

HALOZYME THERAPEUTICS INC  
Form 10-Q  
November 08, 2013

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q  
(Mark One)

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

For the quarterly period ended September 30, 2013  
OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 001-32335

HALOZYME THERAPEUTICS, INC.  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

88-0488686  
(I.R.S. Employer Identification No.)

11388 Sorrento Valley Road, San Diego, CA  
(Address of principal executive offices)  
(858) 794-8889  
(Registrant's telephone number, including area code)

92121  
(Zip 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  No

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

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

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

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

The number of outstanding shares of the registrant's common stock, par value \$0.001 per share, was 114,028,596 as of November 4, 2013.



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## PART I — FINANCIAL INFORMATION

## Item 1. Financial Statements

## HALOZYME THERAPEUTICS, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2013 (Unaudited)	December 31, 2012
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$17,492,131	\$99,501,264
Marketable securities, available-for-sale	47,818,851	—
Accounts receivable, net	24,521,742	15,703,087
Inventories	3,846,290	2,670,696
Prepaid expenses and other assets	9,139,014	12,752,888
Total current assets	102,818,028	130,627,935
Property and equipment, net	4,935,928	3,700,462
Prepaid expenses and other assets	1,891,170	—
Restricted cash	500,000	400,000
Total Assets	\$110,145,126	\$134,728,397
<b>LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY</b>		
Current liabilities:		
Accounts payable	\$5,591,763	\$2,271,689
Accrued expenses	20,624,501	7,783,447
Deferred revenue, current portion	7,437,433	8,891,017
Current portion of long-term debt, net	5,970,119	—
Total current liabilities	39,623,816	18,946,153
Deferred revenue, net of current portion	45,940,511	34,954,966
Long-term debt, net	23,781,955	29,661,680
Lease financing obligation	2,550,000	1,450,000
Deferred rent, net of current portion	813,689	861,879
Other long-term liability	921,460	—
Commitments and contingencies (Note 8)		
Stockholders' (deficit) equity:		
Preferred stock - \$0.001 par value; 20,000,000 shares authorized; no shares issued and outstanding	—	—
Common stock - \$0.001 par value; 200,000,000 shares authorized; 113,986,739 shares issued and outstanding at September 30, 2013 and 150,000,000 shares authorized; 112,709,174 shares issued and outstanding at December 31, 2012	113,987	112,709
Additional paid-in capital	356,449,825	347,314,658
Accumulated other comprehensive income	15,779	—
Accumulated deficit	(360,065,896 )	(298,573,648 )
Total stockholders' (deficit) equity	(3,486,305 )	48,853,719
Total Liabilities and Stockholders' (Deficit) Equity	\$110,145,126	\$134,728,397
See accompanying notes to condensed consolidated financial statements.		

HALOZYME THERAPEUTICS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Revenues:				
Product sales, net	\$ 10,024,902	\$ 715,354	\$ 14,633,349	\$ 1,427,707
Revenues under collaborative agreements	5,988,262	4,618,969	27,667,165	19,103,970
Total revenues	16,013,164	5,334,323	42,300,514	20,531,677
Operating expenses:				
Cost of product sales	682,713	226,635	2,705,633	440,516
Research and development	25,689,189	19,503,491	75,714,381	51,476,329
Selling, general and administrative	8,135,118	5,634,034	22,990,777	17,833,165
Total operating expenses	34,507,020	25,364,160	101,410,791	69,750,010
Operating loss	(18,493,856 )	(20,029,837 )	(59,110,277 )	(49,218,333 )
Other income (expense):				
Investment and other income	51,424	23,991	164,544	72,187
Interest expense	(849,936 )	—	(2,546,515 )	—
Net loss	\$(19,292,368 )	\$(20,005,846 )	\$(61,492,248 )	\$(49,146,146 )
Basic and diluted net loss per share	\$(0.17 )	\$(0.18 )	\$(0.55 )	\$(0.44 )
Shares used in computing basic and diluted net loss per share	112,765,155	112,305,002	112,554,447	110,658,757

See accompanying notes to condensed consolidated financial statements.

HALOZYME THERAPEUTICS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS  
 (UNAUDITED)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Net loss	\$(19,292,368)	\$(20,005,846)	\$(61,492,248)	\$(49,146,146)
Other comprehensive income (loss):				
Unrealized gain on marketable securities	55,088	—	15,779	—
Comprehensive loss	\$(19,237,280)	\$(20,005,846)	\$(61,476,469)	\$(49,146,146)

See accompanying notes to condensed consolidated financial statements.

HALOZYME THERAPEUTICS, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (UNAUDITED)

	Nine Months Ended September 30,	
	2013	2012
Operating activities:		
Net loss	\$(61,492,248 )	\$(49,146,146 )
Adjustments to reconcile net loss to net cash used in operating activities:		
Share-based compensation	7,139,998	6,362,372
Depreciation and amortization	893,477	796,163
Non-cash interest expense	1,036,502	—
Amortization of premiums on investments, net of accretion of discounts	816,196	—
Gain on disposals of equipment	—	(6,610 )
Changes in operating assets and liabilities:		
Accounts receivable, net	(8,818,655 )	(2,201,808 )
Inventories	(1,175,594 )	(1,618,800 )
Prepaid expenses and other assets	2,017,859	(3,021,100 )
Restricted cash	(100,000 )	—
Accounts payable and accrued expenses	16,070,721	(2,106,754 )
Deferred rent	(39,742 )	62,385
Deferred revenue	9,531,961	3,469,392
Net cash used in operating activities	(34,119,525 )	(47,410,906 )
Investing activities:		
Purchases of marketable securities	(48,946,616 )	—
Purchases of property and equipment	(939,439 )	(873,165 )
Net cash used in investing activities	(49,886,055 )	(873,165 )
Financing activities:		
Proceeds from issuance of common stock, net	—	81,476,845
Proceeds from issuance of common stock under equity incentive plans, net	1,996,447	1,596,590
Net cash provided by financing activities	1,996,447	83,073,435
Net (decrease) increase in cash and cash equivalents	(82,009,133 )	34,789,364
Cash and cash equivalents at beginning of period	99,501,264	52,825,527
Cash and cash equivalents at end of period	\$17,492,131	\$87,614,891
Supplemental disclosure of cash flow information:		
Interest and fees paid	\$1,529,438	\$—
Supplemental disclosure of non-cash investing and financing activities:		
Capitalized property and liability associated with a build-to-suit lease arrangement	\$1,100,000	\$—
Property and equipment purchases in accounts payable and accrued expenses	\$89,504	\$508,990
See accompanying notes to condensed consolidated financial statements.		

HALOZYME THERAPEUTICS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. Organization and Business

Halozyme Therapeutics, Inc. is a science-driven, biopharmaceutical company committed to making molecules into medicines for patients in need. Our research focuses primarily on human enzymes that alter the extracellular matrix. The extracellular matrix is a complex matrix of proteins and carbohydrates surrounding the cell that provides structural support in tissues and orchestrates many important biological activities, including cell migration, signaling and survival. Over many years, we have developed unique technology and scientific expertise enabling us to pursue this target-rich environment for the development of therapies.

Our proprietary enzymes can be used to facilitate the delivery of injected drugs and fluids, thus enhancing the efficacy and the convenience of other drugs or to alter abnormal tissue structures for clinical benefit. We have chosen to exploit our technology and expertise in a balanced way to modulate both risk and spend by: (1) developing our own proprietary products in therapeutic areas with significant unmet medical needs, such as diabetes, oncology and dermatology, and (2) licensing our technology to biopharmaceutical companies to collaboratively develop products which combine our technology with the collaborators' proprietary compounds.

The majority of the product candidates in our current pipeline are based on rHuPH20, a patented human recombinant hyaluronidase enzyme. rHuPH20 temporarily breaks down hyaluronic acid - a naturally occurring substance that is a major component of the extracellular matrix in tissues throughout the body such as skin and cartilage. We have one proprietary commercial product, Hylenex<sup>®</sup> recombinant. Our proprietary pipeline consists of multiple clinical stage products in diabetes, oncology and dermatology. We currently have collaborations with F. Hoffmann-La Roche, Ltd. and Hoffmann-La Roche, Inc. ("Roche"), Pfizer Inc. ("Pfizer"), Baxter Healthcare Corporation ("Baxter"), ViroPharma Incorporated ("ViroPharma"), and Intrexon Corporation ("Intrexon"), with two approved products in Europe, one product candidate which has been submitted for regulatory approval in the U.S. and one product candidate which has been submitted for regulatory approval in Europe as well as several others at various stages of development.

We were founded in 1998 and reincorporated from the State of Nevada to the State of Delaware in November 2007.

Except where specifically noted or the context otherwise requires, references to "Halozyme," "the Company," "we," "our," and "us" in these Notes to Condensed Consolidated Financial Statements refer to Halozyme Therapeutics, Inc. and our wholly-owned subsidiary, Halozyme, Inc.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying interim unaudited condensed consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles ("U.S. GAAP") and with the rules and regulations of the U.S. Securities and Exchange Commission ("SEC") related to a quarterly report on Form 10-Q. Accordingly, they do not include all of the information and disclosures required by U.S. GAAP for a complete set of financial statements. These interim unaudited condensed consolidated financial statements and notes thereto should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2012, filed with the SEC on March 1, 2013. The unaudited financial information for the interim periods presented herein reflects all adjustments which, in the opinion of management, are necessary for a fair presentation of the financial condition and results of operations for the periods presented, with such adjustments consisting only of normal recurring adjustments. Operating results for interim periods are not necessarily indicative of the operating results for an entire fiscal year.

The condensed consolidated financial statements include the accounts of Halozyme Therapeutics, Inc. and our wholly owned subsidiary, Halozyme, Inc. All intercompany accounts and transactions have been eliminated.



The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in our consolidated financial statements and accompanying notes. On an ongoing basis, we evaluate our estimates and judgments, which are based on historical and anticipated results and trends and on various other assumptions that management believes to be reasonable under the circumstances. By their nature, estimates are subject to an inherent degree of uncertainty and, as such, actual results may differ from management's estimates.

#### Adoption of Recent Accounting Pronouncement

Effective January 1, 2013, we adopted Financial Accounting Standards Board's ("FASB") Accounting Standards Update ("ASU") No. 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. The provisions of ASU No. 2013-02 require companies to present reclassifications out of accumulated other comprehensive income and other amounts of other comprehensive income separately by each component of other comprehensive income on the face of the financial statements or in the notes. This update is effective prospectively for reporting periods beginning after December 15, 2012. The adoption of ASU No. 2013-02 did not have a material impact on our consolidated financial position or results of operations as the requirements are disclosure only in nature. ASU No. 2013-02 did not impact our disclosures as there were no reclassifications in any periods reported.

#### Pending Adoption of Recent Accounting Pronouncement

In July 2013, FASB issued ASU No. 2013-11, Income Taxes (Topic 740), Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The provisions of ASU No. 2013-11 require entities to present unrecognized tax benefits as a decrease in a net operating loss, similar tax loss or tax credit carryforward if certain criteria are met. The determination of whether a deferred tax asset is available is based on the unrecognized tax benefit and the deferred tax asset that exists at the reporting date and presumes disallowance of the tax position at the reporting date. The guidance will eliminate the diversity in practice in the presentation of unrecognized tax benefits but will not alter the way in which entities assess deferred tax assets for realizability. The amendments are effective for public companies for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. The amendments should be applied prospectively to unrecognized tax benefits that exist at the effective date. Early adoption is permitted. The adoption of ASU No. 2013-11 will not have a material impact on our consolidated financial position or results of operations.

#### Cash Equivalents and Marketable Securities

Cash equivalents consist of highly liquid investments, readily convertible to cash, that mature within ninety days or less from date of purchase. Our cash equivalents consist of money market funds.

Marketable securities are investments with original maturities of more than ninety days from the date of purchase that are specifically identified to fund current operations. Marketable securities are considered available-for-sale. These investments are classified as current assets, even though the stated maturity date may be one year or more beyond the current balance sheet date which reflects management's intention to use the proceeds from the sale of these investments to fund our operations, as necessary. Such available-for-sale investments are carried at fair value with unrealized gains and losses recorded in other comprehensive loss and included as a separate component of stockholders' (deficit) equity. The cost of marketable securities is adjusted for amortization of premiums or accretion of discounts to maturity, and such amortization or accretion is included in investment income. We use the specific method for calculating realized gains and losses on marketable securities sold. Realized gains and losses and declines in value judged to be other than temporary on marketable securities, if any, are included in investment income in the consolidated statement of operations. There were no realized gains or losses during the reporting periods.

### Restricted Cash

Under the terms of the leases of our facilities, we are required to maintain letters of credit as security deposits during the term of such leases. At September 30, 2013 and December 31, 2012, restricted cash of \$500,000 and \$400,000, respectively, was pledged as collateral for the letters of credit. To conform to the current period presentation, we have reclassified \$400,000 from cash and cash equivalents to restricted cash in the consolidated balance sheet at December 31, 2012.

### Fair Value of Financial Instruments

The authoritative guidance for fair value measurements establishes a three tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

Our financial instruments include cash equivalents, marketable securities, accounts receivable, prepaid expenses, accounts payable, accrued expenses and long-term debt. Fair value estimates of these instruments are made at a specific point in time, based on relevant market information. These estimates may be subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. The carrying amount of cash equivalents, accounts receivable, prepaid expenses, accounts payable and accrued expenses are generally considered to be representative of their respective fair values because of the short-term nature of those instruments. Further, based on the borrowing rates currently available to us for loans with similar terms, we believe the fair value of long-term debt approximates its carrying value.

Available-for-sale marketable securities consist of corporate debt securities, commercial paper and certificates of deposit and were measured at fair value using Level 2 inputs. Level 2 financial instruments are valued using market prices on less active markets and proprietary pricing valuation models with observable inputs, including interest rates, yield curves, maturity dates, issue dates, settlement dates, reported trades, broker-dealer quotes, issue spreads, benchmark securities or other market related data. We obtain the fair value of Level 2 investments from our investment manager, who obtains these fair values from a third-party pricing service. We validate the fair values of Level 2 financial instruments provided by our investment manager by comparing these fair values to a third-party pricing source.

The following table summarizes, by major security type, our cash equivalents and marketable securities that are measured at fair value on a recurring basis and are categorized using the fair value hierarchy:

	September 30, 2013		Total estimated fair value	December 31, 2012		Total estimated fair value
	Level 1	Level 2		Level 1	Level 2	
Cash equivalents:						
Money market funds	\$11,853,450	\$—	\$11,853,450	\$98,024,269	\$—	\$98,024,269
Available-for-sale marketable securities:						
Corporate debt securities	—	38,826,192	38,826,192	—	—	—
Commercial paper	—	5,992,659	5,992,659	—	—	—
Certificate of deposit	—	3,000,000	3,000,000	—	—	—
	\$11,853,450	\$47,818,851	\$59,672,301	\$98,024,269	\$—	\$98,024,269

There were no transfers between Level 1 and Level 2 of the fair value hierarchy in the nine months ended September 30, 2013 and 2012. We have no instruments that are classified within Level 3 as of September 30, 2013 and December 31, 2012.

#### Inventories

Inventories are stated at lower of cost or market. Cost is determined on a first-in, first-out basis. Inventories are reviewed periodically for potential excess, dated or obsolete status. Management evaluates the carrying value of inventories on a regular basis, taking into account such factors as historical and anticipated future sales compared to quantities on hand, the price we expect to obtain for products in their respective markets compared with historical cost and the remaining shelf life of goods on hand.

We expense costs relating to the purchase and production of pre-approval inventories for which the sole use is pre-approval products as research and development expense in the period incurred until such time as we believe future commercialization is probable and future economic benefit is expected to be realized. Inventories used in clinical trials are expensed at the time the inventories are packaged for the clinical trials. Prior to receiving approval from the U.S. Food and Drug Administration ("FDA") or comparable regulatory agencies in foreign countries, costs related to purchases of bulk rHuPH20 enzyme ("active pharmaceutical ingredient" or "API") and raw materials and the manufacturing of the product candidates are recorded as research and development expense. All direct manufacturing costs incurred after approval are capitalized as inventory.

As of September 30, 2013 and December 31, 2012, inventories consisted of \$2.5 million and \$2.7 million of Hylenex recombinant inventory, respectively, and \$1.3 million and zero of API used in the manufacture of Herceptin SC, respectively. Roche received European marketing approval for its collaboration product, Herceptin<sup>®</sup> SC, in August 2013 and Baxter for its collaboration product, HyQvia, in May 2013. As such, direct manufacturing costs of API for Herceptin SC and HyQvia incurred after the receipt of the European marketing approvals are being capitalized as inventory.

#### Revenue Recognition

We generate revenues from product sales and collaborative agreements. Payments received under collaborative agreements may include nonrefundable fees at the inception of the agreements, license fees, milestone payments for specific achievements designated in the collaborative agreements, reimbursements of research and development services and supply of rHuPH20 API, and/or royalties on sales of products resulting from collaborative arrangements. We recognize revenues in accordance with the authoritative guidance for revenue recognition. We recognize revenue when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the seller's price to the buyer is fixed or determinable; and (4) collectibility is reasonably assured.

#### Product Sales, Net

##### Hylenex Recombinant

In December 2011, we reintroduced Hylenex recombinant to the market and began promoting Hylenex recombinant through our sales force. We sell Hylenex recombinant in the United States to wholesale pharmaceutical distributors, who sell the product to hospitals and other end-user customers. The wholesale distributors take title to the product, bear the risk of loss of ownership and have economic substance to the inventory. Further, we have no significant obligations for future performance to generate pull-through sales; however, we allow the wholesale distributors to return product that is damaged or received in error. In addition, we allow for product to be returned beginning six months prior to and ending twelve months following product expiration.

Given our limited history of selling Hylenex recombinant and the lengthy return period, we currently cannot reliably estimate expected returns and chargebacks of Hylenex recombinant at the time the product is received by the wholesale distributors. Therefore, we do not recognize revenue upon delivery of Hylenex recombinant to the wholesale distributor until the point at which

we can reliably estimate expected product returns and chargebacks from the wholesale distributors. Shipments of Hylenex recombinant are recorded as deferred revenue until evidence exists to confirm that pull-through sales to the hospitals or other end-user customers have occurred. We recognize revenue when the product is sold through from the distributors to the distributors' customers. In addition, the costs of manufacturing Hylenex recombinant associated with the deferred revenue are recorded as deferred costs, which are included in inventory, until such time as the related deferred revenue is recognized. We estimate sell-through revenue and certain sales allowances based on analysis of third-party information including information obtained from certain distributors with respect to their inventory levels and sell-through to the distributors' customers. At the time we can reliably estimate product returns and chargebacks from the wholesale distributors, we will record a one-time increase in net product sales revenue related to the recognition of product sales revenue previously deferred.

We recognize product sales allowances as a reduction of product sales in the same period the related revenue is recognized. Product sales allowances are based on amounts owed or to be claimed on the related sales. These estimates take into consideration the terms of our agreements with wholesale distributors and hospitals. We must make significant judgments in determining these allowances. If actual results differ from our estimates, we will be required to make adjustments to these allowances in the future, which could have an effect on product sales revenue in the period of adjustment.

Our product sales allowances include:

**Distribution Fees.** The distribution fees, based on contractually determined rates, arise from contractual agreements we have with certain wholesale distributors for distribution services they provide with respect to Hylenex recombinant. At the time the sale is made to the respective wholesale distributors, we record an allowance for distribution fees by reducing our accounts receivable and deferred revenue associated with such product sales.

**Prompt Payment Discounts.** We offer cash discounts to certain wholesale distributors as an incentive to meet certain payment terms. We expect our customers will take advantage of this discount; therefore, at the time the sale is made to the respective wholesale distributors, we accrue the entire prompt payment discount, based on the gross amount of each invoice, by reducing our accounts receivable and deferred revenue associated with such product sales.

**Other Discounts and Fees.** We provide discounts to end-user members of certain group purchasing organizations ("GPO") under collective purchasing contracts between us and the GPOs. We also provide discounts to certain hospitals, who are members of the GPOs, with which we do not have contracts. The end-user members purchase products from the wholesale distributors at a contracted discounted price, and the wholesale distributors then charge back to us the difference between the current retail price and the price the end-users paid for the product. Given our lack of historical sales data, we recognize these chargebacks in the same period the related product sales revenue is recognized and reduce our accounts receivable accordingly. We incur GPO fees for these transactions which are also recorded in the same period the related product sales revenue is recognized and are included in accrued expenses.

**Product Returns.** The product returns reserve is based on management's best estimate of the product sales recognized as revenue during the period that are anticipated to be returned. The product returns reserve is recorded as a reduction of product sales revenue in the same period the related product sales revenue is recognized and is included in accrued expenses.

#### rHuPH20 API

Subsequent to receiving approval from the FDA or comparable regulatory agencies in foreign countries, sales of API for collaboration commercial products are recognized as product sales when the API has met all the specifications required for the customer's acceptance and title and risk of loss have transferred to the customer. Following the receipts of European marketing approvals of Roche's Herceptin SC product in August 2013 and Baxter's HyQvia product in May 2013, revenue from the sales of API for these collaboration products will be recognized as product sales. For the three and nine months ended September 30, 2013, we recognized product sales of API in the amounts of \$7.9 million for Herceptin SC and zero and \$1.1 million, respectively, for HyQvia.

### Revenues under Collaborative Agreements

We have license and collaboration agreements under which the collaborators obtained worldwide rights for the use of our proprietary rHuPH20 enzyme in the development and commercialization of the collaborators' biologic compounds. The collaborative agreements contain multiple elements including nonrefundable payments at the inception of the arrangement, license fees, exclusivity fees, payments based on achievement of specified milestones designated in the collaborative agreements, annual maintenance fees, reimbursements of research and development services, payments for supply of rHuPH20 API for the collaborator and/or royalties on sales of products resulting from collaborative agreements. We analyze each element of our collaborative agreements and consider a variety of factors in determining the appropriate method of revenue recognition of each element.

In order to account for the multiple-element arrangements, we identify the deliverables included within the agreement and evaluate which deliverables represent units of accounting. Analyzing the arrangement to identify deliverables requires the use of judgment, and each deliverable may be an obligation to deliver services, a right or license to use an asset, or another performance obligation. The deliverables under our collaborative agreements include (i) the license to our rHuPH20 technology, (ii) at the collaborator's request, research and development services which are reimbursed at contractually determined rates, and (iii) at the collaborator's request, supply of rHuPH20 API which is reimbursed at our cost plus a margin. A delivered item is considered a separate unit of accounting when the delivered item has value to the collaborator on a standalone basis based on the consideration of the relevant facts and circumstances for each arrangement. Factors considered in this determination include the research capabilities of the collaborator and the availability of research expertise in this field in the general marketplace.

Arrangement consideration is allocated at the inception of the agreement to all identified units of accounting based on their relative selling price. The relative selling price for each deliverable is determined using vendor specific objective evidence ("VSOE") of selling price or third-party evidence of selling price if VSOE does not exist. If neither VSOE nor third-party evidence of selling price exists, we use our best estimate of the selling price for the deliverable. The amount of allocable arrangement consideration is limited to amounts that are not contingent upon the delivery of additional items or meeting other specified performance conditions. The consideration received is allocated among the separate units of accounting, and the applicable revenue recognition criteria are applied to each of the separate units. Changes in the allocation of the sales price between delivered and undelivered elements can impact revenue recognition but do not change the total revenue recognized under any agreement.

Nonrefundable upfront license fee payments are recognized upon delivery of the license if facts and circumstances dictate that the license has standalone value from the undelivered items, which generally include research and development services and the manufacture of rHuPH20 API, the relative selling price allocation of the license is equal to or exceeds the upfront license fee, persuasive evidence of an arrangement exists, our price to the collaborator is fixed or determinable and collectibility is reasonably assured. Upfront license fee payments are deferred if facts and circumstances dictate that the license does not have standalone value. The determination of the length of the period over which to defer revenue is subject to judgment and estimation and can have an impact on the amount of revenue recognized in a given period.

Prior to the adoption of ASU No. 2009-13, Multiple-Deliverable Revenue Arrangements, on January 1, 2011, in order for a delivered item to be accounted for separately from other deliverables in a multiple-element arrangement, the following three criteria had to be met: (i) the delivered item had standalone value to the customer, (ii) there was objective and reliable evidence of fair value of the undelivered items and (iii) if the arrangement included a general right of return relative to the delivered item, delivery or performance of the undelivered items was considered probable and substantially in the control of the vendor. For the collaborative agreements entered into prior to January 1, 2011, there was no objective and reliable evidence of fair value of the undelivered items. Thus, the delivered licenses did not meet all of the required criteria to be accounted for separately from undelivered items. Therefore, we recognize revenue on nonrefundable upfront payments and license fees from these collaborative agreements over the period of significant involvement under the related agreements.

The terms of our collaborative agreements provide for milestone payments upon achievement of certain development and regulatory events and/or specified sales volumes of commercialized products by the collaborator. We account for milestone payments in accordance with the provisions of ASU No. 2010-17, Revenue Recognition - Milestone Method. We recognize consideration that is contingent upon the achievement of a milestone in its entirety as revenue in the period in which the milestone is achieved only if the milestone is substantive in its entirety. A milestone is considered substantive when it meets all of the following criteria:

The consideration is commensurate with either the entity's performance to achieve the milestone or the enhancement

1. of the value of the delivered item(s) as a result of a specific outcome resulting from the entity's performance to achieve the milestone,

2. The consideration relates solely to past performance, and

3. The consideration is reasonable relative to all of the deliverables and payment terms within the arrangement.

A milestone is defined as an event (i) that can only be achieved based in whole or in part on either the entity's performance or on the occurrence of a specific outcome resulting from the entity's performance, (ii) for which there is substantive uncertainty at the date the arrangement is entered into that the event will be achieved and (iii) that would result in additional payments being due to the vendor.

Reimbursements of research and development services are recognized as revenue during the period in which the services are performed as long as there is persuasive evidence of an arrangement, the fee is fixed or determinable and collection of the related receivable is reasonably assured. Revenue from the manufacture of rHuPH20 API is recognized when the API has met all specifications required for the collaborator's acceptance and title and risk of loss have transferred to the collaborator. We do not directly control when any collaborator will request research and development services or supply of rHuPH20 API; therefore, we cannot predict when we will recognize revenues in connection with research and development services and supply of rHuPH20 API.

Royalty revenue from sales of collaboration products by our collaborators will be recognized when received, which is generally in the quarter following the quarter in which the corresponding sales occur.

The collaborative agreements typically provide the collaborators the right to terminate such agreement in whole or on a product-by-product or target-by-target basis at any time upon 30 to 90 days prior written notice to us. There are no performance, cancellation, termination or refund provisions in any of our collaborative agreements that contain material financial consequences to us.

#### Cost of Product Sales

Cost of product sales consists primarily of raw materials, third-party manufacturing costs, fill and finish costs, freight costs, internal costs and manufacturing overhead associated with the production of Hylenex recombinant. Cost of product sales also consists of the write-down of excess, dated and obsolete inventories and the write-off of any inventories that do not meet certain product specifications. Prior to European marketing approvals of Herceptin SC and HyQvia, all costs related to the manufacturing of API for these products were charged to research and development expenses in the periods such costs were incurred. Therefore, there was minimal cost recognized for the product sales of API for these collaboration products in the three and nine months ended September 30, 2013. Of the Herceptin SC API on hand as of September 30, 2013, \$2.6 million in manufacturing costs have been previously recorded as research and development expenses.

#### Research and Development Expenses

Research and development expenses include salaries and benefits, facilities and other overhead expenses, external clinical trial expenses, research related manufacturing services, contract services and other outside expenses. Research and development expenses are charged to operations as incurred when these expenditures relate to our research and development efforts and have no alternative future uses. Costs related to purchases of API and the manufacturing of a collaboration product incurred after receiving approval from the FDA or comparable regulatory agencies in foreign countries for such product are capitalized as inventory. The manufacturing costs of API for Herceptin SC and HyQvia incurred after the receipt of the European marketing approvals are capitalized as inventory.

In accordance with certain research and development agreements, we are obligated to make certain upfront payments upon execution of the agreement. Advance payments, including nonrefundable amounts, for goods or services that will be used or rendered for future research and development activities are deferred and capitalized. Such amounts will be recognized as an expense as the related goods are delivered or the related services are performed or such time when we do not expect the goods to be delivered or services to be performed.

Milestone payments that we make in connection with in-licensed technology or product candidates are expensed as incurred when there is uncertainty in receiving future economic benefits from the licensed technology or product candidates. We consider the future economic benefits from the licensed technology or product candidates to be uncertain until such licensed technology or product candidates are approved for marketing by the regulatory bodies such as the FDA or when other significant risk factors are abated. Management has viewed future economic benefits for all of our licensed technology or product candidates to be uncertain and has expensed these amounts as incurred.

#### Clinical Trial Expenses

Payments in connection with our clinical trials are often made under contracts with multiple contract research organizations that conduct and manage clinical trials on our behalf. The financial terms of these agreements are subject to negotiation and vary from contract to contract and may result in uneven payment flows. Generally, these agreements set forth the scope of work to be performed at a fixed fee, unit price or on a time-and-material basis. Payments under these contracts depend on factors such as the successful enrollment or treatment of patients or the completion of other clinical trial milestones.

Expenses related to clinical trials are accrued based on our estimates and/or representations from service providers regarding work performed, including actual level of patient enrollment, completion of patient studies and progress of the clinical trials. Other incidental costs related to patient enrollment or treatment are accrued when reasonably certain. If the contracted amounts are modified (for instance, as a result of changes in the clinical trial protocol or scope of work to be performed), we modify our accruals accordingly on a prospective basis. Revisions in the scope of a contract are charged to expense in the period in which the facts that give rise to the revision become reasonably certain. Historically, we have had no material changes in clinical trial expense accruals that would have had a material impact on our consolidated results of operations or financial position.

## Share-Based Compensation

Total share-based compensation expense related to all of our share-based awards was allocated as follows:

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Research and development	\$1,089,249	\$913,946	\$3,351,629	\$3,279,940
Selling, general and administrative	1,214,413	1,008,447	3,788,369	3,082,432
Share-based compensation expense	\$2,303,662	\$1,922,393	\$7,139,998	\$6,362,372
Net share-based compensation expense, per basic and diluted share	\$0.02	\$0.02	\$0.06	\$0.06
Share-based compensation expense from:				
Stock options	\$1,284,364	\$1,164,973	\$4,068,793	\$3,491,220
Restricted stock awards and restricted stock units	1,019,298	757,420	3,071,205	2,871,152
	\$2,303,662	\$1,922,393	\$7,139,998	\$6,362,372

Since we have a net operating loss carryforward as of September 30, 2013, no excess tax benefits for the tax deductions related to share-based awards were recognized in the interim unaudited condensed consolidated statements of operations for the three and nine months ended September 30, 2013.

As of September 30, 2013, total unrecognized estimated compensation cost related to non-vested stock options and non-vested restricted stock awards and restricted stock units granted prior to that date was approximately \$10.4 million and \$7.8 million, respectively, which is expected to be recognized over a weighted-average period of approximately 2.7 years and 2.9 years, respectively.

## Net Loss Per Share

Basic net loss per common share is computed by dividing loss for the period by the weighted average number of common shares outstanding during the period, without consideration for common stock equivalents. Stock options, unvested restricted stock awards ("RSAs") and unvested restricted stock units ("RSUs") are considered common stock equivalents and are only included in the calculation of diluted earnings per common share when their effect is dilutive. Because of our net loss, outstanding stock options, outstanding RSUs and unvested RSAs totaling approximately 8.6 million and 7.3 million were excluded from the calculation of diluted net loss per common share for the three and nine months ended September 30, 2013 and 2012, respectively, because their effect is anti-dilutive.

## Segment Information

We operate our business in one segment, which includes all activities related to the research, development and commercialization of our proprietary enzymes that can be used to facilitate the delivery of injected drugs and fluids, thus enhancing the efficacy and the convenience of other drugs or to alter abnormal tissue structures for clinical benefit. This segment also includes revenues and expenses related to (i) research and development and API manufacturing activities conducted under our collaborative agreements with third parties and (ii) product sales of Hylenex recombinant. The chief operating decision-maker reviews the operating results on an aggregate basis and manages the operations as a single operating segment.



## 3. Marketable Securities

Available-for-sale marketable securities consist of the following:

	September 30, 2013			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Corporate debt securities	\$38,810,413	\$18,279	\$(2,500)	\$38,826,192
Commercial paper	5,992,659	—	—	5,992,659
Certificate of deposit	3,000,000	—	—	3,000,000
	\$47,803,072	\$18,279	\$(2,500)	\$47,818,851

As of September 30, 2013, \$47.8 million of available-for-sale marketable securities are scheduled to mature within the next 12 months. There were no securities sold during the nine months ended September 30, 2013. None of these investments have been in a continuous unrealized loss position for more than twelve months as of September 30, 2013.

## 4. Collaborative Agreements

## Roche Collaboration

In December 2006, we and Roche entered into a license and collaborative agreement under which Roche obtained a worldwide, exclusive license to develop and commercialize product combinations of rHuPH20 and up to thirteen Roche target compounds (the "Roche Collaboration"). As of September 30, 2013, Roche has elected a total of five exclusive targets and retains the option to develop and commercialize rHuPH20 with three additional targets, provided that Roche continues to pay annual maintenance fees to us. As of September 30, 2013, we have received \$71.75 million from Roche, including the \$20.0 million upfront license fee payment for the application of rHuPH20 to the initial three Roche exclusive targets, \$20.75 million in connection with Roche's election of two additional exclusive targets and annual license maintenance fees for the right to designate the remaining targets as exclusive targets, \$13.0 million in clinical development milestone payments and \$8.0 million in regulatory milestone payments.

In August 2013, Roche received European marketing approval for its collaboration product, Herceptin SC, for the treatment of patients with HER2-positive breast cancer and launched Herceptin SC in the European Union (EU) which triggered a \$10.0 million payment to us for the achievement of the first commercial sale pursuant to the terms of the Roche Collaboration. We determined this payment to be a sales-based payment. Due to our continuing involvement obligations, revenue from the \$10.0 million sales-based payment was deferred and is being recognized over the remaining term of the Roche Collaboration.

Roche assumes all development, manufacturing, clinical, regulatory, sales and marketing costs under the Roche Collaboration, while we are responsible for the supply of rHuPH20 API. We are entitled to receive reimbursements for providing research and development services and rHuPH20 API to Roche at its request.

Under the terms of the Roche Collaboration, Roche will pay us a royalty on each product commercialized under the agreement consisting of a mid-single digit percent of the net sales of such product. Unless terminated earlier in accordance with its terms, the Roche Collaboration continues in effect until the expiration of Roche's obligation to pay royalties. Roche has the obligation to pay royalties with respect to each product in each country, during the period equal to the longer of: (a) the duration of any valid claim of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers the product in such country or (b) ten years following the date of the first commercial sale of such product in such country. Pursuant to the terms of the Roche Collaboration, we scaled up the production of rHuPH20 API and identified a second source manufacturer that would help meet anticipated production obligations arising from the Roche Collaboration.

Due to our continuing involvement obligations (for example, support activities associated with rHuPH20), revenues from the upfront payment, exclusive designation fees, annual license maintenance fees and sales-based payment ("Roche Deferred Revenues") were deferred and are being recognized over the term of the Roche Collaboration. In addition, we received prepayments associated with the manufacture of rHuPH20 API as requested by Roche. The manufacturing prepayments have been deferred and are being recognized as revenue as API is delivered to Roche. For the three months ended September 30, 2013 and 2012, we recognized amortization of the Roche Deferred Revenues as revenues under collaborative agreements totaling approximately \$575,000 and \$503,000, respectively. For the nine months ended September 30, 2013 and 2012, we recognized amortization of the Roche Deferred Revenues and manufacturing prepayments totaling approximately \$3.9 million and \$1.5 million, respectively. The total of Roche Deferred Revenues and manufacturing prepayments was approximately \$42.0 million and \$35.9 million as of September 30, 2013 and December 31, 2012, respectively.

We recognized zero and \$4.0 million as revenues under collaborative agreements related to the achievement of a regulatory milestone pursuant to the terms of the Roche Collaboration for the three and nine months ended September 30, 2012, respectively.

#### Gammagard Collaboration

In September 2007, we entered into a license and collaborative agreement with Baxter, under which Baxter obtained a worldwide, exclusive license to develop and commercialize a product consisting of rHuPH20 combined with a current Baxter product, GAMMAGARD LIQUID™ (the "Gammagard Collaboration"). As of September 30, 2013, we have received \$17.0 million under the Gammagard Collaboration, including the \$10.0 million upfront license fee payment, a \$3.0 million regulatory milestone payment and a \$4.0 million sales-based payment. Baxter will pay us a royalty on each product commercialized under the agreement consisting of a mid-single digit percent of the net sales of such product.

In May 2013, the European Commission granted Baxter marketing authorization in all EU Member States for the use of HyQvia (solution for subcutaneous use), a combination of GAMMAGARD LIQUID and rHuPH20 in dual vial units, as replacement therapy for adult patients with primary and secondary immunodeficiencies. Baxter launched HyQvia into the first EU country in July 2013 and plans to introduce HyQvia in additional selected EU countries during 2013 and expand the launch to other EU markets in 2014. The achievement of the first commercial sale triggered a \$4.0 million payment to us. We determined this payment to be a sales-based payment. Due to our continuing involvement obligations, revenue from the sales-based payment was deferred and is being recognized over the remaining term of the Gammagard Collaboration.

The Gammagard Collaboration is applicable to both kit and formulation combinations. Baxter assumes all development, manufacturing, clinical, regulatory, sales and marketing costs under the Gammagard Collaboration, while we are responsible for the supply of rHuPH20 API. We perform research and development activities and supply rHuPH20 API at the request of Baxter, which are reimbursed by Baxter under the terms of the Gammagard Collaboration. In addition, Baxter has certain product development and commercialization obligations in major markets identified in the Gammagard Collaboration.

Unless terminated earlier in accordance with its terms, the Gammagard Collaboration continues in effect until the expiration of Baxter's obligation to pay royalties. Baxter has the obligation to pay royalties, with respect to each product in each country, during the period equal to the longer of: (a) the duration of any valid claim of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers the product in such country or (b) ten years following the date of the first commercial sale of such product in such country.

Due to our continuing involvement obligations (for example, support activities associated with rHuPH20 enzyme), the upfront and sales-based payments were deferred and are being recognized over the term of the Gammagard Collaboration. We recognized revenue from the upfront and sales-based payments in the amount of approximately \$174,000 and \$121,000 for the three months ended September 30, 2013 and 2012, respectively. We recognized revenue from the upfront and sales-based payments in the amount of approximately \$415,000 and \$362,000 for the nine months ended September 30, 2013 and 2012, respectively. Deferred revenue relating to the upfront and sales-based payments under the Gammagard Collaboration was approximately \$10.7 million and \$7.1 million as of September 30, 2013 and December 31, 2012, respectively.



### Other Collaborations

In December 2012, we and Pfizer entered into a collaboration and license agreement, under which Pfizer has the worldwide license to develop and commercialize products combining rHuPH20 enzyme with Pfizer proprietary biologics directed at six targets, of which three were specified (the “Pfizer Collaboration”). Targets may be selected on an exclusive or non-exclusive basis. In September 2013, Pfizer designated a fourth target on an exclusive basis which resulted in a \$1.5 million license fee payment to us. As of September 30, 2013, we have received \$11.0 million in upfront and license fee payments for the licenses to four specified exclusive targets and two additional targets which Pfizer has the right to elect in the future upon payment of additional fees. Unless terminated earlier in accordance with its terms, the Pfizer Collaboration continues in effect until the later of (i) expiration of the last to expire of the valid claims of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers a product developed under the collaboration, and (ii) expiration of the last to expire royalty term for a product developed under the collaboration. The royalty term of a product developed under the Pfizer Collaboration, with respect to each country, consists of the period equal to the longer of: (a) the duration of any valid claim of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers the product in such country or (b) ten years following the date of the first commercial sale of such product in such country. Pfizer may terminate the agreement prior to expiration for any reason in its entirety or on a target-by-target basis upon 30 days prior written notice to us. Upon any such termination, the license granted to Pfizer (in total or with respect to the terminated target, as applicable) will terminate, provided, however, that in the event of expiration of the agreement, the licenses granted will become perpetual, non-exclusive and fully paid-up.

In May 2011, we and ViroPharma entered into a collaboration and license agreement, under which ViroPharma obtained a worldwide exclusive license for the use of rHuPH20 enzyme in the development and commercialization of a subcutaneous injectable formulation of ViroPharma's commercialized product, Cinryze® (C1 esterase inhibitor [human]) (the “ViroPharma Collaboration”). In addition, the license provides ViroPharma with exclusivity to C1 esterase inhibitor and to the hereditary angioedema indication, along with three additional orphan indications. As of September 30, 2013, we have received \$14.0 million from ViroPharma, including the \$9.0 million nonrefundable upfront license fee payment and a \$3.0 million clinical development milestone payment. We are entitled to receive a royalty on each product commercialized under the agreement consisting of ten percent of the net sales of such product. Unless terminated earlier in accordance with its terms, the ViroPharma Collaboration continues in effect until the later of (i) expiration of the last to expire of the valid claims of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers a product developed under the collaboration, and (ii) expiration of the last to expire royalty term for a product developed under the collaboration. The royalty term of a product developed under the ViroPharma Collaboration, with respect to each country, consists of the period equal to the longer of: (a) the duration of any valid claim of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers the product in such country or (b) ten years following the date of the first commercial sale of such product in such country. ViroPharma may terminate the agreement prior to expiration for any reason on a product-by-product basis upon 90 days prior written notice to us. Upon any such termination, the license granted to ViroPharma (in total or with respect to the terminated product, as applicable) will terminate.

In June 2011, we and Intrexon entered into a collaboration and license agreement, under which Intrexon obtained a worldwide exclusive license for the use of rHuPH20 enzyme in the development and commercialization of a subcutaneous injectable formulation of Intrexon's recombinant human alpha 1-antitrypsin (rHuA1AT) (the “Intrexon Collaboration”). In addition, the license provides Intrexon with exclusivity for a defined indication (“Exclusive Field”). As of September 30, 2013, we have received \$11.0 million from Intrexon, including a nonrefundable upfront license fee payment of \$9.0 million. We are entitled to receive a royalty on each product commercialized under the agreement consisting of a percentage of the net sales of such product ranging from mid-single digits up to a low double-digit percentage. Unless terminated earlier in accordance with its terms, the Intrexon Collaboration continues in effect until the later of (i) expiration of the last to expire of the valid claims of our patents covering rHuPH20 or other specified patents developed under the collaboration which valid claim covers a product developed under the collaboration, and (ii) expiration of the last to expire royalty term for a product developed under the collaboration. The royalty term of a

product developed under the Intrexon Collaboration, with respect to each country, consists of the period equal to the longer of: (a) the duration of any valid claim of our patents covering rHuPH20 or other specified patents developed under the

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collaboration which valid claim covers the product in such country or (b) ten years following the date of the first commercial sale of such product in such country. Intrexon may terminate the agreement prior to expiration for any reason on a product-by-product basis upon 90 days prior written notice to us. Upon any such termination, the license granted to Intrexon (in total or with respect to the terminated product, as applicable) will terminate. Intrexon's chief executive officer, chairman of its board of directors and major shareholder is also a member of our board of directors. We identified the deliverables at the inception of the Pfizer, ViroPharma and Intrexon agreements which are the license, research and development services and API supply. We have determined that the license, research and development services and API supply individually represent separate units of accounting, because each deliverable has standalone value. The estimated selling prices for these units of accounting were determined based on market conditions, the terms of comparable collaborative arrangements for similar technology in the pharmaceutical and biotech industry and entity-specific factors such as the terms of our previous collaborative agreements, our pricing practices and pricing objectives and the nature of the research and development services to be performed for the collaborators. The arrangement consideration was allocated to the deliverables based on the relative selling price method.

The amount allocable to the delivered unit or units of accounting is limited to the amount that is not contingent upon the delivery of additional items or meeting other specified performance conditions (the noncontingent amount). As such, we excluded from the allocable arrangement consideration the milestone payments, annual exclusivity fees and royalties regardless of the probability of receipt. Based on the results of our analysis, we allocated \$11.0 million in license fees from Pfizer, the \$9.0 million upfront license fee from ViroPharma and the \$9.0 million upfront license fee from Intrexon to the license fee deliverable under each of the arrangements. We determined that the upfront payments were earned upon the granting of the worldwide, exclusive right to our technology to the collaborators in these arrangements. As a result, we recognized \$11.0 million in license fees under the Pfizer Collaboration, the \$9.0 million upfront license fee under the ViroPharma Collaboration and the \$9.0 million upfront license fee received under the Intrexon Collaboration as revenues under collaborative agreements in the period when such license fees were earned. There were no revenues recognized related to milestone payments under these collaborations for the three and nine months ended September 30, 2013 and 2012.

Pfizer, ViroPharma and Intrexon are each solely responsible for the development, manufacturing and marketing of any products resulting from their respective collaborations. We are entitled to receive payments for research and development services and supply of rHuPH20 API to these collaborators if requested by such collaborator. We recognize amounts allocated to research and development services as revenues under collaborative agreements as the related services are performed. We recognize amounts allocated to the sales of API as revenues under collaborative agreements when such API has met all required specifications by the collaborators and the related title and risk of loss and damages have passed to the collaborators. We cannot predict the timing of delivery of research and development services and API as they are at the collaborators' requests.

Pursuant to the terms of all of our existing collaborations collectively, we are entitled to receive additional milestone payments for the successful development of the elected targets in the aggregate of up to approximately \$68.0 million upon achievement of specified clinical development milestone events and up to approximately \$84.0 million upon achievement of specified regulatory milestone events in connection with specified regulatory filings and receipt of marketing approvals.

5. Certain Balance Sheet Items

Accounts receivable, net consist of the following:

	September 30, 2013	December 31, 2012
Accounts receivable from revenues under collaborative agreements	\$15,474,799	\$15,058,163
Accounts receivable from product sales to collaborators	7,931,957	—
Accounts receivable from other product sales	1,512,236	823,064
	24,918,992	15,881,227
Allowance for distribution fees and discounts	(397,250 )	(178,140 )
	\$24,521,742	\$15,703,087

Inventories consist of the following:

	September 30, 2013	December 31, 2012
Raw materials	\$1,218,406	\$1,127,061
Work-in-process	1,580,610	792,257
Finished goods	1,047,274	751,378
	\$3,846,290	\$2,670,696

Prepaid expenses and other assets, current consist of the following:

	September 30, 2013	December 31, 2012
Prepaid manufacturing expenses	\$5,720,041	\$8,152,602
Prepaid research and development expenses	3,121,834	2,274,551
Other prepaid expenses	1,603,147	2,250,791
Other assets	585,162	74,944
	11,030,184	12,752,888
Less long-term portion	1,891,170	—
	\$9,139,014	\$12,752,888

Property and equipment, net consist of the following:

	September 30, 2013	December 31, 2012
Research equipment	\$6,714,830	\$6,360,004
Computer and office equipment	1,738,669	1,432,975
Leasehold improvements	1,272,151	1,138,110
Building (1)	2,550,000	1,450,000
	12,275,650	10,381,089
Accumulated depreciation and amortization	(7,339,722 )	(6,680,627 )
	\$4,935,928	\$3,700,462

(1) Represents capitalized building under a build-to-suit lease arrangement where we are considered the owner (for accounting purposes only) during the construction period.

Depreciation and amortization expense totaled approximately \$301,000 and \$286,000 for the three months ended September 30, 2013 and 2012, respectively, and approximately \$893,000 and \$796,000 for the nine months ended September 30, 2013 and 2012, respectively.

Accrued expenses consist of the following:

	September 30, 2013	December 31, 2012
Accrued outsourced manufacturing expenses	\$8,613,848	\$984,192
Accrued outsourced research and development expenses	4,496,267	1,239,050
Accrued compensation and payroll taxes	5,351,965	4,053,590
Other accrued expenses	2,162,421	1,506,615
	\$20,624,501	\$7,783,447

Deferred revenue consists of the following:

	September 30, 2013	December 31, 2012
Collaborative agreements	\$49,481,253	\$43,222,473
Product sales	3,896,691	623,510
Total deferred revenue	53,377,944	43,845,983
Less current portion	7,437,433	8,891,017
Deferred revenue, net of current portion	\$45,940,511	\$34,954,966

Refer to Note 4 for a further discussion of our collaborative agreements and deferred revenue.



## 6. Long-Term Debt

In December 2012, we entered into a Loan and Security Agreement (the "Loan Agreement") with Oxford Finance LLC ("Oxford") and Silicon Valley Bank ("SVB") (collectively, the "Lenders") for a \$30 million secured single-draw term loan facility with a maturity date, as amended, of January 1, 2017, which was fully drawn on December 28, 2012. The proceeds are to be used for working capital and general business requirements. The term loan bears a fixed interest rate of 7.55% per annum. The monthly repayment schedule includes interest only payments in arrears for the first 12 months followed by equal principal and interest payments for the subsequent 36 months. The term loan requires a final payment of \$2.55 million which is due when the term loan becomes due or upon the prepayment of the facility. We have the option to prepay the outstanding balance of the term loan in full, subject to a prepayment fee of 1% to 3% depending upon when the prepayment occurs.

In connection with the term loan, the debt offering costs have been recorded as a debt discount on our condensed consolidated balance sheet which together with the final \$2.55 million payment and fixed interest rate payments will be amortized to interest expense throughout the life of the term loan using the effective interest rate method. As of September 30, 2013, accrued interest expense associated with this final payment was approximately \$921,000 and classified as other long-term liability on the condensed consolidated balance sheet.

The term loan is secured by substantially all of the assets of the Company and Halozyme, Inc., except that the collateral does not include any intellectual property (including licensing, collaboration and similar agreements relating thereto), and certain other excluded assets. The Loan Agreement contains customary representations, warranties and covenants by us, as well as customary events of default and our indemnification obligations. One of the events of default is a material adverse change which is defined as a material adverse change in our business, operations, or condition (financial or otherwise); a material impairment of the prospect of repayment of any portion of the loan; or a material impairment in the perfection or priority of lender's lien in the collateral or in the value of such collateral. As of September 30, 2013, we believe we were in compliance with all material covenants under the Loan Agreement and there was no material adverse change.

Interest expense, including amortization of the debt discount, related to the long-term debt for the three and nine months ended September 30, 2013 was approximately \$850,000 and \$2.5 million, respectively.

## 7. Stockholders' (Deficit) Equity

During the nine months ended September 30, 2013 and 2012, we issued an aggregate of 726,538 and 426,277 shares of common stock, respectively, in connection with the exercises of stock options at a weighted average exercise price of \$3.26 and \$4.56 per share, respectively, for net proceeds of approximately \$2.4 million and \$1.9 million, respectively. In addition, for the nine months ended September 30, 2013 and 2012, we issued 85,782 and 81,070 shares of common stock, respectively, upon vesting of certain RSUs. The RSU holders surrendered 58,061 and 46,930 RSUs, respectively, to pay for minimum withholding taxes totaling approximately \$374,000 and \$347,000, respectively. Stock options and unvested RSUs totaling approximately 7.9 million and 7.1 million shares of our common stock were outstanding as of September 30, 2013 and December 31, 2012, respectively. In addition, we issued 465,245 and 375,908 shares of common stock in connection with the grants of RSAs during the nine months ended September 30, 2013 and 2012, respectively.

In May 2013, our stockholders approved an amendment to our Certificate of Incorporation to increase our authorized number of shares of common stock from 150 million shares to 200 million shares. The stockholders also approved the Amended and Restated 2011 Stock Plan which provides for the grant of up to an additional 6.5 million shares of common stock.

In February 2012, we completed an underwritten public offering and issued 7,820,000 shares of common stock, including 1,020,000 shares sold pursuant to the full exercise of an over-allotment option granted to the underwriter. All of the shares were offered at a public offering price of \$10.61 per share, generating approximately \$81.5 million in net proceeds. Of the 7,820,000 shares of common stock sold, Randal J. Kirk, a member of our board of directors, through his affiliates, purchased 1,360,000 shares of common stock in this offering at the public offering price of \$10.61 per share for a total of approximately \$14.4 million.



#### 8. Commitments and Contingencies

From time to time, we may be involved in disputes, including litigation, relating to claims arising out of operations in the normal course of our business. Any of these claims could subject us to costly legal expenses and, while we generally believe that we have adequate insurance to cover many different types of liabilities, our insurance carriers may deny coverage or our policy limits may be inadequate to fully satisfy any damage awards or settlements. If this were to happen, the payment of any such awards could have a material adverse effect on our consolidated results of operations and financial position. Additionally, any such claims, whether or not successful, could damage our reputation and business. We currently are not a party to any legal proceedings, the adverse outcome of which, in management's opinion, individually or in the aggregate, would have a material adverse effect on our consolidated results of operations or financial position.

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

As used in this report, unless the context suggests otherwise, references to "Halozyme," "the Company," "we," "our," "ours," and "us" refer to Halozyme Therapeutics, Inc., and its wholly owned subsidiary, Halozyme, Inc. References to "Notes" refer to the Notes to Condensed Consolidated Financial Statements included herein (refer to Item 1 of Part 1).

The following information should be read in conjunction with the interim unaudited condensed consolidated financial statements and Notes thereto included in Item 1 of this Quarterly Report on Form 10-Q. Past financial or operating performance is not necessarily a reliable indicator of future performance, and our historical performance should not be used to anticipate results or future period trends.

This report contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. All statements in this report other than statements of historical fact are, or may be deemed to be, forward-looking statements. Words such as "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate," "think," "may," "will," "would," "should," "continue," "potential," "likely," "opportunity" and similar expressions or variations of such words are intended to identify forward-looking statements, but are not the exclusive means of identifying forward-looking statements in this report. Additionally, statements concerning future matters such as the development or regulatory approval of new products, enhancements of existing products or technologies, timing and success of the launch of new products by us or by our collaborators, third party performance under key collaboration agreements, revenue and expense levels and other statements regarding matters that are not historical are forward-looking statements. Such statements reflect management's current forecast of certain aspects of our future, are based on currently available operating, financial and competitive information and are subject to various risks, uncertainties and assumptions that could cause actual results to differ materially from those anticipated or implied in our forward-looking statements due to a number of factors including, but not limited to, those set forth below under the section entitled "Risks Factors" and elsewhere in this Quarterly Report on Form 10-Q and our most recent Annual Report on Form 10-K.

### Overview

Halozyme is a science-driven, biopharmaceutical company committed to making molecules into medicines for patients in need. Our research focuses primarily on human enzymes that alter the extracellular matrix. The extracellular matrix is a complex matrix of proteins and carbohydrates surrounding the cell that provides structural support in tissues and orchestrates many important biological activities, including cell migration, signaling and survival. Over many years, we have developed unique technology and scientific expertise enabling us to pursue this target-rich environment for the development of therapies.

Our proprietary enzymes can be used to facilitate the delivery of injected drugs and fluids, thus enhancing the efficacy and the convenience of other drugs or can be used to alter abnormal tissue structures for clinical benefit. We have chosen to exploit our technology and expertise in a balanced way to modulate both risk and spend by: (1) developing our own proprietary products in therapeutic areas with significant unmet medical needs, such as diabetes, oncology and dermatology, and (2) licensing our technology to biopharmaceutical companies to collaboratively develop products which combine our technology with the collaborators' proprietary compounds.

The majority of the products and product candidates in our current pipeline are based on rHuPH20, a patented human recombinant hyaluronidase enzyme. rHuPH20 temporarily breaks down hyaluronic acid (HA) - a naturally occurring substance that is a major component of the extracellular matrix in tissues throughout the body such as skin and cartilage. We believe this temporary degradation creates an opportunistic window for the improved subcutaneous delivery of injectable biologics, such as monoclonal antibodies and other large therapeutic molecules, as well as small molecules and fluids. The HA reconstitutes its normal density within several days and, therefore, we anticipate that any effect of rHuPH20 on the architecture of the subcutaneous space is temporary. rHuPH20 can thus be applied as a drug delivery platform to increase dispersion and absorption of other injected drugs and fluids that are injected under the skin or in the muscle thereby enhancing efficacy or convenience. For example, rHuPH20 can be used to convert drugs that must be delivered intravenously into subcutaneous injections or reducing the number of subcutaneous injections needed for effective therapy. We refer to the application of rHuPH20 to facilitate the delivery of other drugs or fluids as Enhance<sup>TM</sup> technology. rHuPH20 is also the active ingredient in our first commercially approved product, Hylenex<sup>®</sup>



recombinant (hyaluronidase human injection). Additionally, we are expanding our scientific work in the extracellular matrix by developing other enzymes and agents that target its unique aspects, giving rise to potentially new molecular entities that can be indicated in endocrinology, oncology and dermatology.

Our proprietary pipeline consists of multiple clinical stage products in diabetes, oncology and dermatology. We currently have collaborations with F. Hoffmann-La Roche, Ltd. and Hoffmann-La Roche, Inc. (Roche), Pfizer Inc. (Pfizer), Baxter Healthcare Corporation (Baxter), ViroPharma Incorporated (ViroPharma) and Intrexon Corporation (Intrexon), with two products approved for marketing in Europe, one product candidate which has been submitted for regulatory approval in the U.S., one product candidate which have been submitted for regulatory approval in Europe as well as several others at various stages of development.

Our operations to date have involved: (i) building infrastructure for and staffing our operations; (ii) acquiring, developing and securing proprietary protection for our technology; (iii) developing our proprietary product pipeline; (iv) entering into and supporting our collaborations with other companies to advance licensed product candidates; and (v) selling our own approved commercial product, Hylenex recombinant. Currently, we have received only limited revenue from the sales of Hylenex recombinant, in addition to other revenues from our collaborations.

Future revenues from the sales and/or royalties of our product candidates which have not been approved will depend on the ability of Halozyme and our collaborators to develop, manufacture, secure regulatory approvals for and commercialize the product candidates. We have incurred net operating losses each year since inception, with an accumulated deficit of approximately \$360.1 million as of September 30, 2013.

Highlights of Halozyme's third quarter activities and recent events include:

• In July 2013, Baxter launched HyQvia into the first European Union (EU) country which triggered a \$4 million payment to us.

• In September 2013, Roche launched in Europe the subcutaneous formulation of Herceptin® (trastuzumab) using rHuPH20 (Herceptin SC) for the treatment of patients with HER2-positive breast cancer. Roche received the European marketing approval for Herceptin SC in August 2013. The first commercial sale of Herceptin SC triggered a \$10 million payment to us.

• In September 2013, Pfizer elected a fourth target on an exclusive basis under our collaboration and license agreement, which triggered a \$1.5 million license fee payment to us.

• In September 2013 at the European Cancer Congress 2013, we presented exploratory analysis of progression free survival and overall survival of a small subset of patients with available biopsy samples and HA scores in a Phase 1b study of the combination of an investigational PEGylated form of rHuPH20 (PEGPH20) with gemcitabine for the treatment of patients with phase IV metastatic pancreatic cancer. Progression free survival was 219 days in patients with high levels of tumor HA (n=6), compared to 108 days for patients with low levels of tumor HA (n=11). The overall survival in the high HA group was 529 days compared to 174 days for the low HA group. Overall survival data is still not mature for the high HA group. With respect to the intent to treat population irrespective of HA status (n=24), progression free survival was 154 days and overall survival was 200 days.

#### Product and Product Candidates

We have one marketed product and multiple product candidates targeting several indications in various stages of development. The following table summarizes our proprietary product and product candidates as well as two approved products and product candidates under development with our collaborators:

##### Proprietary Pipeline

##### Hylenex Recombinant (hyaluronidase human injection)

Hylenex recombinant is a formulation of rHuPH20 that has received FDA approval to facilitate subcutaneous fluid administration for achieving hydration, to increase the dispersion and absorption of other injected drugs and, in subcutaneous urography, to improve resorption of radiopaque agents. We reintroduced Hylenex recombinant to the market in December 2011 after resolution of Baxter's voluntary recall and the return by Baxter of marketing rights to us. Upon its return to the market, our focus was to take advantage of the initial markets previously developed by Baxter. We are continuing to assess our commercial and strategic options for the product to address additional uses such as in connection with insulin pumps as described further below under "More Physiologic (Ultrafast) Insulin Program."

### More Physiologic (Ultrafast) Insulin Program

Our most advanced proprietary program uses rHuPH20 with prandial (mealtime) insulin for the treatment of diabetes mellitus. Diabetes mellitus is an increasingly prevalent, costly condition associated with substantial morbidity and mortality. Attaining and maintaining normal blood sugar levels to minimize the long-term clinical risks is a key treatment goal for people living with diabetes.

The primary goal of our more physiologic insulin program is to develop or enable a best-in-class insulin product, with demonstrated clinical benefits for diabetes mellitus patients, in comparison to the current standard of care analog insulin products. Towards that goal, we pair rHuPH20 with prandial insulin to facilitate faster insulin dispersion in, and absorption from, the subcutaneous space into the vascular compartment, leading to faster insulin response. By making mealtime insulin onset faster, i.e., providing earlier insulin to the blood and thus earlier glucose-lowering activity, PH20 may yield a more physiologic insulin effect, similar to that found in healthy, non-diabetic people. A number of clinical trials investigating the various attributes of our product candidates have been completed.

We currently view two distinct opportunities to exploit the prandial insulin market. The first opportunity (what we refer to as the Multiple Daily Injection (MDI) market) is to combine rHuPH20 with a rapid acting analog insulin, e.g., insulin lispro (Humalog®) (Lispro-PH20), insulin aspart (Novolog®) (Aspart-PH20) and insulin glulisine (Apidra®), (each such combination, Analog-PH20), to accelerate their action. Based on the data we have seen thus far, we believe that a large biotechnology or pharmaceutical company with global access to the primary care markets would be best positioned to maximize the value of the MDI market, and therefore entering into a collaboration would be an attractive option for us to leverage this opportunity.

The second opportunity (what we refer to as the Continuous Subcutaneous Insulin Injection (CSII) market) is to pre-administer Hylenex recombinant in analog insulin pump therapy at the time of infusion site change (once every 48-72 hours). We believe that the pre-administration of Hylenex recombinant could be the best product offering for the CSII market, and we currently intend to commercially exploit this opportunity ourselves in type 1 diabetes patients on insulin pumps.

The following sets forth the current development status of our insulin programs with respect to the MDI and CSII markets:

#### MDI

With regard to MDI opportunities, we published data from two treatment studies - one in type 1 diabetes patients and one in type 2 diabetes patients. Copies of these publications can be found at <http://www.halozyme.com/Technology/Journals-Abstracts-And-Posters/default.aspx>. Both studies met their primary endpoints of A1C non-inferiority (A1C is a measure of average blood sugar over three months) and improved post-prandial glucose control compared to patients who were treated with analog insulin alone. Additionally, data from the type 1 diabetes treatment study indicated that Analog-PH20 formulations reduced hypoglycemia compared to analog insulin alone.

#### CSII

For the CSII market, we have published interim data from a study evaluating the use of Hylenex recombinant in analog insulin pump therapy that showed pre-administration of Hylenex recombinant provided a “faster-on faster-off” more physiologic profile than current rapid insulin analogs. Copies of these publications can be found at <http://www.halozyme.com/Technology/Journals-Abstracts-And-Posters/default.aspx>. Data from the double-blind cross-over study showed that pre-administration of Hylenex recombinant, at the time of infusion set change, not only accelerated the absorption and action of mealtime insulin, but also provided a more consistent insulin action profile over the three days of the infusion set life and also resulted in improved post-prandial glucose control.

In preparation for commercializing Hylenex recombinant in the CSII market in type 1 diabetes for pre-administration with analog insulin, we are developing our regulatory and commercial strategy, manufacturing product, developing the delivery accessories and conducting supportive clinical studies. We are conducting additional Phase 4 clinical studies to support the commercial launch of the CSII product. In the first quarter of 2013, we initiated CONSISTENT 1, the largest study of those additional studies. CONSISTENT 1 is a multi-center, randomized, Phase 4 trial that will evaluate Hylenex recombinant as an adjunct in the treatment of people with type 1 diabetes using insulin pumps. This study is designed to evaluate treatment differences





in safety and key outcomes, with primary endpoints at four months looking at A1C, post-prandial glucose and hypoglycemic rates. Enrollment for this trial was completed in the third quarter of 2013 with more than 400 subjects. PEGPH20

We are developing PEGPH20, a new molecular entity, as a candidate for the systemic treatment of tumors that accumulate HA. PEGylation refers to the attachment of polyethylene glycol to rHuPH20, thereby creating PEGPH20. One of the novel properties of PEGPH20 is that it lasts for an extended duration in the bloodstream and, therefore, can be used to maintain therapeutic effect to treat systemic disease.

Solid malignancies often accumulate high levels of HA, including pancreatic, lung, breast, colon and prostate cancers, and therefore we believe that PEGPH20 has the potential to help patients with these types of cancer. Among solid tumors, pancreatic ductal adenocarcinoma is associated with the highest frequency of HA overexpression. This pathologic accumulation of HA, along with other matrix components, creates a unique microenvironment for the growth of tumor cells compared to normal cells. We believe that depleting the HA component of the tumor architecture with PEGPH20 disrupts the tumor microenvironment, resulting in tumor growth inhibition. In addition, removal of HA rich matrix results in opening previously constricted vessels to allow anti-cancer therapies to have greater access to the tumor, which may enhance the treatment effect of complementary therapeutic modalities. Increased blood flow may also enable increased efficacy of radiotherapy treatment.

In June 2013, we presented the results from a Phase 1b clinical study of PEGPH20 in combination with gemcitabine for the treatment of patients with stage IV metastatic pancreatic cancer (Phase 1b PEGPH20 Clinical Study) at the 2013 American Society of Clinical Oncology (ASCO) Annual meeting. This study enrolled 28 patients with previously untreated stage IV pancreatic ductal adenocarcinoma. Patients were treated with one of three doses of PEGPH20 (1.0, 1.6 and 3.0  $\mu\text{g}/\text{kg}$  twice weekly for four weeks, then weekly thereafter) in combination with gemcitabine 1000  $\text{mg}/\text{m}^2$  administered intravenously. In this study, the overall response rate (complete response + partial response) by RECIST 1.1 criteria was 42 percent (10 of 24 patients, 95 percent CI 22 – 62 percent) for those treated at therapeutic dose levels of PEGPH20 (1.6 and 3.0  $\mu\text{g}/\text{kg}$ ) as assessed by an independent radiology review. In September 2013, at the European Cancer Congress 2013, we presented exploratory analysis of progression free survival and overall survival of a small subset of patients with available biopsy samples and HA scores in the Phase 1b study. Progression free survival was 219 days in patients with high levels of tumor HA (n=6), compared to 108 days for patients with low levels of tumor HA (n=11). The overall survival in the high HA group was 529 days compared to 174 days for the low HA group. Overall survival data is still not mature for the high HA group. With respect to the intent to treat population irrespective of HA status (n=24), progression free survival was 154 days and overall survival was 200 days. The observation that patients with tumors characterized by high levels of HA may respond best to PEGPH20 has resulted in our effort to develop a companion diagnostic to enable preselection of these patients.

In the second quarter of 2013, we initiated a Phase 2 multicenter, randomized clinical trial evaluating PEGPH20 as a first-line therapy for patients with stage IV metastatic pancreatic cancer. Approximately 124 patients are expected to participate in the study and receive gemcitabine and nab-paclitaxel (ABRAXANE)<sup>TM</sup> either with or without PEGPH20. The primary outcome will be to measure progression-free survival between patients administered with PEGPH20 and those who are not.

#### HTI-501

HTI-501, an engineered drug formulation variant of cathepsin L (a lysosomal proteinase), that acts by degrading collagen, is our first conditionally-active biologic. Collagen is an abundant protein in the body, particularly in connective tissue, and is present in high amounts in the extracellular matrix in the form of collagen fibers. Collagens are a class of helical proteins that are assembled into macromolecular fibrils and fibers. The collagen fiber network provides a structural scaffolding framework in the extracellular matrix. In the skin, these collagen fibers connect the superficial epithelial tissues to the underlying connective tissues. Collagen abnormalities contribute to a number of conditions, including frozen shoulder, Dupuytren's contracture, Peyronie's disease and cellulite.

A conditionally active biologic is a molecule that is only active under certain physiological conditions. HTI-501 is active under mildly acidic conditions and inactive at the neutral pH normally found in the tissue. The enzyme is combined with a mildly



acidic buffer and injected in its active state. The enzyme is only active locally and for a short period of time. Once the mildly acidic conditions of the HTI-501 administration have been neutralized by the body, the enzyme becomes inactive. We intend to harness this conditional activity to exert control over the duration and location of the enzyme's therapeutic activity, potentially improving the efficacy or safety of this product candidate for both medical and aesthetic conditions.

We are exploring HTI-501 as an approach to the treatment of edematous fibrosclerotic panniculopathy, also known as cellulite. The condition affects the great majority of post-adolescent women and is prevalent in all races. We believe that the collagen fibers (fibrous septa) anchor the epidermis against the swelling of subcutaneous fat, which creates the dimpled appearance associated with the condition. We believe that HTI-501 deposited under the skin can release the tension in the collagenous fibrous septa and thereby smoothing the dimpled appearance of the skin. HTI-501 may also be potentially utilized as a treatment for other conditions involving collagen, such as frozen shoulder, Dupuytren's contracture, Peyronie's disease, keloids and hypertrophic scarring.

In September 2011, we initiated a Phase 1/2 clinical trial for HTI-501 outside the U.S. in women with moderate to severe cellulite. The Phase 1 dose-escalation portion of the trial was completed in 2012 while the ongoing Phase 2 portion of the trial is designed to assess the pharmacologic activity of HTI-501 and extend the safety assessment to multiple injections in a treatment area. In the third quarter of 2013, we completed the enrollment for the Phase 2 portion and the independent panel review of one month data.

Interim results from this trial were presented June 29, 2013 at the 9th Annual World Congress of Cosmetic Dermatology in Athens, Greece. The primary endpoint is physician assessment at Day 28, supported by secondary endpoints of subject self-evaluations and objective measurements of changes to the skin topography. The interim results from 12 of the planned 34 evaluable patients from this Phase 1/2 trial indicates pharmacologic activity at the primary 28 day observation point, with 83 percent of subjects (10 of 12) showing improvement from the pretreatment assessment, with a median improvement of 53 percent ( $p=.006$ ) by the primary physician assessment. In comparison, 75 percent of subjects (9 of 12) showed improvement with a median improvement of 22 percent ( $p=.009$ ) for the vehicle injection control at the same observation point. The objective measure (skin topography) for the treated area showed modest improvement in 80 percent of evaluable subjects (8 of 10) treated with HTI-501 ( $p=.042$ ), but was not significantly changed for the vehicle control ( $p=.84$ ) or a post-hoc evaluation of non-injected areas. To query the robustness of any study conclusions, an independent blinded panel evaluation of images will be performed on the evaluable subjects at one and six months following treatment. The HTI-501 enzyme and its formulation have been well tolerated so far in this trial at all doses and formulations tested, with no serious or severe adverse events. The most common side effects have been mild to moderate transient injection site discomfort and mild to moderate injection site bruising, resolving within about two weeks without intervention.

#### Collaborations

##### Roche Collaboration

In December 2006, we and Roche entered into an agreement under which Roche obtained a worldwide, exclusive license to develop and commercialize product combinations of rHuPH20 with up to thirteen Roche target compounds (the Roche Collaboration). Roche initially had the exclusive right to apply rHuPH20 to only three pre-defined Roche biologic targets with the option to exclusively develop and commercialize rHuPH20 with ten additional targets. As of September 30, 2013, Roche has elected a total of five exclusive targets and retains the option to develop and commercialize rHuPH20 with three additional targets through the payment of annual license maintenance fees. Refer to Note 4 for a further discussion of the material terms of the Roche Collaboration.

In August 2013, Roche launched in Europe the subcutaneous formulation of Herceptin SC for the treatment of patients with HER2-positive breast cancer. Roche received European marketing approval for Herceptin SC in August 2013. In March 2012, Roche announced positive results from the Phase 3 clinical trial in women with early HER2-positive breast cancer who received a fixed dose of Herceptin SC. Herceptin is approved to treat HER2-positive breast cancer and currently is given intravenously. Breast cancer is the most common cancer among women worldwide. Each year, more than 1.4 million new cases of breast cancer are diagnosed worldwide, and nearly 450,000 people will die of the disease annually. In HER2-positive breast cancer, increased quantities of the HER2 protein are present on the surface of the tumor cells. This is known as 'HER2 positivity' and affects



approximately 15-20% of people with breast cancer. The trial was designed to compare trastuzumab (active ingredient of Herceptin) concentration in the blood (pharmacokinetics), efficacy (pathologic complete response) and safety of Herceptin SC to that of Herceptin IV. The trial met its co-primary endpoints of showing that the subcutaneous formulation produced comparable results to the IV formulation including trastuzumab concentration in the blood (serum concentrations) and efficacy. No new safety signals were observed and adverse events were overall consistent with Herceptin IV. Herceptin SC is administered in about 5 minutes whereas Herceptin IV requires about 30-90 minutes to infuse. Roche is also developing an auto-injector device that should further simplify the process and could enable patients to be dosed at home or in the doctor's office rather than at an infusion clinic or hospital. Herceptin SC is also a ready-to-use formulation, and thus may also significantly reduce pharmacy time as no medicine preparation time is required. This Phase 3 clinical trial was an open-label trial involving 595 women with HER2-positive early breast cancer.

In December 2012, Roche submitted Line Extension Applications to the European Medicines Agency (EMA) for the subcutaneous formulation of MabThera® (rituximab) (MabThera SC) using rHuPH20. In February 2011, Roche began a Phase 3 clinical trial for MabThera SC. MabThera IV is approved for the treatment of non-Hodgkin's lymphoma (NHL) and Chronic Lymphocytic Leukemia (CLL), types of cancer that affect lymphocytes (white blood cells). An estimated 66,000 new cases of NHL were diagnosed in the U.S. in 2009 with approximately 125,000 new cases reported worldwide. In December 2012, Roche presented positive data from the first stage of this two-stage study at the annual meeting of the American Society of Hematology. The study investigates pharmacokinetics, efficacy and safety of MabThera SC. The primary endpoint in the first stage of the study was met, showing the MabThera SC injection resulted in non-inferior MabThera concentrations in the blood compared with IV-infused MabThera (MabThera IV).

In 2009, Roche completed a Phase 1 clinical trial for a subcutaneous formulation of Actemra. This trial investigated the safety and pharmacokinetics of subcutaneous Actemra in patients with rheumatoid arthritis. The results from this Phase 1 trial suggest that further exploration may be warranted. Actemra administered intravenously is approved for the treatment of rheumatoid arthritis. Roche is separately developing a subcutaneous form of Actemra that does not use rHuPH20 and is being investigated for weekly or biweekly administration.

Additional information about the Phase 3 Herceptin SC and Phase 3 MabThera SC clinical trials can be found at [www.clinicaltrials.gov](http://www.clinicaltrials.gov) and [www.roche-trials.com](http://www.roche-trials.com). Information available on these websites is not incorporated into this report.

#### Baxter Gammagard Collaboration

GAMMAGARD LIQUID is a current Baxter product that is indicated for the treatment of primary immunodeficiency disorders associated with defects in the immune system. In September 2007, we and Baxter entered into an agreement under which Baxter obtained a worldwide, exclusive license to develop and commercialize product combinations of rHuPH20 with GAMMAGARD LIQUID (HyQvia) (the Gammagard Collaboration). Refer to Note 4 for a further discussion of the material terms of the Gammagard Collaboration.

Baxter filed a biologic license application (BLA) for HyQvia in the U.S. in the second quarter of 2011. On August 1, 2012, we announced that the FDA had issued a complete response letter (CRL) for Baxter's HyQvia BLA. The CRL requested additional preclinical data to support the BLA. The primary issues raised in the CRL focused on non-neutralizing antibodies generated against rHuPH20 and the possible effects of these antibodies on reproduction, development and fertility. Elevated anti-rHuPH20 antibody titers were detected in the registration trial, but have not been associated with any adverse events. Pending Baxter and us providing additional preclinical data sufficient to address the regulatory questions, the FDA has requested that patients should no longer be dosed with rHuPH20 in the Baxter HyQvia program. Baxter has submitted preclinical data to the FDA and is in active dialogue with the FDA regarding what data will be required for the HyQvia BLA. Baxter has stated that it intends to resubmit the HyQvia BLA to the FDA in response to the CRL before the end of 2013.

In May 2013, the European Commission granted Baxter marketing authorization in all EU Member States for the use of HyQvia (solution for subcutaneous use) as replacement therapy for adult patients with primary and secondary immunodeficiencies. This therapy offers patients the option to administer their therapy at home, in a single subcutaneous site every three to four weeks.



Baxter has launched HyQvia into the first EU country in July 2013 and plans to introduce HyQvia in additional selected EU countries in 2013 and expand the launch to other EU markets in 2014.

#### Pfizer Collaboration

In December 2012, we and Pfizer entered into a collaboration and license agreement, under which Pfizer has the worldwide license to develop and commercialize products combining rHuPH20 enzyme with Pfizer proprietary biologics directed to up to six targets in primary care and specialty care indications (the Pfizer Collaboration). Targets may be selected on an exclusive or non-exclusive basis. In September 2013, Pfizer elected the fourth therapeutic target on an exclusive basis. Refer to Note 4 for a further discussion of the material terms of the Pfizer Collaboration.

#### ViroPharma Collaboration

In May 2011, we and ViroPharma entered into a collaboration and license agreement under which ViroPharma obtained a worldwide exclusive license for the use of rHuPH20 enzyme in the development and commercialization of a subcutaneous injectable formulation of ViroPharma's commercialized product, Cinryze (C1 esterase inhibitor [human]) (the ViroPharma Collaboration). In addition, the license provides ViroPharma with exclusivity to C1 esterase inhibitor and to hereditary angioedema, a rare, debilitating and potentially fatal genetic disease, along with three additional orphan indications. Refer to Note 4 for a further discussion of the material terms of the ViroPharma Collaboration.

In December 2012, ViroPharma initiated a Phase 2 double blind, multicenter, dose ranging study to evaluate the safety and efficacy of subcutaneous administration of Cinryze in combination with rHuPH20 in adolescents and adults with hereditary angioedema attacks. On August 1, 2013, ViroPharma announced that it was discontinuing the study following discussions with the Center for Biologics Evaluation and Research (CBER) division of the FDA as a precaution related to the emergence of an unexpected incidence and titer of non-neutralizing anti-rHuPH20 antibodies in a number of patients with the formulation being used in this study. These antibodies have not been associated with any adverse clinical effects.

#### Intrexon Collaboration

In June 2011, we and Intrexon entered into a collaboration and license agreement under which Intrexon obtained a worldwide exclusive license for the use of rHuPH20 enzyme in the development and commercialization of a subcutaneous injectable formulation of Intrexon's recombinant human alpha 1-antitrypsin (rHuA1AT) (the Intrexon Collaboration). In addition, the license provides Intrexon with exclusivity for a defined indication. Refer to Note 4 for a further discussion of the material terms of the Intrexon Collaboration.

#### Results of Operations

##### Three Months Ended September 30, 2013 Compared to Three Months Ended September 30, 2012

Product Sales, Net – Product sales, net was \$10.0 million for the three months ended September 30, 2013 compared to \$0.7 million for the three months ended September 30, 2012. The increase of \$9.3 million was mainly due to \$7.9 million in product sales of rHuPH20 enzyme (active pharmaceutical ingredients or API) for Herceptin SC and a \$1.3 million increase in product sales of Hylenex recombinant in the current period. For the three months ended September 30, 2012, we recognized \$0.7 million and zero in sales of API for HyQvia and Herceptin SC, respectively, as revenues under collaborative agreements. Based on the reintroduction of Hylenex recombinant in December 2011 and the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, we expect product sales to continue to increase through the end of 2013 as compared to 2012.



Revenues Under Collaborative Agreements – Revenues under collaborative agreements were as follows:

	Three Months Ended		
	September 30,		
	2013	2012	Change
License fee and amortization of deferred upfront payments, license fees and sales-based payments:			
Roche	\$574,822	\$503,154	\$71,668
Pfizer	1,500,000	—	1,500,000
Baxter	173,663	120,663	53,000
	2,248,485	623,817	1,624,668
Reimbursements for research and development services and supply of rHuPH20 API:			
Roche (1)	3,209,385	2,786,369	423,016
Pfizer	135,726	—	135,726
Baxter (1)	329,135	890,153	(561,018 )
ViroPharma	65,531	309,498	(243,967 )
Other	—	9,132	(9,132 )
	3,739,777	3,995,152	(255,375 )
Total revenues under collaborative agreements	\$5,988,262	\$4,618,969	\$1,369,293

(1) Subsequent to the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, revenue from supply of rHuPH20 API to the collaborators is recognized as product sales.

Research and development services rendered by us on behalf of our collaborators are at the request of the collaborators; therefore, the amount and timing of future revenues related to reimbursable research and development services and supply of API for collaboration product candidates is uncertain. We expect the non-reimbursement revenues under our collaborative agreements to continue to fluctuate in future periods based on our collaborators' abilities to meet various clinical, regulatory and sales-based milestones set forth in such agreements and our abilities to obtain new collaborative agreements.

Cost of Product Sales – Cost of product sales were \$0.7 million for the three months ended September 30, 2013 compared to \$0.2 million for the three months ended September 30, 2012. The increase of \$0.5 million in cost of product sales was mainly due to the increased product sales of Hylenex recombinant. The manufacturing costs of API for Herceptin SC incurred prior to receiving the marketing approval have been charged to research and development expenses in the periods such costs were incurred. Therefore, there was minimal cost of product sales of API for Herceptin SC in the current period. Based on the reintroduction of Hylenex recombinant in December 2011 and the European approvals of and Herceptin SC in August 2013 and HyQvia in May 2013, we expect cost of product sales to continue to increase through the end of 2013 as compared to 2012.

Research and Development – Research and development expenses consist of external costs, salaries and benefits and allocation of facilities and other overhead expenses related to research manufacturing, clinical trials, preclinical and regulatory activities. Since our inception in 1998 through September 30, 2013, we have incurred research and development expenses of \$404.9 million. From January 1, 2009 through September 30, 2013, approximately 22% and 16% of our research and development expenses were associated with the development of our more physiologic insulin and PEGPH20 product candidates, respectively. Research and development expenses incurred were as follows:

Programs	Three Months Ended		
	September 30,		
	2013	2012	Change
Product Candidates:			
More physiologic insulin program	\$7,122,223	\$1,007,313	\$6,114,910
PEGPH20	4,616,731	2,980,175	1,636,556
Hylenex recombinant	2,570,188	2,706,226	(136,038 )
HTI-501	903,742	432,969	470,773
Enhance collaborations (1)	8,076,298	8,819,243	(742,945 )
rHuPH20 platform (2)	1,640,375	1,887,988	(247,613 )
Other	759,632	1,669,577	(909,945 )
Total research and development expenses	\$25,689,189	\$19,503,491	\$6,185,698

(1) Subsequent to the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, the manufacturing costs of these collaboration products are capitalized as inventory.

(2) Includes research, development and manufacturing expenses related to our proprietary rHuPH20 enzyme. These expenses were not designated to a specific program at the time the expenses were incurred.

Research and development expenses for the more physiologic insulin program increased in the three months ended September 30, 2013 compared to the three months ended September 30, 2012 primarily due to the increased clinical trial activities in the current period. Subsequent to the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, the manufacturing costs of these collaboration products are capitalized as inventory. Except for manufacturing expenses of the approved collaboration products, we expect other research and development expenses to continue to increase through the end of 2013 as compared to 2012 as we continue with our clinical trial programs. Selling, General and Administrative – Selling, general and administrative (SG&A) expenses were \$8.1 million for the three months ended September 30, 2013 compared to \$5.6 million for the three months ended September 30, 2012. The increase of \$2.5 million, or 44%, was primarily due to a \$1.7 million increase in compensation costs mainly related to an increase in headcount and higher bonus accrual, and a \$0.5 million increase in marketing activities. In connection with the reintroduction of Hylenex recombinant in December 2011, we expect SG&A expenses to continue to increase through the end of 2013 as compared to 2012 as we plan to increase sales and marketing activities.

Interest Expense – Interest expense included interest expense and amortization of the debt discount related to the long-term debt acquired in December 2012.

Nine Months Ended September 30, 2013 Compared to Nine Months Ended September 30, 2012

Product Sales, Net – Product sales, net was \$14.6 million for the nine months ended September 30, 2013 compared to \$1.4 million for the nine months ended September 30, 2012. The increase of \$13.2 million was primarily due to \$9.0 million in product sales of rHuPH20 API for Herceptin SC and HyQvia and a \$4.0 million increase in product sales of Hylenex recombinant in the current period. For the nine months ended September 30, 2013, we recognized \$9.5 million as revenues under collaborative agreements for sales of API for Herceptin SC and HyQvia prior to the European approvals. For the nine months ended September

30, 2012, we recognized \$4.7 million in sales of API for HyQvia as revenues under collaborative agreements. Based on the reintroduction of Hylenex recombinant in December 2011 and the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, we expect product sales to continue to increase through the end of 2013 as compared to 2012.

Revenues Under Collaborative Agreements – Revenues under collaborative agreements were as follows:

	Nine Months Ended		
	September 30,		
	2013	2012	Change
Annual exclusivity fees, license fees and amortization of deferred upfront payments, license fees and sales-based payments:			
Roche	\$ 1,606,466	\$ 1,509,462	\$ 97,004
Pfizer	1,500,000	—	1,500,000
ViroPharma	1,000,000	1,000,000	—
Intrexon	1,000,000	1,000,000	—
Baxter	414,989	361,989	53,000
Other	—	428,573	(428,573 )
	5,521,455	4,300,024	1,221,431
Milestone payments:			
Roche	—	4,000,000	(4,000,000 )
	—	4,000,000	(4,000,000 )
Reimbursements for research and development services and supply of rHuPH20 API:			
Roche (1)	18,581,183	3,979,728	14,601,455
Baxter (1)	3,238,672	5,518,612	(2,279,940 )
ViroPharma	181,352	1,204,025	(1,022,673 )
Pfizer	144,503	—	144,503
Other	—	101,581	(101,581 )
	22,145,710	10,803,946	11,341,764
Total revenues under collaborative agreements	\$ 27,667,165	\$ 19,103,970	\$ 8,563,195

(1) Subsequent to the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, revenue from supply of rHuPH20 API to the collaborators is recognized as product sales.

The increase in revenue from reimbursements for research and development services and supply of rHuPH20 API was primarily due to the increase in reimbursements for manufacturing services to support potential launches by Roche. Subsequent to the marketing approvals of Herceptin SC in August 2013 and HyQvia in May 2013, revenue from supply of API to the collaborators will be recognized as product sales. Research and development services rendered by us on behalf of our collaborators are at the request of the collaborators; therefore, the amount and timing of future revenues related to reimbursable research and development services and supply of API for collaboration product candidates is uncertain. We expect the non-reimbursement revenues under our collaborative agreements to continue to fluctuate in future periods based on our collaborators' abilities to meet various clinical, regulatory and sales-based milestones set forth in such agreements and our abilities to obtain new collaborative agreements.

Cost of Product Sales – Cost of product sales were \$2.7 million for the nine months ended September 30, 2013 compared to \$0.4 million for the nine months ended September 30, 2012. The increase of \$2.3 million in cost of product sales was mainly

due to the \$1.6 million increase in cost of product sales related to the increased Hylenex recombinant sales and a \$0.6 million write-off of certain work-in-process and finished goods inventory. The manufacturing costs of API for Herceptin SC and HyQvia incurred prior to receiving the marketing approvals have been charged to research and development expenses in the periods such costs were incurred. Therefore, there was minimal cost of product sales of API for Herceptin SC and HyQvia in the current period. Based on the reintroduction of Hylenex recombinant in December 2011 and the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, we expect cost of product sales to continue to increase through the end of 2013 as compared to 2012.

Research and Development – Research and development expenses consist of external costs, salaries and benefits and allocation of facilities and other overhead expenses related to research manufacturing, clinical trials, preclinical and regulatory activities. Research and development expenses incurred were as follows:

Programs	Nine Months Ended		
	September 30, 2013	2012	Change
Product Candidates:			
More physiologic insulin program	\$ 17,918,345	\$ 3,886,571	\$ 14,031,774
PEGPH20	13,300,508	9,085,429	4,215,079
Hylenex recombinant	8,549,010	8,402,986	146,024
HTI-501	2,171,718	1,582,740	588,978
Enhanze collaborations (1)	27,843,470	17,466,229	10,377,241
rHuPH20 platform (2)	4,205,288	6,676,730	(2,471,442 )
Other	1,726,042	4,375,644	(2,649,602 )
Total research and development expenses	\$ 75,714,381	\$ 51,476,329	\$ 24,238,052

(1) Subsequent to the European approvals of Herceptin SC in August 2013 and HyQvia in May 2013, the manufacturing costs of these collaboration products are capitalized as inventory.

(2) Includes research, development and manufacturing expenses related to our proprietary rHuPH20 enzyme. These expenses were not designated to a specific program at the time the expenses were incurred.

Research and development expenses for more physiologic insulin and PEGPH20 programs increased in the nine months ended September 30, 2013 compared to the nine months ended September 30, 2012 primarily due to the increased clinical trial activities. Research and development expenses for Enhanze collaborations increased mainly due to an increase in manufacturing activities to support our collaborators' potential launches of the collaboration product candidates. Subsequent to the European approvals of Herceptin SC and HyQvia in August 2013 and May 2013, respectively, the manufacturing costs of these collaboration products are capitalized as inventory. Except for the manufacturing costs related to the collaboration product candidates, we expect other research and development costs to continue to increase through the end of 2013 as compared to 2012 as we continue with our clinical trial programs. Selling, General and Administrative – SG&A expenses were \$23.0 million for the nine months ended September 30, 2013 compared to \$17.8 million for the nine months ended September 30, 2012. The increase of \$5.2 million, or 29%, was primarily due to a \$2.4 million increase in compensation costs mainly related to an increase in headcount and higher bonus accrual, a \$1.4 million increase in marketing activities and \$0.8 million increase in professional and consulting services. In connection with the reintroduction of Hylenex recombinant in December 2011, we expect SG&A expenses to continue to increase through the end of 2013 as compared to 2012 as we plan to increase sales and marketing activities.

Interest Expense – Interest expense included interest expense and amortization of the debt discount related to the long-term debt acquired in December 2012.

## Liquidity and Capital Resources

### Overview

Our principal sources of liquidity are our existing cash, cash equivalents and available-for-sale marketable securities. As of September 30, 2013, we had cash, cash equivalents and marketable securities of approximately \$65.3 million. We will continue to have significant cash requirements to support product development activities. The amount and timing of cash requirements will depend on the success of our clinical development programs, regulatory and market acceptance, and the resources we devote to research and other commercialization activities.

We believe that our current cash and cash equivalents will be sufficient to fund our operations for at least the next twelve months. Currently, we anticipate total net cash burn of approximately \$45 to \$50 million for the year ending December 31, 2013, depending on the progress of various preclinical and clinical programs, the timing of our manufacturing scale up and the achievement of various milestones and royalties under our existing collaborative agreements. We do not expect our revenues to be sufficient to fund operations until 2014, at the earliest. We expect to fund our operations going forward with existing cash resources, anticipated revenues from our existing collaborations and cash that we may raise through future transactions. We may finance future cash needs through any one of the following financing vehicles: (i) the public offering of securities; (ii) new collaborative agreements; (iii) expansions or revisions to existing collaborative relationships; (iv) private financings; and/or (v) other equity or debt financings.

In February 2012, we filed an automatic shelf registration statement on Form S-3 (Registration No. 333-179444) with the SEC, which allows us, from time to time, to offer and sell equity, debt securities and warrants to purchase any of such securities, either individually or in units. We may, in the future, offer and sell equity, debt securities and warrants to purchase any of such securities, either individually or in units to raise capital to fund the continued development of our product candidates, the commercialization of our products or for other general corporate purposes.

Our existing cash and cash equivalents may not be adequate to fund our operations until we become cash flow positive, if ever. We cannot be certain that additional financing will be available when needed or, if available, financing will be obtained on favorable terms. If we are unable to raise sufficient funds, we may need to delay, scale back or eliminate some or all of our research and development programs, delay the launch of our product candidates, if approved, and/or restructure our operations. If we raise additional funds by issuing equity securities, substantial dilution to existing stockholders could result. If we raise additional funds by incurring debt financing, the terms of the debt may involve significant cash payment obligations, the issuance of warrants that may ultimately dilute existing stockholders when exercised and covenants that may restrict our ability to operate our business.

### Cash Flows

Net cash used in operations was \$34.1 million during the nine months ended September 30, 2013 compared to \$47.4 million during the nine months ended September 30, 2012. The \$13.3 million decrease in utilization of cash in operations was mainly due to an increase in accounts payable and accrued expenses resulting from the increased operating expenses and an increase in deferred revenue relating to the first commercial sale payments from Roche and Baxter, offset in part by an increase in accounts receivable resulting from the increased revenues.

Net cash used in investing activities was \$49.9 million during the nine months ended September 30, 2013 compared to net cash used in investing activities of \$0.9 million during the nine months ended September 30, 2012. This increase was due to the purchases of marketable securities of \$48.9 million during the nine months ended September 30, 2013. Net cash provided by financing activities was \$2.0 million during the nine months ended September 30, 2013 compared to net cash provided of \$83.1 million during the nine months ended September 30, 2012. Net cash provided by financing activities for the nine months ended September 30, 2012 consisted of \$81.5 million in net proceeds from the sale of our common stock in February 2012 and \$1.9 million in net proceeds from stock option exercises.

#### Off-Balance Sheet Arrangements

As of September 30, 2013, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which would have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. In addition, we did not engage in trading activities involving non-exchange traded contracts. As such, we are not materially exposed to any financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

#### Critical Accounting Policies and Estimates

This discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles, or U.S. GAAP. The preparation of our consolidated 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 review our estimates on an ongoing 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. Actual results may differ from these estimates under different assumptions or conditions. We believe the following accounting policies to be critical to the judgments and estimates used in the preparation of our consolidated financial statements.

#### Revenue Recognition

We generate revenues from product sales and collaborative agreements. Payments received under collaborative agreements may include nonrefundable fees at the inception of the agreements, license fees, milestone payments for specific achievements designated in the collaborative agreements, reimbursements of research and development services and supply of rHuPH20 API, and/or royalties on sales of products resulting from collaborative arrangements. We recognize revenue in accordance with the authoritative guidance on revenue recognition. Revenue is recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the seller's price to the buyer is fixed or determinable; and (4) collectibility is reasonably assured. Refer to Note 2 for a further discussion of our revenue recognition policies for product sales and revenues under our collaborative agreements and Note 4 for a further discussion of our collaborative agreements.

#### Share-Based Payments

We use the fair value method to account for share-based payments in accordance with the authoritative guidance for share-based compensation. The fair value of each option award is estimated on the date of grant using a Black-Scholes-Merton option pricing model (Black-Scholes model) that uses assumptions regarding a number of complex and subjective variables. Changes in these assumptions may lead to variability with respect to the amount of expense we recognize in connection with share-based payments. Refer to Note 2 for a further discussion of share-based payments.

#### Research and Development Expenses

Research and development expenses include salaries and benefits, research-related manufacturing services, clinical trial expenses, contract services, facilities and other overhead expenses and other outside expenses. Research and development expenses are charged to operations as they are incurred when these expenditures relate to our research and development efforts and have no alternative future uses. Costs related to purchases or manufacture of the API and the manufacturing of a collaboration product incurred after receiving approval from the FDA or comparable regulatory agencies in foreign countries for such product are capitalized as inventory. The manufacturing costs of rHuPH20 API for Herceptin SC and HyQvia incurred after the receipt of the European marketing approvals of these products will be capitalized as inventory. Refer to Note 2 for a further discussion of research and development expenses.

Due to the uncertainty in obtaining the FDA and other regulatory approvals, our reliance on third parties and competitive pressures, we are unable to estimate with any certainty the additional costs we will incur in the continued development of our proprietary product candidates for commercialization. However, we expect our research and development expenses to increase this year as we continue with our clinical trial programs and continue to develop and manufacture our product candidates.

Clinical development timelines, likelihood of success and total costs vary widely. We anticipate that we will make ongoing determinations as to which research and development projects to pursue and how much funding to direct to each project on an ongoing basis in response to existing resource levels, the scientific and clinical progress of each product candidate, and other market and regulatory developments. We plan on focusing our resources on those proprietary and collaboration product candidates that represent the most valuable economic and strategic opportunities.

Product candidate completion dates and costs vary significantly for each product candidate and are difficult to estimate. The lengthy process of seeking regulatory approvals and the subsequent compliance with applicable regulations require the expenditure of substantial resources. Any failure by us to obtain, or any delay in obtaining, regulatory approvals could cause our research and development expenditures to increase and, in turn, have a material adverse effect on our results of operations. We cannot be certain when, or if, our product candidates will receive regulatory approval or whether any net cash inflow from our other product candidates, or development projects, will commence.

#### Inventories

Inventories are stated at lower of cost or market. Cost is determined on a first-in, first-out basis. Refer to Note 2 for a further discussion of our inventories.

The above listing is not intended to be a comprehensive list of all of our accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by U.S. GAAP. There are also areas in which our management's judgment in selecting any available alternative would not produce a materially different result. Please see our audited consolidated financial statements and notes thereto included in Part II, Item 8 of our Annual Report on Form 10-K for the year ended December 31, 2012, which contain accounting policies and other disclosures required by U.S. GAAP.

#### Recent Accounting Pronouncements

Refer to Note 2, Summary of Significant Accounting Policies – Adoption of Recent Accounting Pronouncement and Pending Adoption of Recent Accounting Pronouncement, for a discussion of recent accounting pronouncements and their effect, if any, on us.

#### Risk Factors

##### Risks Related To Our Business

We have generated only minimal revenue from product sales to date; we have a history of net losses and negative cash flow, and we may never achieve or maintain profitability.

Relative to expenses incurred in our operations, we have generated only minimal revenues from product sales, licensing fees, milestone payments, rHuPH20 API supply payments and research reimbursements to date and we may never generate sufficient revenues from future product sales, licensing fees and milestone payments to offset expenses. Even if we ultimately do achieve significant revenues from product sales, licensing fees, research reimbursements, rHuPH20 API supply payments and/or milestone payments, we expect to incur significant operating losses over the next few years. We have never been profitable, and we may never become profitable. Through September 30, 2013, we have incurred aggregate net losses of approximately \$360.1 million.

If our product candidates do not receive and maintain regulatory approvals, or if approvals are not obtained in a timely manner, such failure or delay would substantially impair our ability to generate revenues.

Approval from the FDA is necessary to manufacture and market pharmaceutical products in the United States, and the other countries in which we anticipate doing business have similar requirements. The process for obtaining FDA and other regulatory approvals is extensive, time-consuming, risky and costly, and there is no guarantee that the FDA or other regulatory bodies will approve any applications that may be filed with respect to any of our product candidates, or that the timing of any such approval will be appropriate for the desired product launch schedule for a product candidate. We, and our collaborators, attempt to provide guidance as to the timing for the filing and acceptance of such regulatory approvals, but such filings and approvals may not occur when we or our collaborators expect or at all. The FDA or other foreign regulatory agency may refuse or delay approval of our product candidates for failure to collect sufficient clinical or animal safety data and require us or our collaborators to conduct additional clinical or animal safety studies which may cause lengthy delays and increased costs to our programs. For example, we announced on August 1, 2012 that the FDA had issued a CRL for Baxter's HyQvia BLA. The CRL requested additional preclinical data to support the BLA. The primary issues raised in the letter focused on non-neutralizing antibodies generated against rHuPH20 and the possible effects of these antibodies on reproduction, development and fertility. Elevated anti-rHuPH20 antibody titers were detected in the registration trial, but have not been associated with any adverse events. Pending Baxter and us providing additional preclinical data sufficient to address the regulatory questions, the FDA has requested that patients should no longer be dosed with rHuPH20 in the Baxter clinical studies.

There can be no assurance that Baxter and we will be able to resolve the issues raised by the FDA in a timely manner which could result in a delay or failure to gain regulatory approval for the HyQvia product candidate. In addition, ViroPharma discontinued their Phase 2 study of subcutaneous Cinryze with rHuPH20 following discussions with the FDA as a precaution related to the emergence of an unexpected incidence and titer of non-neutralizing anti-rHuPH20 antibodies in a number of patients with the formulation being used in this study. These antibodies have not been associated with any adverse clinical effects. Although we do not believe at this time that the issues raised by the FDA with respect to the HyQvia BLA and the ViroPharma Phase 2 trial will have a significant impact on our proprietary and other collaboration product candidates, there can be no assurance that these concerns will not also be raised by the FDA or other health authorities in the future.

The HyQvia product developed under the Gammagard Collaboration with Baxter has been approved for marketing in Europe for the use of HyQvia (solution for subcutaneous use) as replacement therapy for adult patients with primary and secondary immunodeficiencies. In addition, Roche's Herceptin SC product has been approved for marketing in Europe for the treatment of HER2-positive breast cancer, and Roche's MabThera SC product is pending approval in Europe. We have no proprietary product candidates currently in the regulatory approval process. We and our collaborators may not be successful in obtaining such approvals for any potential products in a timely manner, or at all. Refer to the risk factor titled "Our proprietary and collaboration product candidates may not receive regulatory approvals for a variety of reasons, including unsuccessful clinical trials" for additional information relating to the approval of product candidates.

Additionally, in order to continue to manufacture and market pharmaceutical products, we must maintain our regulatory approvals. If we or any of our collaborators are unsuccessful in maintaining our regulatory approvals, our ability to generate revenues would be adversely affected.

Use of our product candidates or those of our collaborators could be associated with side effects or adverse events. As with most pharmaceutical products, use of our product candidates or those of our collaborators could be associated with side effects or adverse events which can vary in severity (from minor reactions to death) and frequency (infrequent or prevalent). Side effects or adverse events associated with the use of our product candidates or those of our collaborators may be observed at anytime, including in clinical trials or when a product is commercialized, and any such side effects or adverse events may negatively affect our or our collaborators' ability to obtain regulatory approval or market our product candidates. Side effects such as toxicity or other safety issues associated with the use of our product candidates or those of our collaborators could require us or our collaborators to perform additional studies or halt development or sale of these product candidates or expose us to product liability lawsuits which will



harm our business. We or our collaborators may be required by regulatory agencies to conduct additional animal or human studies regarding the safety and efficacy of our pharmaceutical product candidates which we have not planned

or anticipated. Furthermore, there can be no assurance that we or our collaborators will resolve any issues related to any product related adverse events to the satisfaction of the FDA or any regulatory agency in a timely manner or ever, which could harm our business, prospects and financial condition.

If our contract manufacturers are unable to manufacture and supply to us API in the quantity and quality required by us or our collaborators for use in our products and product candidates, our product development and commercialization efforts could be delayed or stopped and our collaborations could be damaged.

We have existing supply agreements with contract manufacturing organizations Avid and Cook to produce bulk API. These manufacturers each produce API under current cGMP for clinical uses. In addition, Avid currently produces API for Hylenex recombinant. In addition to supply obligations, Avid and Cook will also provide support for the chemistry, manufacturing and controls sections for FDA and other regulatory filings. We rely on their ability to successfully manufacture these batches according to product specifications, and Cook has relatively limited experience manufacturing our API. In addition, as a result of our contractual obligations to Roche, we have been required to significantly scale up our commercial API production at Cook during the last three years. If Cook is unable to obtain status as an approved manufacturing facility, or if either Avid or Cook: (i) is unable to retain status as an approved manufacturing facilities; (ii) is unable to otherwise successfully scale up our API production; (iii) fails to manufacture and supply API in the quantity and quality required by us or our collaborators for use in our proprietary and collaboration products and product candidates for any other reason, or (iv) provides the necessary support for the chemistry, manufacturing and controls sections for FDA and other regulatory filings, our business will be adversely affected. In addition, a significant change in such parties' business or financial condition could adversely affect their abilities to fulfill their contractual obligations to us. We have not established, and may not be able to establish, favorable arrangements with additional API manufacturers and suppliers of the ingredients necessary to manufacture the API should the existing manufacturers and suppliers become unavailable or in the event that our existing manufacturers and suppliers are unable to adequately perform their responsibilities. We have attempted to mitigate the impact of supply interruption through the establishment of excess API inventory, but there can be no assurances that this safety stock will be maintained or that it will be sufficient to address any delays, interruptions or other problems experienced by Avid and/or Cook. Any delays, interruptions or other problems regarding the ability of Avid and/or Cook to supply API on a timely basis could: (i) cause the delay of clinical trials or otherwise delay or prevent the regulatory approval of proprietary or collaboration product candidates; (ii) delay or prevent the effective commercialization of proprietary or collaboration products; and/or (iii) cause us to breach contractual obligations to deliver API to our collaborators. Such delays would likely damage our relationship with our collaborators under our key collaboration agreements, and they would have a material adverse effect on our business and financial condition. If any party to a key collaboration agreement, including us, fails to perform material obligations under such agreement, or if a key collaboration agreement, or any other collaboration agreement, is terminated for any reason, our business could significantly suffer.

We have entered into multiple collaboration agreements under which we may receive significant future payments in the form of milestone payments, target designation fees, maintenance fees and royalties. We are dependent on our collaborators to develop and commercialize product candidates subject to our collaborations in order for us to realize any financial benefits from these collaborations. Our collaborators may not devote the attention and resources to such efforts that we would to such efforts ourselves or simultaneously develop and commercialize products in competition to those products we have licensed to them. In addition, in the event that a party fails to perform under a key collaboration agreement, or if a key collaboration agreement is terminated, the reduction in anticipated revenues could delay or suspend our product development activities for some of our product candidates, as well as our commercialization efforts for some or all of our products. Specifically, the termination of a key collaboration agreement by one of our collaborators could materially impact our ability to enter into additional collaboration agreements with new collaborators on favorable terms, if at all. In certain circumstances, the termination of a key collaboration agreement would require us to revise our corporate strategy going forward and reevaluate the applications and value of our technology.



Most of our current proprietary and collaboration products and product candidates rely on the rHuPH20 enzyme, and any adverse development regarding rHuPH20 could substantially impact multiple areas of our business, including current and potential collaborations, as well as proprietary programs.

rHuPH20 is a key technological component of Enhance technology and our most advanced proprietary and collaboration products and product candidates, including the product candidates under our Roche, Pfizer, Baxter, ViroPharma and Intrexon collaborations, our more physiologic insulin program, our PEGPH20 program and Hylenex recombinant. An adverse development for rHuPH20 (e.g., an adverse regulatory determination relating to rHuPH20, if we are unable to obtain sufficient quantities of rHuPH20, if we are unable to obtain or maintain material proprietary rights to rHuPH20 or if we discover negative characteristics of rHuPH20) would substantially impact multiple areas of our business, including current and potential collaborations, as well as proprietary programs. For example, elevated anti-rHuPH20 antibody titers have been detected in the registration trial for Baxter's HyQvia product candidate as well as in ViroPharma's Phase 2 clinical trial with subcutaneous Cinryze with rHuPH20, but have not been associated, in either case, with any adverse events. Baxter has submitted interim preclinical data to the FDA regarding the antibodies related to the CRL Letter received for the HyQvia BLA, and is in active dialogue with the FDA regarding what data will be required for the HyQvia BLA. ViroPharma has chosen to discontinue the Phase 2 clinical trial with subcutaneous Cinryze with rHuPH20 due to the unexpected incidence and titer of antibodies in a number of patients with the formulation being used in this study. We monitor for antibodies to rHuPH20 in our collaboration and proprietary programs, and although we do not believe at this time that the incidence of non-neutralizing anti-rHuPH20 antibodies in either the HyQvia program or the ViroPharma program will have a significant impact on our other proprietary and other collaboration product candidates, there can be no assurance that there will not be other such occurrences in our other programs or that concerns regarding these antibodies will not also be raised by the FDA or other health authorities in the future, which could result in delays or discontinuations of our development or commercialization activities or deter entry into additional collaborations with third parties.

Our proprietary and collaboration product candidates may not receive regulatory approvals for a variety of reasons, including unsuccessful clinical trials.

Clinical testing of pharmaceutical products is a long, expensive and uncertain process, and the failure or delay of a clinical trial can occur at any stage. Even if initial results of preclinical and nonclinical studies or clinical trial results are promising, we or our collaborators may obtain different results in subsequent trials or studies that fail to show the desired levels of safety and efficacy, or we may not, or our collaborators may not, obtain applicable regulatory approval for a variety of other reasons. Preclinical, nonclinical, and clinical trials for any of our proprietary or collaboration product candidates could be unsuccessful, which would delay or prohibit regulatory approval and commercialization of the product candidates. In the United States and other jurisdictions, regulatory approval can be delayed, limited or not granted for many reasons, including, among others:

- clinical results may not meet prescribed endpoints for the studies or otherwise provide sufficient data to support the efficacy of our product candidates;
- clinical and nonclinical test results may reveal side effects, adverse events or unexpected safety issues associated with the use of our product candidates;
- regulatory review may not find a product candidate safe or effective enough to merit either continued testing or final approval;
- regulatory review may not find that the data from preclinical testing and clinical trials justifies approval, or they may require additional studies that would significantly delay or make continued pursuit of approval commercially unattractive;
- a regulatory agency may reject our trial data or disagree with our interpretations of either clinical trial data or applicable regulations;
- the cost of clinical trials required for product approval may be greater than what we originally anticipate, and we may decide to not pursue regulatory approval for such a product;
- a regulatory agency may not approve our manufacturing processes or facilities, or the processes or facilities of our collaborators, our contract manufacturers or our raw material suppliers;
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a regulatory agency may identify problems or other deficiencies in our existing manufacturing processes or facilities, or the existing processes or facilities of our collaborators, our contract manufacturers or our raw material suppliers;

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- a regulatory agency may change its formal or informal approval requirements and policies, act contrary to previous guidance, adopt new regulations or raise new issues or concerns late in the approval process; or a product candidate may be approved only for indications that are narrow or under conditions that place the product at a competitive disadvantage, which may limit the sales and marketing activities for such product candidate or otherwise adversely impact the commercial potential of a product.

If a proprietary or collaboration product candidate is not approved in a timely fashion on commercially viable terms, or if development of any product candidate is terminated due to difficulties or delays encountered in the regulatory approval process, it could have a material adverse impact on our business, and we will become more dependent on the development of other proprietary or collaboration product candidates and/or our ability to successfully acquire other products and technologies. There can be no assurances that any proprietary or collaboration product candidate will receive regulatory approval in a timely manner, or at all.

We anticipate that certain proprietary and collaboration products will be marketed, and perhaps manufactured, in foreign countries. The process of obtaining regulatory approvals in foreign countries is subject to delay and failure for the reasons set forth above, as well as for reasons that vary from jurisdiction to jurisdiction. The approval process varies among countries and jurisdictions and can involve additional testing. The time required to obtain approval may differ from that required to obtain FDA approval. Foreign regulatory agencies may not provide approvals on a timely basis, if at all. Approval by the FDA does not ensure approval by regulatory authorities in other countries or jurisdictions, and approval by one foreign regulatory authority does not ensure approval by regulatory authorities in other foreign countries or jurisdictions or by the FDA.

Our third party collaborators are responsible for providing certain proprietary materials that are essential components of our collaboration product candidates, and any failure to supply these materials could delay the development and commercialization efforts for these collaboration product candidates and/or damage our collaborations.

Our development and commercialization collaborators are responsible for providing certain proprietary materials that are essential components of our collaboration product candidates. For example, Roche is responsible for producing the Herceptin and MabThera required for its subcutaneous product candidates and Baxter is responsible for producing the GAMMAGARD LIQUID for its product candidate. If a collaborator, or any applicable third party service provider of a collaborator, encounters difficulties in the manufacture, storage, delivery, fill, finish or packaging of the collaboration product candidate or component of such product candidate, such difficulties could (i) cause the delay of clinical trials or otherwise delay or prevent the regulatory approval of collaboration product candidates; and/or (ii) delay or prevent the effective commercialization of collaboration products. Such delays could have a material adverse effect on our business and financial condition. For example, Baxter received a Warning Letter from the FDA in January 2010 regarding Baxter's GAMMAGARD LIQUID manufacturing facility in Lessines, Belgium. The FDA indicated in March 2010 that the issues raised in the Warning Letter had been addressed by Baxter, and we do not expect these issues to impact the development of the GAMMAGARD LIQUID product candidate.

We rely on third parties to prepare, fill, finish and package our products and product candidates, and if such third parties should fail to perform, our commercialization and development efforts for our products and product candidates could be delayed or stopped.

We rely on third parties to store and ship API on our behalf and to also prepare, fill, finish and package our products and product candidates prior to their distribution. If we are unable to locate third parties to perform these functions on terms that are acceptable to us, or if the third parties we identify fail to perform their obligations, the progress of clinical trials could be delayed or even suspended and the commercialization of approved product candidates could be delayed or prevented. For example, Hylenex recombinant was voluntarily recalled in May 2010 because a portion of the Hylenex recombinant manufactured by Baxter was not in compliance with the requirements of the underlying Hylenex recombinant agreements. During the second quarter of 2011, we submitted the data that the FDA had requested to support the reintroduction of Hylenex recombinant. The FDA approved the submitted data and granted the reintroduction of Hylenex recombinant, and we reintroduced Hylenex recombinant to the market in December 2011. In June 2011, we entered into a commercial manufacturing and supply agreement with Baxter, under which Baxter will fill, finish and package Hylenex recombinant for us. Under our commercial manufacturing and supply agreement with Baxter, Baxter has agreed to fill and finish Hylenex recombinant for us for a limited period of time.

The initial term of the commercial manufacturing and supply agreement with Baxter expires on December 31, 2013. However, upon regulatory approval of a second

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filling line, the initial term will automatically be extended to December 31, 2015, subject to further extensions in accordance with the terms and conditions of the agreement. In June 2011, we entered into a services agreement with a third party manufacturer for the technology transfer and manufacture of Hylenex recombinant. If we are unable to receive regulatory approval for the third party manufacturer prior to the expiration of the commercial manufacturing and supply agreement with Baxter or if the new manufacturer encounters difficulties in the manufacture, fill, finish or packaging of Hylenex recombinant, our business and financial condition could be adversely effected.

If we are unable to sufficiently develop our sales, marketing and distribution capabilities or enter into successful agreements with third parties to perform these functions, we will not be able to fully commercialize our products. We may not be successful in marketing and promoting our approved product, Hylenex recombinant or any other products we develop or acquire in the future. Our sales, marketing and distribution capabilities are very limited. In order to commercialize any products successfully, we must internally develop substantial sales, marketing and distribution capabilities or establish collaborations or other arrangements with third parties to perform these services. We do not have extensive experience in these areas, and we may not be able to establish adequate in-house sales, marketing and distribution capabilities or engage and effectively manage relationships with third parties to perform any or all of such services. To the extent that we enter into co-promotion or other licensing arrangements, our product revenues are likely to be lower than if we directly marketed and sold our products, and any revenues we receive will depend upon the efforts of third parties, whose efforts may not meet our expectations or be successful. These third parties would be largely responsible for the speed and scope of sales and marketing efforts, and may not dedicate the resources necessary to maximize product opportunities. Our ability to cause these third parties to increase the speed and scope of their efforts may also be limited. In addition, sales and marketing efforts could be negatively impacted by the delay or failure to obtain additional supportive clinical trial data for our products. In some cases, third party collaborators are responsible for conducting these additional clinical trials, and our ability to increase the efforts and resources allocated to these trials may be limited. For example, in January 2011, we and Baxter mutually agreed to terminate the Hylenex Collaboration and the associated agreements.

If we or our collaborators fail to comply with regulatory requirements applicable to promotion, sale and manufacturing of approved products, regulatory agencies may take action against us or them, which could significantly harm our business.

Any approved products, along with the manufacturing processes, post-approval clinical data, labeling, advertising and promotional activities for these products, are subject to continual requirements and review by the FDA, state and foreign regulatory bodies. Regulatory authorities subject a marketed product, its manufacturer and the manufacturing facilities to continual review and periodic inspections. We, our collaborators and our respective contractors, suppliers and vendors, will be subject to ongoing regulatory requirements, including complying with regulations and laws regarding advertising, promotion and sales of drug products, required submissions of safety and other post-market information and reports, registration requirements, cGMP regulations (including requirements relating to quality control and quality assurance, as well as the corresponding maintenance of records and documentation), and the requirements regarding the distribution of samples to physicians and recordkeeping requirements. Regulatory agencies may change existing requirements or adopt new requirements or policies. We, our collaborators and our respective contractors, suppliers and vendors, may be slow to adapt or may not be able to adapt to these changes or new requirements.

In particular, regulatory requirements applicable to pharmaceutical products make the substitution of suppliers and manufacturers costly and time consuming. We have minimal internal manufacturing capabilities and are, and expect to be in the future, entirely dependent on contract manufacturers and suppliers for the manufacture of our products and for their active and other ingredients. The disqualification of these manufacturers and suppliers through their failure to comply with regulatory requirements could negatively impact our business because the delays and costs in obtaining and qualifying alternate suppliers (if such alternative suppliers are available, which we cannot assure) could delay clinical trials or otherwise inhibit our ability to bring approved products to market, which would have a material adverse effect on our business and financial condition. Likewise, if we, our collaborators and our respective contractors, suppliers and vendors involved in sales and promotion of our products do not comply with applicable laws and regulations, for example off-label or false or misleading promotion, this could materially harm our business



and financial condition.

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Failure to comply with regulatory requirements may result in any of the following:

- restrictions on our products or manufacturing processes;
- warning letters;
- withdrawal of the products from the market;
- voluntary or mandatory recall;
- fines;
- suspension or withdrawal of regulatory approvals;
- suspension or termination of any of our ongoing clinical trials;
- refusal to permit the import or export of our products;
- refusal to approve pending applications or supplements to approved applications that we submit;
- product seizure;
- injunctions; or
- the imposition of civil or criminal penalties.

We may wish to raise additional capital in the next twelve months and there can be no assurance that we will be able to obtain such funds.

During the next twelve months, we may wish to raise additional capital to continue the development of our product candidates or for other current corporate purposes. Our current cash reserves and expected revenues during the next few years may not be sufficient for us to continue the development of our proprietary product candidates, to fund general operations and conduct our business at the level desired. In addition, if we engage in acquisitions of companies, products or technologies in order to execute our business strategy, we may need to raise additional capital. We may raise additional capital in the future through one or more financing vehicles that may be available to us including (i) the public or private issuance of securities; (ii) new collaborative agreements; and/or (iii) expansions or revisions to existing collaborative relationships.

In view of our stage of development, business prospects, the nature of our capital structure and general market conditions, if we are required to raise additional capital in the future, the additional financing may not be available on favorable terms, or at all. If additional capital is not available on favorable terms when needed, we will be required to raise capital on adverse terms or significantly reduce operating expenses through the restructuring of our operations. If we raise additional capital, a substantial number of additional shares may be issued, and these shares will dilute the ownership interest of our current investors.

We currently have significant debt and failure by us to fulfill our obligations under the applicable loan agreements may cause the repayment obligations to accelerate.

On December 28, 2012, we and our subsidiary, Halozyne, Inc., a California corporation, entered into a Loan and Security Agreement (the Loan Agreement) with Oxford Finance LLC, a Delaware limited liability company, and Silicon Valley Bank, a California corporation, providing for a \$30 million secured single-draw term loan facility with a maturity date of January 1, 2017. The term loan was fully drawn at close and the proceeds are to be used for working capital and general business requirements. The term loan facility is secured by substantially all of the assets of the Company and Halozyne, Inc., except that the collateral does not include any equity interests in Halozyne, Inc., any intellectual property (including licensing, collaboration and similar agreements relating thereto), and certain other excluded assets. The Loan Agreement contains customary representations, warranties and covenants by us, as well as customary events of default and our indemnification obligations. One of the events of default is a material adverse change which is defined as a material adverse change in our business, operations or condition (financial or otherwise); a material impairment of the prospect of repayment of any portion of the loan; or a material impairment in the perfection or priority of lender's lien in the collateral or in the value of such collateral. If we are unable to fulfill our obligations to the lenders under the applicable loan agreements, this could create a material default such that our obligation to repay the loan is accelerated which could harm our financial condition.

If proprietary or collaboration product candidates are approved for marketing but do not gain market acceptance, our business may suffer and we may not be able to fund future operations.

Assuming that our proprietary or collaboration product candidates obtain the necessary regulatory approvals for commercial sale, a number of factors may affect the market acceptance of these existing product candidates or any other products which are developed or acquired in the future, including, among others:

- the price of products relative to other therapies for the same or similar treatments;
- the perception by patients, physicians and other members of the health care community of the effectiveness and safety of these products for their prescribed treatments relative to other therapies for the same or similar treatments;
- our ability to fund our sales and marketing efforts and the ability and willingness of our collaborators to fund sales and marketing efforts;
- the degree to which the use of these products is restricted by the approved product label;
- the effectiveness of our sales and marketing efforts and the effectiveness of the sales and marketing efforts of our collaborators;
- the introduction of generic competitors; and
- the extent to which reimbursement for our products and related treatments will be available from third party payors including government insurance programs (Medicare and Medicaid) and private insurers.

If these products do not gain market acceptance, we may not be able to fund future operations, including the development or acquisition of new product candidates and/or our sales and marketing efforts for our approved products, which would cause our business to suffer.

In addition, our proprietary and collaboration product candidates will be restricted to the labels approved by FDA and applicable regulatory bodies, and these restrictions may limit the marketing and promotion of the ultimate products. If the approved labels are restrictive, the sales and marketing efforts for these products may be negatively affected. Developing and marketing pharmaceutical products for human use involves significant product liability risks for which we currently have limited insurance coverage.

The testing, marketing and sale of pharmaceutical products involves the risk of product liability claims by consumers and other third parties. Although we maintain product liability insurance coverage, product liability claims can be high in the pharmaceutical industry, and our insurance may not sufficiently cover our actual liabilities. If product liability claims were to be made against us, it is possible that the liabilities may exceed the limits of our insurance policy, or our insurance carriers may deny, or attempt to deny, coverage in certain instances. If a lawsuit against us is successful, then the lack or insufficiency of insurance coverage could materially and adversely affect our business and financial condition. Furthermore, various distributors of pharmaceutical products require minimum product liability insurance coverage before purchase or acceptance of products for distribution. Failure to satisfy these insurance requirements could impede our ability to achieve broad distribution of our proposed products, and higher insurance requirements could impose additional costs on us. In addition, since many of our collaboration product candidates include the pharmaceutical products of a third party, we run the risk that problems with the third party pharmaceutical product will give rise to liability claims against us.

Our inability to attract, hire and retain key management and scientific personnel could negatively affect our business. Our success depends on the performance of key management and scientific employees with relevant experience. We depend substantially on our ability to hire, train, motivate and retain high quality personnel, especially our scientists and management team. Particularly in view of the small number of employees on our staff to cover our numerous programs and key functions, if we are unable to retain existing personnel or identify or hire additional personnel, we may not be able to research, develop, commercialize or market our products and product candidates as expected or on a timely basis and we may not be able to adequately support current and future alliances with strategic collaborators. Furthermore, if we were to lose key management personnel, such as Gregory Frost, Ph.D., our President and Chief Executive Officer, we would likely lose some portion of our institutional knowledge and technical know-how, potentially causing a substantial

delay in one or more of our development programs until adequate replacement personnel could be hired and trained. For example, Dr. Frost has been with us from soon after our inception, and he possesses a substantial amount of knowledge about our development efforts and business. If we were to lose his services, we would experience delays in meeting our product development schedules. We currently have a severance policy applicable to all employees and a change in control policy applicable to senior executives. We have not adopted any other policies or entered into any other agreements specifically designed to motivate officers or other employees to remain with us.

We do not have key man life insurance policies on the lives of any of our employees, including Dr. Frost.

Our operations might be interrupted by the occurrence of a natural disaster or other catastrophic event.

Our operations, including laboratories, offices and other research facilities, are located in three buildings in San Diego, California. We depend on our facilities and on our collaborators, contractors and vendors for the continued operation of our business. Natural disasters or other catastrophic events, interruptions in the supply of natural resources, political and governmental changes, wildfires and other fires, floods, explosions, actions of animal rights activists, earthquakes and civil unrest could disrupt our operations or those of our collaborators, contractors and vendors. Even though we believe we carry commercially reasonable business interruption and liability insurance, and our contractors may carry liability insurance that protect us in certain events, we may suffer losses as a result of business interruptions that exceed the coverage available under our and our contractors' insurance policies or for which we or our contractors do not have coverage. Any natural disaster or catastrophic event could have a significant negative impact on our operations and financial results. Moreover, any such event could delay our research and development programs.

If we or our collaborators do not achieve projected development, clinical or regulatory goals in the timeframes we publicly announce or otherwise expect, the commercialization of our products and the development of our product candidates may be delayed and, as a result, our stock price may decline, and we may face lawsuits relating to such declines.

From time to time, we or our collaborators may publicly articulate the estimated timing for the accomplishment of certain scientific, clinical, regulatory and other product development goals. The accomplishment of any goal is typically based on numerous assumptions, and the achievement of a particular goal may be delayed for any number of reasons both within and outside of our control. If scientific, regulatory, strategic or other factors cause us to not meet a goal, regardless of whether that goal has been publicly articulated or not, our stock price may decline rapidly. For example, the announcement of the CRL received for HyQvia caused a rapid decline in our stock price. Stock price declines may also trigger direct or derivative shareholder lawsuits. As with any litigation proceeding, the eventual outcome of any legal action is difficult to predict. If any such lawsuits occur, we will incur expenses in connection with the defense of these lawsuits, and we may have to pay substantial damages or settlement costs in connection with any resolution thereof. Although we have insurance coverage against which we may claim recovery against some of these expenses and costs, the amount of coverage may not be adequate to cover the full amount or certain expenses and costs may be outside the scope of the policies we maintain. In the event of an adverse outcome or outcomes, our business could be materially harmed from depletion of cash resources, negative impact on our reputation, or restrictions or changes to our governance or other processes that may result from any final disposition of the lawsuit. Moreover, responding to and defending pending litigation significantly diverts management's attention from our operations.

In addition, the consistent failure to meet publicly announced milestones may erode the credibility of our management team with respect to future milestone estimates.

Future acquisitions could disrupt our business and harm our financial condition.

In order to augment our product pipeline or otherwise strengthen our business, we may decide to acquire additional businesses, products and technologies. As we have limited experience in evaluating and completing acquisitions, our ability as an organization to make such acquisitions is unproven. Acquisitions could require significant capital infusions and could involve many risks, including, but not limited to, the following:

- we may have to issue convertible debt or equity securities to complete an acquisition, which would dilute our stockholders and could adversely affect the market price of our common stock;



- an acquisition may negatively impact our results of operations because it may require us to amortize or write down amounts related to goodwill and other intangible assets, or incur or assume substantial debt or liabilities, or it may cause adverse tax consequences, substantial depreciation or deferred compensation charges;
- we may encounter difficulties in assimilating and integrating the business, products, technologies, personnel or operations of companies that we acquire;
- certain acquisitions may impact our relationship with existing or potential collaborators who are competitive with the acquired business, products or technologies;
- acquisitions may require significant capital infusions and the acquired businesses, products or technologies may not generate sufficient value to justify acquisition costs;
- we may take on liabilities from the acquired company such as debt, legal liabilities or business risk which could be significant;
- an acquisition may disrupt our ongoing business, divert resources, increase our expenses and distract our management;
- acquisitions may involve the entry into a geographic or business market in which we have little or no prior experience; and
- key personnel of an acquired company may decide not to work for us.

If any of these risks occurred, it could adversely affect our business, financial condition and operating results. There is no assurance that we will be able to identify or consummate any future acquisitions on acceptable terms, or at all. If we do pursue any acquisitions, it is possible that we may not realize the anticipated benefits from such acquisitions or that the market will not view such acquisitions positively.

Security breaches may disrupt our operations and harm our operating results.

The wrongful use, theft, deliberate sabotage or any other type of security breach with respect to any of our information technology storage and access systems could result in disclosure or dissemination of our proprietary and confidential information that is electronically stored, including research or clinical data, resulting in a material adverse impact on our business, operating results and financial condition. Our security and data recovery measures may not be adequate to protect against computer viruses, break-ins, and similar disruptions from unauthorized tampering with our electronic storage systems. Furthermore, any physical break-in or trespass of our facilities could result in the misappropriation, theft, sabotage or any other type of security breach with respect to our proprietary and confidential information, including research or clinical data or damage to our research and development equipment and assets. Such adverse effects could be material and irrevocable to our business, operating results and financial condition.

#### Risks Related To Ownership of Our Common Stock

Our stock price is subject to significant volatility.

We participate in a highly dynamic industry which often results in significant volatility in the market price of common stock irrespective of company performance. As a result, our high and low sales prices of our common stock during the twelve months ended September 30, 2013 were \$12.15 and \$4.80, respectively. We expect our stock price to continue to be subject to significant volatility and, in addition to the other risks and uncertainties described elsewhere in this quarterly report on Form 10-Q and all other risks and uncertainties that are either not known to us at this time or which we deem to be immaterial, any of the following factors may lead to a significant drop in our stock price:

- the presence of competitive products to those being developed by us;
- failure (actual or perceived) of our collaborators to devote attention or resources to the development or commercialization of product candidates licensed to such collaborator;
- a dispute regarding our failure, or the failure of one of our third party collaborators, to comply with the terms of a collaboration agreement;
- the termination, for any reason, of any of our collaboration agreements;
- the sale of common stock by any significant stockholder, including, but not limited to, direct or indirect sales by members of management or our Board of Directors;

- the resignation, or other departure, of members of management or our Board of Directors;
- general negative conditions in the healthcare industry;
- general negative conditions in the financial markets;
- the failure, for any reason, to obtain regulatory approval for any of our proprietary or collaboration product candidates;
- the failure, for any reason, to secure or defend our intellectual property position;
- for those products that are not yet approved for commercial sale, the failure or delay of applicable regulatory bodies to approve such products;
- identification of safety or tolerability issues;
- failure of clinical trials to meet efficacy endpoints;
- suspensions or delays in the conduct of clinical trials or securing of regulatory approvals;
- our failure, or the failure of our third party collaborators, to successfully commercialize products approved by applicable regulatory bodies such as the FDA;
- our failure, or the failure of our third party collaborators, to generate product revenues anticipated by investors;
- problems with an API contract manufacturer or a fill and finish manufacturer for any product or product candidate;
- the sale of additional debt and/or equity securities by us;
- our failure to obtain financing on acceptable terms; or
- a restructuring of our operations.

Future transactions where we raise capital may negatively affect our stock price.

We currently have the ability to offer and sell additional equity, debt securities and warrants to purchase such securities, either individually or in units, under an effective automatic shelf registration statement. Sales of substantial amounts of shares of our common stock or other securities under our shelf registration statements could lower the market price of our common stock and impair our ability to raise capital through the sale of equity securities. In the future, we may issue additional options, warrants or other derivative securities convertible into our common stock. Trading in our stock has historically been limited, so investors may not be able to sell as much stock as they want to at prevailing market prices.

Our stock has historically traded at a low daily trading volume. If low trading volume continues, it may be difficult for stockholders to sell their shares in the public market at any given time at prevailing prices.

Our rights agreement and anti-takeover provisions in our charter documents and Delaware law may make an acquisition of us more difficult.

We are party to a Rights Agreement designed to deter abusive takeover tactics and to encourage prospective acquirors to negotiate with our board of directors rather than attempt to acquire us in a manner or on terms that our board deems unacceptable, which could delay or discourage takeover attempts that stockholders may consider favorable.

In addition, anti-takeover provisions in our charter documents and Delaware law may make an acquisition of us more difficult. First, our board of directors is classified into three classes of directors. Under Delaware law, directors of a corporation with a classified board may be removed only for cause unless the corporation's certificate of incorporation provides otherwise. Our amended and restated certificate of incorporation, as amended, does not provide otherwise. In addition, our bylaws limit who may call special meetings of stockholders, permitting only stockholders holding at least 50% of our outstanding shares to call a special meeting of stockholders. Our amended and restated certificate of incorporation, as amended, does not include a provision for cumulative voting for directors. Under cumulative voting, a minority stockholder holding a sufficient percentage of a class of shares may be able to ensure the election of one or more directors. Finally, our bylaws establish procedures, including advance notice procedures, with regard to the nomination of candidates for election as directors and stockholder proposals.

These provisions may discourage potential takeover attempts, discourage bids for our common stock at a premium over market price or adversely affect the market price of, and the voting and other rights of the holders of, our common stock. These provisions could also discourage proxy contests and make it more difficult for stockholders to elect directors other than the candidates nominated by our board of directors.





In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which may prohibit large stockholders from consummating a merger with, or acquisition of, us.

These provisions may deter an acquisition of us that might otherwise be attractive to stockholders.

#### Risks Related To Our Industry

Our products must receive regulatory approval before they can be sold, and compliance with the extensive government regulations is expensive and time consuming and may result in the delay or cancellation of product sales, introductions or modifications.

Extensive industry regulation has had, and will continue to have, a significant impact on our business. All pharmaceutical companies, including ours, are subject to extensive, complex, costly and evolving regulation by the health regulatory agencies including the FDA (and with respect to controlled drug substances, the U.S. Drug Enforcement Administration (DEA)) and equivalent foreign regulatory agencies and state and local/regional government agencies. The Federal Food, Drug and Cosmetic Act, the Controlled Substances Act and other domestic and foreign statutes and regulations govern or influence the testing, manufacturing, packaging, labeling, storing, recordkeeping, safety, approval, advertising, promotion, sale and distribution of our products. We are dependent on receiving FDA and other governmental approvals prior to manufacturing, marketing and shipping our products. Consequently, there is always a risk that the FDA or other applicable governmental authorities will not approve our products or may impose onerous, costly and time-consuming requirements such as additional clinical or animal testing. The FDA or other foreign regulatory agency may, at any time, halt our and our collaborators' development and commercialization activities due to safety concerns. In addition, even if our products are approved, regulatory agencies may also take post-approval action limiting or revoking our ability to sell our products. Any of these regulatory actions may adversely affect the economic benefit we may derive from our products and therefore harm our financial condition.

Under certain of these regulations, we and our contract suppliers and manufacturers are subject to periodic inspection of our or their respective facilities, procedures and operations and/or the testing of products by the FDA, the DEA and other authorities, which conduct periodic inspections to confirm that we and our contract suppliers and manufacturers are in compliance with all applicable regulations. The FDA also conducts pre-approval and post-approval reviews and plant inspections to determine whether our systems, or our contract suppliers' and manufacturers' processes, are in compliance with cGMP and other FDA regulations. If we, or our contract supplier, fail these inspections, we may not be able to commercialize our product in a timely manner without incurring significant additional costs, or at all.

In addition, the FDA imposes a number of complex regulatory requirements on entities that advertise and promote pharmaceuticals including, but not limited to, standards and regulations for direct-to-consumer advertising, off-label promotion, industry-sponsored scientific and educational activities, and promotional activities involving the internet. We may be required to initiate or defend against legal proceedings related to intellectual property rights, which may result in substantial expense, delay and/or cessation of the development and commercialization of our products.

We primarily rely on patents to protect our intellectual property rights. The strength of this protection, however, is uncertain. For example, it is not certain that:

- we will be able to obtain patent protection for our products and technologies;
- the scope of any of our issued patents will be sufficient to provide commercially significant exclusivity for our products and technologies;
- others will not independently develop similar or alternative technologies or duplicate our technologies and obtain patent protection before we do; and
- any of our issued patents, or patent pending applications that result in issued patents, will be held valid, enforceable and infringed in the event the patents are asserted against others.

We currently own or license several patents and also have pending patent applications applicable to rHuPH20 and other proprietary materials. There can be no assurance that our existing patents, or any patents issued to us as a result of our pending patent applications, will provide a basis for commercially viable products, will provide us with any competitive advantages, or



will not face third party challenges or be the subject of further proceedings limiting their scope or enforceability. Any weaknesses or limitations in our patent portfolio could have a material adverse effect on our business and financial condition. In addition, if any of our pending patent applications do not result in issued patents, or result in issued patents with narrow or limited claims, this could result in us having no or limited protection against generic or biosimilar competition against our product candidates which would have a material adverse effect on our business and financial condition.

We may become involved in interference proceedings in the U.S. Patent and Trademark Office, or other proceedings in other jurisdictions, to determine the priority, validity or enforceability of our patents. In addition, costly litigation could be necessary to protect our patent position.

We also rely on trademarks to protect the names of our products (e.g. Hylenex recombinant). We may not be able to obtain trademark protection for any proposed product names we select. In addition, product names for pharmaceutical products must be approved by health regulatory authorities such as the FDA in addition to meeting the legal standards required for trademark protection and product names we propose may not be timely approved by regulatory agencies which may delay product launch. In addition, our trademarks may be challenged by others. If we enforce our trademarks against third parties, such enforcement proceedings may be expensive.

We also rely on trade secrets, unpatented proprietary know-how and continuing technological innovation that we seek to protect with confidentiality agreements with employees, consultants and others with whom we discuss our business. Disputes may arise concerning the ownership of intellectual property or the applicability or enforceability of these agreements, and we might not be able to resolve these disputes in our favor.

In addition to protecting our own intellectual property rights, third parties may assert patent, trademark or copyright infringement or other intellectual property claims against us. If we become involved in any intellectual property litigation, we may be required to pay substantial damages, including but not limited to treble damages, attorneys' fees and costs, for past infringement if it is ultimately determined that our products infringe a third party's intellectual property rights. Even if infringement claims against us are without merit, defending a lawsuit takes significant time, may be expensive and may divert management's attention from other business concerns. Further, we may be stopped from developing, manufacturing or selling our products until we obtain a license from the owner of the relevant technology or other intellectual property rights. If such a license is available at all, it may require us to pay substantial royalties or other fees.

Patent protection for protein-based therapeutic products and other biotechnology inventions is subject to a great deal of uncertainty, and if patent laws or the interpretation of patent laws changes, our competitors may be able to develop and commercialize products based on our discoveries.

Patent protection for protein-based therapeutic products is highly uncertain and involves complex legal and factual questions. In recent years, there have been significant changes in patent law, including the legal standards that govern the scope of protein and biotechnology patents. Standards for patentability of full-length and partial genes, and their corresponding proteins, are changing. Recent court decisions have made it more difficult to obtain patents, by making it more difficult to satisfy the patentable subject matter requirement and the requirement of non-obviousness, have decreased the availability of injunctions against infringers, and have increased the likelihood of challenging the validity of a patent through a declaratory judgment action. Taken together, these decisions could make it more difficult and costly for us to obtain, license and enforce our patents. In addition, the Leahy-Smith America Invents Act (HR 1249) was signed into law in September 2011, which among other changes to the U.S. patent laws, changes patent priority from "first to invent" to "first to file," implements a post-grant opposition system for patents and provides for a prior user defense to infringement. These judicial and legislative changes have introduced significant uncertainty in the patent law landscape and may potentially negatively impact our ability to procure, maintain and enforce patents to provide exclusivity for our products.

There also have been, and continue to be, policy discussions concerning the scope of patent protection awarded to biotechnology inventions. Social and political opposition to biotechnology patents may lead to narrower patent protection within the biotechnology industry. Social and political opposition to patents on genes and proteins and recent court decisions concerning patentability of isolated genes may lead to narrower patent protection, or narrower claim interpretation, for isolated genes, their



corresponding proteins and inventions related to their use, formulation and manufacture. Patent protection relating to biotechnology products is also subject to a great deal of uncertainty outside the United States, and patent laws are evolving and undergoing revision in many countries. Changes in, or different interpretations of, patent laws worldwide may result in our inability to obtain or enforce patents, and may allow others to use our discoveries to develop and commercialize competitive products, which would impair our business.

If third party reimbursement and customer contracts are not available, our products may not be accepted in the market. Our ability to earn sufficient returns on our products will depend in part on the extent to which reimbursement for our products and related treatments will be available from government health administration authorities, private health insurers, managed care organizations and other healthcare providers.

Third-party payors are increasingly attempting to limit both the coverage and the level of reimbursement of new drug products to contain costs. Consequently, significant uncertainty exists as to the reimbursement status of newly approved healthcare products. Third party payors may not establish adequate levels of reimbursement for the products that we commercialize, which could limit their market acceptance and result in a material adverse effect on our financial condition.

Customer contracts, such as with group purchasing organizations and hospital formularies, will often not offer contract or formulary status without either the lowest price or substantial proven clinical differentiation. If our products are compared to animal-derived hyaluronidases by these entities, it is possible that neither of these conditions will be met, which could limit market acceptance and result in a material adverse effect on our financial condition.

The rising cost of healthcare and related pharmaceutical product pricing has led to cost containment pressures that could cause us to sell our products at lower prices, resulting in less revenue to us.

Any of the proprietary or collaboration products that have been, or in the future are, approved by the FDA may be purchased or reimbursed by state and federal government authorities, private health insurers and other organizations, such as health maintenance organizations and managed care organizations. Such third party payors increasingly challenge pharmaceutical product pricing. The trend toward managed healthcare in the United States, the growth of such organizations, and various legislative proposals and enactments to reform healthcare and government insurance programs, including the Medicare Prescription Drug Modernization Act of 2003, could significantly influence the manner in which pharmaceutical products are prescribed and purchased, resulting in lower prices and/or a reduction in demand. Such cost containment measures and healthcare reforms could adversely affect our ability to sell our products.

In March 2010, the United States adopted the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Affordability Reconciliation Act (the Healthcare Reform Act). This law substantially changes the way healthcare is financed by both governmental and private insurers, and significantly impacts the pharmaceutical industry. The Healthcare Reform Act contains a number of provisions that are expected to impact our business and operations, in some cases in ways we cannot currently predict. Changes that may affect our business include those governing enrollment in federal healthcare programs, reimbursement changes, fraud and abuse and enforcement. These changes will impact existing government healthcare programs and will result in the development of new programs, including Medicare payment for performance initiatives and improvements to the physician quality reporting system and feedback program.

Additional provisions of the Healthcare Reform Act, some of which became effective in 2011, may negatively affect our revenues in the future. For example, the Healthcare Reform Act imposes a non-deductible excise tax on pharmaceutical manufacturers or importers that sell branded prescription drugs to U.S. government programs that we believe will impact our revenues from our products. In addition, as part of the Healthcare Reform Act's provisions closing a funding gap that currently exists in the Medicare Part D prescription drug program, we will also be required to provide a 50% discount on branded prescription drugs dispensed to beneficiaries under this prescription drug program. We expect that the Healthcare Reform Act and other healthcare reform measures that may be adopted in the future could have a material adverse effect on our industry generally and on our ability to maintain or increase our product sales or successfully commercialize our product candidates or could limit or eliminate our future spending on development projects.



Furthermore, individual states have become increasingly aggressive in passing legislation and implementing regulations designed to control pharmaceutical product pricing, including price or patient reimbursement constraints, discounts, restrictions on certain product access, importation from other countries and bulk purchasing. Legally mandated price controls on payment amounts by third party payors or other restrictions could negatively and materially impact our revenues and financial condition. We anticipate that we will encounter similar regulatory and legislative issues in most other countries outside the United States.

We face intense competition and rapid technological change that could result in the development of products by others that are superior to our proprietary and collaboration products under development.

Our proprietary and collaboration products have numerous competitors in the United States and abroad including, among others, major pharmaceutical and specialized biotechnology firms, universities and other research institutions that have developed competing products. The competitors for Hylenex recombinant include, but are not limited to, Bausch & Lomb Inc. and Amphastar Pharmaceuticals, Inc. For our more physiologic insulin product candidates, such competitors may include Bidel Inc., Eli Lilly, Sanofi Aventis, Novo Nordisk Inc. and Mannkind Corporation. These competitors may develop technologies and products that are more effective, safer, or less costly than our current or future proprietary and collaboration product candidates or that could render our technologies and product candidates obsolete or noncompetitive. Many of these competitors have substantially more resources and product development, manufacturing and marketing experience and capabilities than we do. In addition, many of our competitors have significantly greater experience than we do in undertaking preclinical testing and clinical trials of pharmaceutical product candidates and obtaining FDA and other regulatory approvals of products and therapies for use in healthcare.

#### Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our market risks during the quarter ended September 30, 2013.

As of September 30, 2013, our cash equivalents and marketable securities consisted of investments in money market funds, corporate debt obligations, commercial paper and certificates of deposit. These investments were made in accordance with our investment policy which specifies the categories, allocations, and ratings of securities we may consider for investment. The primary objective of our investment activities is to preserve principal while at the same time maximizing the income we receive without significantly increasing risk. Some of the financial instruments that we invest in could be subject to market risk. This means that a change in prevailing interest rates may cause the value of the instruments to fluctuate. For example, if we purchase a security that was issued with a fixed interest rate and the prevailing interest rate later rises, the value of that security will probably decline. As of September 30, 2013, based on our current investment portfolio, we do not believe that our results of operations would be materially impacted by an immediate change of 10% in interest rates.

We do not hold or issue derivatives, derivative commodity instruments or other financial instruments for speculative trading purposes. Further, we do not believe our cash, cash equivalents and investment securities have significant risk of default or illiquidity. We made this determination based on discussions with our investment advisors and a review of our holdings. While we believe our cash, cash equivalents and marketable securities do not contain excessive risk, we cannot provide absolute assurance that in the future our investments will not be subject to adverse changes in market value. All of our cash, cash equivalents and marketable securities are held at fair market value.

#### Item 4. Controls and Procedures

##### Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the timelines specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decision regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving the desired control objectives, and in

reaching a reasonable level of assurance, management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Quarterly Report on Form 10-Q.

#### Changes in Internal Control Over Financial Reporting

There have been no changes in our internal control over financial reporting that occurred during the quarter ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

### Item 1. Legal Proceedings

We currently are not a party to any legal proceedings, the adverse outcome of which, in management's opinion, individually or in the aggregate, would have a material adverse effect on our consolidated results of operations or financial position.

From time to time, we may be involved in disputes, including litigation, relating to claims arising out of operations in the normal course of our business. Any of these claims could subject us to costly legal expenses and, while we generally believe that we have adequate insurance to cover many different types of liabilities, our insurance carriers may deny coverage or our policy limits may be inadequate to fully satisfy any damage awards or settlements. If this were to happen, the payment of any such awards could have a material adverse effect on our consolidated results of operations and financial position. Additionally, any such claims, whether or not successful, could damage our reputation and business.

### Item 1A. Risk Factors

We have provided updated Risk Factors in the section labeled "Risk Factors" in Part I, Item 2, "Management's Discussion and Analysis of Financial Condition and Results of Operations". The "Risk Factors" section provides updated information in certain areas, particularly with respect to the risks and uncertainties regarding the use, regulatory approval and commercialization of our product candidates. In this Form 10-Q, we added a risk factor entitled "Security breaches may disrupt our operations and harm our operating results." In addition, as previously disclosed in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, we added a risk factor entitled "Use of our product candidates or those of our collaborators could be associated with side effects or adverse events" in that report. Except for those updates, we do not believe that the updated risk factors in this Quarterly Report have materially changed the type or magnitude of risks we face in comparison to the disclosure provided in our most recent Annual Report on Form 10-K; and we do not believe that the updated risk factors in this Quarterly Report have materially changed the type or magnitude of risks discussed in the risk factors contained in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2013.

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

None.

### Item 3. Defaults Upon Senior Securities

Not applicable.



Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

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Item 6. Exhibits

- 2.1 Agreement and Plan of Merger, dated November 14, 2007, by and between the Registrant and the Registrant's predecessor Nevada corporation (1)
- 3.1 Composite Certificate of Incorporation (2)
- 3.2 Certificate of Designation, Preferences and Rights of the terms of the Series A Preferred Stock (1)
- 3.3 Bylaws, as amended (3)
- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as amended
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and 15d-14(a) of the Securities Exchange Act of 1934, as amended
- 32 Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101.INS Instance Document
- 101.SCH Taxonomy Extension Schema Document
- 101.CAL Taxonomy Extension Calculation Linkbase Document
- 101.DEF Taxonomy Extension Definition Linkbase Document
- 101.LAB Taxonomy Extension Label Linkbase Document
- 101.PRE Taxonomy Extension Presentation Linkbase Document

(1) Incorporated by reference to the Registrant's Current Report on Form 8-K, filed November 20, 2007 (File No. 001-32335).

(2) Incorporated by reference to the Registrant's Quarterly Report on Form 10-Q, filed August 7, 2013 (File No. 001-32335).

(3) Incorporated by reference to the Registrant's Current Report on Form 8-K, filed December 12, 2011 (File No. 001-32335).

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Halozyme Therapeutics, Inc.,  
a Delaware corporation

Dated: November 8, 2013

/s/ Gregory I. Frost, Ph.D.  
Gregory I. Frost, Ph.D.  
President and Chief Executive Officer  
(Principal Executive Officer)

Dated: November 8, 2013

/s/ David A. Ramsay  
David A. Ramsay  
Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)