, several years to complete any such testing, and failure can occur at any stage of testing. Interim results of trials do not necessarily predict final results, and acceptable results in early trials may not be repeated in later trials. Moreover, we or our current or potential future collaborative partners may decide to discontinue development of any project at any time for regulatory, commercial, scientific or other reasons. To date, we have not commercialized any of our drug candidates, and we may never do so.

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For a discussion of the risks and uncertainties associated with the timing and costs of completing the development of our drug candidates, see Part I. Item 1A. Risk Factors, including in particular the following risks:

- We will need additional capital in the future to sufficiently fund our operations and research.
- We might not be able to commercialize our product candidates successfully if problems arise in the clinical testing and approval process.
- There is a high risk that drug discovery and development efforts might not successfully generate good product candidates.
- If our corporate collaborations or license agreements are unsuccessful, or if we fail to form new corporate collaborations or license agreements, our research and development efforts could be delayed.
- If conflicts arise between our collaborators or advisors and us, any of them may act in their self-interest, which may be adverse to our stockholders interests.
- If we are unable to obtain regulatory approval to market products in the United States and foreign jurisdictions, we will not be permitted to commercialize products from our research and development.
- Because we expect to be dependent upon collaborative and license agreements, we might not meet our strategic objectives.
- Delays in clinical testing could result in increased costs to us.
- We lack the capability to manufacture compounds for development and rely on third parties to manufacture our product candidates, and we may be unable to obtain required material in a timely manner, at an acceptable cost or at a quality level required to receive regulatory approval.

For further discussion on research and development activities, see Research and Development Expense under Results of Operations below.

Recent Accounting Pronouncements

In February 2013, the FASB issued ASU No. 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income*, that requires an organization to present the effects on the line items of net income of significant amounts reclassified out of Accumulated Other Comprehensive Income, but only if the item reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. ASU No. 2013-02 is effective for fiscal years beginning after December 15, 2012. We adopted ASU No. 2013-02 on January 1, 2013 on a prospective basis. The adoption had no material effect on our financial position or results of operations.

Critical Accounting Policies and the Use of Estimates

Our discussion and analysis of our financial condition and results of operations is based upon our financial statements, which have been prepared in accordance with U.S. GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. We evaluate our estimates, including those related to the terms of our research and development collaborations (i.e. revenue recognition of upfront fees and certain contingent payments), investments, stock-based compensation, impairment issues, the estimated useful life of assets, and estimated accruals and contingencies, on an on-going basis. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our financial statements:

Revenue Recognition

We present revenue from our collaboration arrangements under the FASB ASC 808, *Collaboration Arrangements*. Our revenue arrangements with multiple elements are evaluated under FASB ASC 605-25, *Multiple-Element Arrangements* (as amended by ASU No. 2009-13), and are divided into separate units of accounting if certain criteria are met. The consideration we receive under collaboration arrangements is allocated among the separate units of accounting based on the selling price hierarchy, and the applicable revenue recognition criteria is applied to each of the separate units. We make significant judgments and estimates in the allocation of the consideration among the deliverables under the agreement, as well as the determination of the periods the units will be delivered to our collaborators.

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Stock-based Compensation

The determination of the fair value of stock-based payment awards on the date of grant using the Black-Scholes option-pricing model is affected by our stock price as well as assumptions regarding a number of complex and subjective variables. These variables include, but are not limited to, volatility, expected term, risk-free interest rate and dividends. We estimate volatility using our historical stock price performance over the expected life of the option up to the point where we have historical market data. For expected term, among other things, we take into consideration our historical data of options exercised, cancelled and expired. The risk-free rate is based on the U.S. Treasury constant maturity rate. We have not paid and do not expect to pay dividends in the foreseeable future. In order to calculate stock-based compensation expense, we also estimate the forfeiture rate using our historical experience with options that cancel before they vest.

Research and Development Accruals

We have various contracts with third parties related to our research and development activities. Costs that are incurred for services rendered, but not billed to us, as of the end of the period are estimated and accrued. We make estimates of the amounts incurred in each period based on the information available to us and our knowledge of the nature of the contractual activities generating such costs. Clinical trial contract expenses are accrued based on units of activity reported by third parties. Expenses related to other research and development contracts, such as research contracts, toxicology study contracts and manufacturing contracts are estimated to be incurred generally on a straight-line basis over the duration of the contracts. Raw materials and study materials purchased for us by third parties are expensed at the time of purchase. Many of our estimates are based significantly or in part on information provided for us by third parties. If such information were not reported properly, our research and development expense amounts could be misstated.

Results of Operations

Three and Nine Months Ended September 30, 2013 and 2012

Revenues

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Aggregate Change	2013	2012	Aggregate Change
	(in thousands)			(in thousands)		
Contract revenues from collaborations	$	$	$	$ 1,400	$ 2,250	$ (850)

Revenues by collaborator were:

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Aggregate Change	2013	2012	Aggregate Change
		(in thousands)			(in thousands)	
Daiichi Sankyo	$	$	$	$ 1,400	$ 750	$ 650
AstraZeneca					1,000	(1,000)
BerGenBio					500	(500)
Total	$	$	$	$ 1,400	$ 2,250	$ (850)

Contract revenue from collaborations in the nine months ended September 30, 2013 was comprised of a $1.4 million payment in the second quarter of 2013 from Daiichi for the IND filing for an oncology compound. Contract revenue from collaborations for the nine months ended September 30, 2012 was comprised of a $1.0 million upfront payment from AZ related to an asthma program in preclinical stage, a $750,000 payment from Daiichi related to an oncology compound, as well as a payment of $500,000 from BerGenBio related to an oncology program. We had no deferred revenue as of September 30, 2013. Our potential future revenues may include payments from our current collaboration partners and from new collaboration partners with which we enter into agreements in the future, if any.

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Research and Development Expense

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Aggregate Change	2013	2012	Aggregate Change
	(in thousands)			(in thousands)		
Total research and development expense	$ 17,574	$ 20,186	$ (2,612)	$ 57,282	$ 59,014	$ (1,732)
Stock-based compensation expense included in research and development expense	$ 1,035	$ 1,866	$ (831)	$ 3,060	$ 5,213	$ (2,153)

The decrease in research and development expense for the three months ended September 30, 2013, compared to the same period in 2012, was primarily due to the decrease in stock-based compensation expense as discussed under Stock-Based Compensation Expense below, as well as a decrease in bonus compensation expense. The decrease in research and development expense for the nine months ended September 30, 2013, compared to the same period in 2012, was primarily due to the decrease in stock-based compensation expense as discussed under Stock-Based Compensation Expense below, as well as a decrease in accrued bonus compensation expense, partially offset by an increase in preclinical and clinical development costs. These costs were mainly related to the costs of R348, our topical JAK/SYK inhibitor program for chronic dry eye and R118, our oral AMPK activator program for intermittent claudication, partially offset by the decrease in research and development costs related to R548, our transplant rejection program. We expect that our research and development expense will increase through the remainder of 2013 due to the continued progress of our Phase 2 clinical trial of R348 in chronic dry eye and our plan to initiate two Phase 3 clinical trials of fostamatinib in ITP.

General and Administrative Expense

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Aggregate Change	2013	2012	Aggregate Change
	(in thousands)			(in thousands)		
Total general and administrative expense	$ 4,677	$ 5,383	$ (706)	$ 14,964	$ 16,997	$ (2,033)
Stock-based compensation expense included in general and administrative expense	$ 789	$ 1,379	$ (590)	$ 2,304	$ 4,141	$ (1,837)

The decrease in general and administrative expense for the three and nine months ended September 30, 2013, compared to the same periods in 2012, was primarily due to the decrease in stock-based compensation expense as discussed under Stock-Based Compensation Expense below, as well as a decrease in bonus compensation expense.

Restructuring Charges

	Three Months Ended September 30,	Nine Months Ended