XOMA Corp
Form 10-Q
May 07, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2014

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 No. 0-14710

XOMA Corporation
(Exact name of registrant as specified in its charter)

Delaware	52-2154066
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2910 Seventh Street, Berkeley, California 94710	(510) 204-7200
(Address of principal executive offices, including zip code)	(Telephone Number)

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 of 1934). Yes ¨ No x

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

Class	Outstanding at May 5, 2014
Common Stock, $0.0075 par value	106,898,733

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PART I - FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

XOMA CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

	March 31, 2014 (unaudited)	December 31, 2013 (Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$73,706	$101,659
Short-term investments	19,996	19,990
Trade and other receivables, net	4,312	3,781
Prepaid expenses and other current assets	2,558	1,630
Total current assets	100,572	127,060
Property and equipment, net	6,028	6,456
Other assets	1,029	1,266
Total assets	$107,629	$134,782
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable	$8,851	$9,616
Accrued and other liabilities	4,895	9,934
Deferred revenue	2,158	2,218
Interest bearing obligation – current	4,085	5,835
Accrued Interest on interest bearing obligations – current	264	2,042
Total current liabilities	20,253	29,645
Deferred revenue – long-term	3,636	4,105
Interest bearing obligations – long-term	34,658	35,150
Contingent warrant liabilities	47,342	69,869
Total liabilities	105,889	138,769
Stockholders' equity (deficit):		
Common stock, $0.0075 par value, 138,666,666 shares authorized, 106,885,926 and 105,386,216 shares outstanding at March 31, 2014 and December 31, 2013, respectively	799	787
Additional paid-in capital	1,086,798	1,076,403
Accumulated comprehensive income (loss)	6	(1)
Accumulated deficit	(1,085,863)	(1,081,176)
Total stockholders' equity (deficit)	1,740	(3,987)
Total liabilities and stockholders' equity (deficit)	$107,629	$134,782

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

(Note 1) The condensed consolidated balance sheet as of December 31, 2013 has been derived from the audited consolidated financial statements as of that date included in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

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XOMA CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(unaudited)

(in thousands, except per share amounts)

	Three months ended March 31,	
	2014	2013
Revenues:		
License and collaborative fees	$964	$399
Contract and other	2,446	9,054
Total revenues	3,410	9,453
Operating expenses:		
Research and development	21,546	16,636
Selling, general and administrative	5,254	4,124
Restructuring	84	17
Total operating expenses	26,884	20,777
Loss from operations	(23,474)	(11,324)
Other income (expense):		
Interest expense	(1,125)	(1,172)
Other (expense) income	(90)	449
Revaluation of contingent warrant liabilities	20,002	(12,840)
Net loss	$(4,687)	$(24,887)
Basic and diluted net loss per share of common stock	$(0.04)	$(0.30)
Shares used in computing basic and diluted net loss per share of common stock	106,158	82,595
Other comprehensive loss:		
Net loss	$(4,687)	$(24,887)
Net unrealized gains on available-for-sale securities	7	3
Comprehensive loss	$(4,680)	$(24,884)

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

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XOMA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

	Three Months Ended March 31, 2014	Three Months Ended March 31, 2013
Cash flows from operating activities:		
Net loss	$(4,687)	$(24,887)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	477	780
Common stock contribution to 401(k)	870	828
Stock-based compensation expense	3,924	1,619
Accrued interest on interest bearing obligations	(1,764)	1,586
Revaluation of contingent warrant liabilities	(20,002)	12,840
Amortization of debt discount, final payment fee on debt, and debt issuance costs	674	603
Unrealized gain on foreign currency exchange	(66)	(515)
Unrealized loss on foreign exchange options	122	189
Other non-cash adjustments	1	(4)
Changes in assets and liabilities:		
Trade and other receivables, net	(530)	1,997
Prepaid expenses and other assets	(923)	(802)
Accounts payable and accrued liabilities	(5,721)	(7,097)
Deferred revenue	(524)	(111)
Other liabilities	(51)	(1,554)
Net cash used in operating activities	(28,200)	(14,528)
Cash flows from investing activities:		
Proceeds from maturities of investments	-	20,000
Net purchase of property and equipment	(49)	(498)
Net cash (used in) provided by investing activities	(49)	19,502
Cash flows from financing activities:		
Proceeds from issuance of common stock, net of issuance costs	3,053	60
Proceeds from exercise of warrants	35	-
Principal payments of debt	(2,792)	-
Net cash provided by financing activities	296	60
Net (decrease) increase in cash and cash equivalents	(27,953)	5,034
Cash and cash equivalents at the beginning of the period	101,659	45,345
Cash and cash equivalents at the end of the period	$73,706	$50,379
Supplemental Cash Flow Information:		
Cash paid for:		
Interest	$2,194	$333
Non-cash investing and financing activities:		
Reclassification of contingent warrant liability to equity upon exercise of warrants	$(2,525)	$-
Interest added to principal balances on long-term debt	$-	$313

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

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XOMA CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Description of Business

XOMA Corporation ("XOMA" or the "Company"), a Delaware corporation combines a portfolio of late-stage clinical programs and research activities to develop innovative therapeutic antibodies that it intends to commercialize. XOMA focuses its scientific research on allosteric modulation, which offers opportunities for new classes of therapeutic antibodies to treat a wide range of human diseases. XOMA is developing its lead product candidate gevokizumab (IL-1 beta modulating antibody) with Servier through a global Phase 3 clinical development program and ongoing proof-of-concept studies in other IL-1-mediated diseases. XOMA's scientific research also has produced the XMet platform, which consists of three classes of preclinical antibodies, including selective insulin receptor modulators that could offer new approaches in the treatment of diabetes. The Company's products are presently in various stages of development and are subject to regulatory approval before they can be commercially launched.

2. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

The condensed consolidated financial statements include the accounts of XOMA and its subsidiaries. All intercompany accounts and transactions among consolidated entities were eliminated during consolidation. The unaudited financial statements were prepared 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. As permitted under those rules certain footnotes or other financial information can be condensed or omitted. These financial statements and related disclosures have been prepared with the assumption that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year. Accordingly, these statements should be read in conjunction with the audited consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013, filed with the U.S. Securities and Exchange Commission ("SEC") on March 12, 2014.

In management's opinion, the accompanying unaudited condensed consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, which are necessary to present fairly the Company's consolidated financial position as of March 31, 2014, the consolidated results of the Company's operations and the Company's cash flows for the three months ended March 31, 2014 and 2013. The interim results of operations are not necessarily indicative of the results that may be expected for the full fiscal year or any other periods.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures. On an on-going basis, management evaluates its estimates including, but not limited to, those related to contingent warrant liabilities, revenue recognition, research and development expense, long-lived assets, derivative instruments and stock-based compensation. The Company bases its estimates on historical experience and on various other market-specific and other relevant assumptions that are believed 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 significantly from these estimates, such as the Company's billing under government contracts. Under the Company's contracts with the National Institute of Allergy and Infectious Diseases ("NIAID"), a part of the National Institutes of Health ("NIH"), the Company bills using NIH provisional rates and thus are subject to future audits at the discretion of NIAID's contracting office. These audits can result in an adjustment to revenue previously reported.

Reclassifications

Certain reclassifications of prior period amounts have been made to the financial statements and accompanying notes to conform to the current period presentation. Prior period presentations of net product sales has been reclassified into contract and other revenue, and cost of sales has been reclassified into research and development expense, because the net product sales were not material for all periods presented. These reclassifications had no impact on the Company’s previously reported net loss or cash flows.

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Concentration of Risk

Cash equivalents and receivables are financial instruments, which potentially subject the Company to concentrations of credit risk, as well as liquidity risk for certain cash equivalents such as money market funds. The Company has not encountered such issues during 2014.

The Company has not experienced any significant credit losses and does not generally require collateral on receivables. For the three months ended March 31, 2014, three customers represented 47%, 40%, and 15% of total revenue and 57%, 28%, and 12% of the accounts receivable balance.

For the three months ended March 31, 2013, two customers represented 79% and 18% of total revenues. As of December 31, 2013, there were receivables outstanding from these two customers representing 73% and 13% of the accounts receivable balance.

3. Condensed Consolidated Financial Statement Detail

Net Loss Per Share of Common Stock

Basic net loss per share of common stock is based on the weighted average number of shares of common stock outstanding during the period. Diluted net loss per share of common stock is based on the weighted average number of shares outstanding during the period, adjusted to include the assumed conversion of certain stock options, restricted stock units ("RSUs"), and warrants for common stock.

Potentially dilutive securities are excluded from the calculation of loss per share if their inclusion is anti-dilutive. The following table shows the total outstanding securities considered anti-dilutive and therefore excluded from the computation of diluted net loss per share (in thousands):

	Three Months Ended March 31,	
	2014	2013
Common stock options and restricted stock units	5,732	6,459
Warrants for common stock	14,273	16,176
Total	20,005	22,635

For the three months ended March 31, 2014 and 2013, all potentially dilutive securities outstanding were considered anti-dilutive, and therefore the calculation of basic and diluted net loss per share was the same.

Cash and Cash Equivalents

At March 31, 2014, cash and cash equivalents consisted of demand deposits of $10.1 million and money market funds of $63.6 million with maturities of less than 90 days at the date of purchase. At December 31, 2013, cash and cash equivalents consisted of demand deposits of $18.9 million and money market funds of $82.8 million with maturities of less than 90 days at the date of purchase.

Short-term Investments

At both March 31, 2014 and December 31, 2013, short-term investments consisted of U.S. treasury securities of $20.0 million with maturities of greater than 90 days and less than one year from the date of purchase.

Foreign Exchange Options

The Company holds debt and may incur revenue and expenses denominated in foreign currencies, which exposes it to market risk associated with foreign currency exchange rate fluctuations between the U.S. dollar and the Euro. The Company is required in the future to make principal and accrued interest payments in Euros on its €15.0 million loan from Servier (See Note 5: Long-Term Debt and Other Arrangements). In order to manage its foreign currency exposure related to these payments, in May 2011, the Company entered into two foreign exchange option contracts to buy €1.5 million and €15.0 million in January 2014 and January 2016, respectively. By having these option contracts in place, the Company's foreign exchange rate risk is reduced if the U.S. dollar weakens against the Euro. However, if the U.S. dollar strengthens against the Euro, the Company is not required to exercise these options, but will not receive any refund on premiums paid.

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Upfront premiums paid on these foreign exchange option contracts totaled $1.5 million. The fair values of these option contracts are revalued at each reporting period and are estimated based on pricing models using readily observable inputs from actively quoted markets. The fair values of these option contracts are included in other assets on the condensed consolidated balance sheet and changes in fair value on these contracts are included in other income (expense) on the condensed consolidated statements of comprehensive loss.

The January 2014 foreign exchange option expired in January 2014 without being exercised. The January 2016 foreign exchange option was revalued at March 31, 2014 and had a fair value of $0.2 million. The Company recognized losses of $0.1 million and $0.2 million related to the revaluation for the three months ended March 31, 2014 and 2013, respectively.

Accrued Liabilities

Accrued liabilities consisted of the following at March 31, 2014 and December 31, 2013 (in thousands):

	March 31, 2014	December 31, 2013
Accrued payroll and other benefits	$2,401	$ 3,009
Accrued management incentive compensation	1,050	4,386
Other	1,444	2,539
Total	$4,895	$ 9,934

Contingent Warrant Liabilities

In March 2012, in connection with an underwritten offering, the Company issued five-year warrants to purchase 14,834,577 shares of XOMA's common stock at an exercise price of $1.76 per share. These warrants contain provisions that are contingent on the occurrence of a change in control, which would conditionally obligate the Company to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Option Pricing Model (the "Black-Scholes Model") on the date of such change in control. Due to these provisions, the Company is required to account for the warrants issued in March 2012 as a liability at fair value. In addition, the estimated liability related to the warrants is required to be revalued at each reporting period until the earlier of the exercise of the warrants, at which time the liability will be reclassified to stockholders' equity, or expiration of the warrants. At December 31, 2013, the fair value of the warrant liability was estimated to be $68.7 million using the Black-Scholes Model. The Company revalued the warrant liability at March 31, 2014 using the Black-Scholes Model and recorded the $19.5 million decrease in the fair value as a gain in the revaluation of contingent warrant liabilities line of its condensed consolidated statements of comprehensive loss. The Company also reclassified $2.5 million from contingent warrant liabilities to equity on its condensed consolidated balance sheets due to the exercise of warrants. As of March 31, 2014, 12,109,418 of these warrants were outstanding and had a fair value of $46.6 million. This decrease in liability is due primarily to the decrease in the market price of XOMA's common stock at March 31, 2014 compared to December 31, 2013.

In February 2010, in connection with an underwritten offering, the Company issued five-year warrants to purchase 1,260,000 shares of XOMA's common stock at an exercise price of $10.50 per share. In June 2009, the Company issued warrants to certain institutional investors as part of a registered direct offering. These warrants represent the right to acquire an aggregate of up to 347,826 shares of XOMA's common stock over a five year period beginning December 11, 2009 at an exercise price of $19.50 per share. These warrants contain provisions that are contingent on the occurrence of a change in control, which would conditionally obligate the Company to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Model on the date of such change in control. Due to these provisions, the Company is required to account for the warrants issued in February 2010 and June 2009 as liabilities at fair value. At December 31, 2013, the fair value of the warrant liability was estimated to be $1.2 million using the Black-Scholes Model. The Company revalued the warrant liability at March 31, 2014 using the Black-Scholes Model and recorded the $0.5 million decrease in the fair value as a gain in the revaluation of contingent warrant liabilities line of our condensed consolidated statements of comprehensive loss. As of March 31, 2014, all of these warrants were outstanding and had an aggregate fair value of approximately $0.7 million.

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4. Fair Value Measurements

Fair value is defined as the price that would be received from selling an asset or the amount that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company applies accounting standards, which establish a framework for measuring fair value and a fair value hierarchy that prioritizes the inputs used in valuation techniques. Accounting standards describe a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

Level 1 – Quoted prices in active markets for identical assets or liabilities.

Level 2 – Observable inputs other than quoted prices in active markets for similar assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of assets and liabilities, therefore requiring in entity to develop its own assumptions.

The following tables set forth the Company's fair value hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2014 and December 31, 2013.

Financial assets and liabilities carried at fair value as of March 31, 2014 and December 31, 2013 were classified as follows (in thousands):

	Fair Value Measurements at March 31, 2014 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Money market funds [1]	$63,561	$ -	$ -	$63,561
U.S. treasury securities	19,996	-	-	19,996
Foreign exchange options	-	239	-	239
Total	$83,557	$ 239	$ -	$83,796
Liabilities:				
Contingent warrant liabilities	$-	$ -	$ 47,342	$47,342

Fair Value Measurements at December 31, 2013 Using		
Quoted Prices in Active Markets for	Significant Other Observable Inputs	Significant Unobservable Inputs

	Identical Assets (Level 1)	(Level 2)	(Level 3)	Total
Assets:				
Money market funds (1)	$82,759	$ -	$ -	$82,759
U.S. treasury securities	19,990	-	-	19,990
Foreign exchange options	-	361	-	361
Total	$102,749	$ 361	$ -	$103,110