

Cyclacel Pharmaceuticals, Inc.
Form 424B3
November 16, 2012

**PROSPECTUS SUPPLEMENT NO. 4
(TO PROSPECTUS DATED APRIL 26, 2012)**

**Filed pursuant to Rule 424(b)(3)
under the Securities Act of 1933
in connection with Registration
Statement No. 333- 173291**

544,117 Shares of Common Stock

of

CYCLACEL PHARMACEUTICALS, INC.

**Issuable Upon Exercise of Outstanding Warrants
Issued in an Underwritten Offering**

This Prospectus Supplement No. 4 supplements and amends the prospectus dated April 26, 2012 (the **Prospectus**), as supplemented by the Prospectus Supplement No. 1 dated May 16, 2012, Prospectus Supplement No. 2 dated August 14, 2012, and Prospectus Supplement No. 3 dated August 24, 2012, relating to the registration of 544,117 shares of common stock, par value \$0.001 per share, of Cyclacel Pharmaceuticals, Inc. (**we** , **us** , **our company** , or **the Company**), which we may issue upon exercise of warrants to purchase common stock at an exercise price of \$9.52 per share which we issued on July 7, 2011 as part of an underwritten offerings, such warrants expiring on July 7, 2016. We refer to these warrants as the July 2011 Warrants.

To the extent any holder of our July 2011 Warrants determines to exercise its warrants, we will receive the payment of the exercise price in connection with such exercise. We will not receive any proceeds from the sale of the common stock issuable upon exercise of the July 2011 Warrants by their holders.

This prospectus supplement should be read in conjunction with the Prospectus, including any supplements or amendments to it. This prospectus supplement is not complete without, and may not be delivered or utilized except in connection with, the Prospectus, including any supplements or amendments to it. The share amounts and prices included herein give effect to the 1-for-7 reverse stock split of our common stock which became effective on August 24, 2012.

On November 16, 2012, we filed our Quarterly Report on Form 10-Q for the quarter ended September 30, 2012. That Quarterly Report on Form 10-Q, without exhibits, is attached hereto.

Investing in our common stock involves risks. See Risk Factors beginning on page 19 of the Prospectus, as well as the section entitled Risk Factors included in our recent quarterly and annual reports filed with the Securities and Exchange Commission.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the Prospectus to which it relates are truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus supplement is November 16, 2012.

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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, 2012

OR

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

Commission file number 0-50626

CYCLACEL PHARMACEUTICALS, INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or Other Jurisdiction
of Incorporation or Organization)

91-1707622
(I.R.S. Employer
Identification No.)

200 Connell Drive, Suite 1500

Berkeley Heights, New Jersey
(Address of principal executive offices)

07922
(Zip Code)

Registrant's telephone number, including area code: **(908) 517-7330**

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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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

Smaller reporting filer

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

As of November 14, 2012 there were 8,434,811 shares of the registrant's common stock outstanding.

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CYCLACEL PHARMACEUTICALS, INC.

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EXPLANATORY NOTE

In filing this Quarterly Report on Form 10-Q for the period ended September 30, 2012 (this Report), Cyclacel Pharmaceuticals, Inc. (the Company) has relied upon the order of the Securities and Exchange Commission, dated November 14, 2012, providing regulatory relief to publicly traded companies affected by Hurricane Sandy. The Company s headquarters is located in New Jersey, where it lacked power, telephone and internet service as a result of Hurricane Sandy. As a result, management required additional time to prepare, substantiate and verify the accuracy of certain disclosures in this Report, which could not be completed without incurring undue hardship and expense

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements.**

CYCLACEL PHARMACEUTICALS, INC.
(A Development Stage Company)
CONDENSED CONSOLIDATED BALANCE SHEETS

(In \$000s, except share amounts)

	December 31, 2011	September 30, 2012 (Unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 24,449	\$ 17,837
Prepaid expenses and other current assets	1,069	1,235
Current assets of discontinued operations	313	881
Total current assets	25,831	19,953
Property, plant and equipment (net)	167	140
Long-term assets of discontinued operations		433
Total assets	\$ 25,998	\$ 20,526
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	\$ 1,717	\$ 1,642
Accrued liabilities and other current liabilities	4,183	4,127
Economic rights		1,070
Other liabilities measured at fair value	71	20
Current liabilities of discontinued operations	527	438
Total current liabilities	6,498	7,297
Total liabilities	6,498	7,297
Stockholders equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized at December 31, 2011 and September 30, 2012; 1,213,142 shares issued and outstanding at December 31, 2011 and September 30, 2012. Aggregate preference in liquidation of \$13,708,505 and \$14,254,419 at December 31, 2011 and September 30, 2012, respectively	1	1
Common stock, \$0.001 par value; 100,000,000 shares authorized at December 31, 2011 and September 30, 2012; 7,745,779 and 8,434,292 shares issued and outstanding at December 31, 2011 and September 30, 2012, respectively	8	8
Additional paid-in capital	276,498	278,655
Accumulated other comprehensive loss	57	51
Deficit accumulated during the development stage	(257,064)	(265,486)
Total stockholders equity	19,500	13,229
Total liabilities and stockholders equity	\$ 25,998	\$ 20,526

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

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CYCLACEL PHARMACEUTICALS, INC.
(A Development Stage Company)
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In \$000s, except share and per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,		Period from August 13, 1996 (inception) to September 30, 2012
	2011	2012	2011	2012	
Revenues:					
Collaboration and research and development revenue	\$	\$	\$	\$	\$ 3,100
Grant revenue		38		64	3,712
Total revenues		38		64	6,812
Operating expenses:					
Research and development	2,066	1,532	7,005	4,596	190,395
General and administrative	1,814	2,028	5,136	5,917	86,748
Goodwill and intangible impairment					2,747
Restructuring costs					2,634
Total operating expenses	3,880	3,560	12,141	10,513	282,524
Operating loss	(3,880)	(3,522)	(12,141)	(10,449)	(275,712)
Other income (expense):					
Costs associated with aborted 2004 IPO					(3,550)
Payment under guarantee					(1,652)
Change in valuation of Economic Rights		(63)		27	27
Change in valuation of other liabilities measured at fair value	440	1	643	51	6,378
Foreign exchange (losses)/gains	28	6	(59)	237	(4,060)
Interest income	9	5	33	17	13,742
Interest expense					(4,567)
Other income		1		77	77
Total other income (expense)	477	(50)	617	409	6,395
Loss from continuing operations before taxes	(3,403)	(3,572)	(11,524)	(10,040)	(269,317)
Income tax benefit	126	419	443	714	19,158
Net loss from continuing operations	(3,277)	(3,153)	(11,081)	(9,326)	(250,159)
Discontinued operations:					
Income (loss) from discontinued operations, net of tax of \$0 for all periods presented	(168)	1,263	(504)	904	(11,812)
Net loss	(3,445)	(1,890)	(11,585)	(8,422)	(261,971)
Dividends on preferred ordinary shares					(38,123)
Deemed dividend on convertible exchangeable preferred shares					(3,515)
Dividend on convertible exchangeable preferred shares	(182)	(182)	(546)	(546)	(4,203)
Net loss applicable to common shareholders	\$ (3,627)	\$ (2,072)	\$ (12,131)	\$ (8,968)	\$ (307,812)
Net loss per share, continuing operations					
Basic and diluted	\$ (0.43)	\$ (0.37)	\$ (1.58)	\$ (1.13)	
	\$ (0.02)	\$ 0.15	\$ (0.07)	\$ 0.11	

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Net income (loss) per share, discontinued operations Basic and diluted								
Net loss per share Basic and diluted	\$	(0.47)	\$	(0.25)	\$	(1.73)	\$	(1.09)
Weighted average common shares outstanding		7,673,096		8,429,269		6,997,391		8,227,721

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

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CYCLACEL PHARMACEUTICALS, INC.
(A Development Stage Company)
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(In \$000s, except share and per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,		Period from August 13, 1996 (inception) to September 30, 2012
	2011	2012	2011	2012	2012
Comprehensive loss	(3,435)	(1,917)	(11,567)	(8,428)	(261,920)

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

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CYCLACEL PHARMACEUTICALS, INC.
(A Development Stage Company)
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In \$000s)
(Unaudited)

	2011	Nine Months Ended September 30, 2012	2012	Period from August 13, 1996 (inception) to September 30, 2012
Cash flows from operating activities:				
Net loss	\$ (11,585)	\$ (8,422)	\$	(261,971)
Adjustments to reconcile net loss to net cash used in operating activities:				
Accretion of interest on notes payable, net of amortization of debt premium				100
Amortization of investment premiums, net				(2,297)
Change in valuation of Economic Rights			(27)	(27)
Change in valuation of other liabilities measured at fair value	(643)	(51)		(6,378)
Depreciation and amortization	250	45		12,600
Amortization of intangible assets				886
Fixed asset impairment				221
Unrealized foreign exchange loss	(29)			7,747
Deferred revenue				(98)
Compensation for warrants issued to non-employees				1,215
Shares issued for IP rights				446
(Gain) loss on disposal of property, plant and equipment			(62)	38
Goodwill and intangibles impairment				7,934
Stock based compensation	677	287		19,310
Provision for restructuring				1,779
Amortization of issuance costs of Preferred Ordinary C shares				2,517
Transaction costs on sale of Economic Rights			33	33
Gain on termination of distribution agreement			(1,192)	(1,192)
Changes in operating assets and liabilities:				
Prepaid expenses, inventory and other current assets	450	25		(33)
Accounts payable, accrued liabilities and other current liabilities	162	(220)		(5,533)
Net cash used in operating activities	(10,718)	(9,584)		(222,703)
Investing activities:				
Purchase of ALIGN				(3,763)
Purchase of property, plant and equipment	(6)	(12)		(8,849)
Proceeds from sale of property, plant and equipment			62	225
Purchase of short-term investments				(156,657)
Redemptions of short-term investments, net of maturities				162,729
Net cash provided by (used in) investing activities	(6)	50		(6,315)
Financing activities:				
Payment of capital lease obligations				(3,719)
Proceeds from issuance of ordinary and preferred ordinary shares, net of issuance costs				121,678
Proceeds from issuance of common stock, warrants and economic rights, net of issuance costs	9,258	2,886		94,557
Net proceeds from stock options and warrants exercised	3	48		221

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Payment of preferred stock dividend	(364)	(1,898)
Repayment of government loan		(455)

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CYCLACEL PHARMACEUTICALS, INC.
(A Development Stage Company)
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(In \$000s)
(Unaudited)

	2011	Nine Months Ended September 30, 2012	2012	Period from August 13, 1996 (inception) to September 30, 2012
Government loan received				414
Loan received from Cyclacel Group Plc				9,103
Proceeds of committable loan notes issued from shareholders				8,883
Loans received from shareholders				1,645
Cash and cash equivalents assumed on stock purchase				17,915
Costs associated with stock purchase				(1,951)
Net cash (used in) provided by financing activities	8,897		2,934	246,393
Effect of exchange rate changes on cash and cash equivalents	7		(12)	462
Net increase (decrease) in cash and cash equivalents	(1,820)		(6,612)	17,837
Cash and cash equivalents at beginning of period	29,495		24,449	
Cash and cash equivalents at end of period	\$ 27,675		\$ 17,837	\$ 17,837

Supplemental disclosure of cash flows information:

Cash received during the period for:

Interest	20		10	11,756
Taxes	688		556	18,763

Cash paid during the period for:

Interest				(1,914)
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Schedule of non-cash transactions:

Acquisitions of equipment purchased through capital leases				3,470
Issuance of common shares in connection with license agreements				592
Issuance of ordinary shares on conversion of bridging loan				1,638
Issuance of preferred ordinary C shares on conversion of secured convertible loan notes and accrued interest				8,893
Issuance of ordinary shares in lieu of cash bonus				164
Issuance of other long term payable on ALIGN acquisition				1,122

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

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**CYCLACEL PHARMACEUTICALS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Nature of Operations

Cyclacel Pharmaceuticals, Inc. (Cyclacel or the Company) is a development-stage biopharmaceutical company dedicated to the development and commercialization of novel, mechanism-targeted drugs to treat human cancers and other serious diseases. Cyclacel's strategy is to build a diversified biopharmaceutical business focused in hematology and oncology based on a development pipeline of novel drug candidates.

Cyclacel's clinical development priorities are focused on sapacitabine, an orally available, cell cycle modulating nucleoside analogue.

Sapacitabine is being evaluated in the SEAMLESS Phase 3 trial being conducted under a Special Protocol Assessment (SPA) agreement with the US Food and Drug Administration (FDA) for the front-line treatment of acute myeloid leukemia (AML) in the elderly and in Phase 2 studies for AML, myelodysplastic syndromes (MDS), non-small cell lung cancer (NSCLC) and chronic lymphocytic leukemia. Sapacitabine is also being evaluated in a Phase 1/2 study in combination with seliciclib, our second clinical candidate.

The Company has ongoing clinical programs with seliciclib in NSCLC and nasopharyngeal cancer (NPC) and once data becomes available and is reviewed, the Company will determine the feasibility of pursuing further development and/or partnering these assets.

In addition, until September 30, 2012 the Company marketed directly in the United States Xclair® Cream for radiation dermatitis and Numoisyn® Liquid and Numoisyn® Lozenges for xerostomia pursuant to a distribution agreement with Sinclair Pharmaceuticals Limited (Sinclair). On August 10, 2012, the Company entered into an agreement with Sinclair to terminate these distribution agreements, effective September 30, 2012. See *Recent Developments* below and *Note 3 Discontinued Operations* for further details.

As a development stage enterprise, substantially all efforts of the Company to date have been devoted to performing research and development, conducting clinical trials, developing and acquiring intellectual property, raising capital and recruiting and training personnel. The Company currently anticipates that its cash and cash equivalents of approximately \$17.8 million as of September 30, 2012 are sufficient to meet its anticipated short-term working capital needs and to fund its on-going sapacitabine clinical trials for at least the next twelve months. However, the Company cannot be certain that it will be able to raise sufficient funds to complete the development and commercialize any of its product candidates currently in clinical development, should they succeed.

Basis of Presentation

The condensed consolidated balance sheet as of September 30, 2012, the condensed consolidated statements of operations and comprehensive loss for the three and nine months ended September 30, 2012 and 2011, the condensed consolidated statement of cash flows for the nine months ended September 30, 2012 and 2011 and the condensed consolidated statement of operations, comprehensive loss and cash flows for the period from August 13, 1996 (inception) to September 30, 2012, and all related disclosures contained in the accompanying notes are unaudited. The condensed consolidated balance sheet as of December 31, 2011 is derived from the audited consolidated financial statements included in the 2011 Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC). The condensed consolidated financial statements are presented on the basis of accounting principles that are generally accepted in the United States (GAAP) for interim financial information and in accordance with the rules and regulations of the SEC. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States for a complete set of financial statements. In

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the opinion of management, all adjustments, which include normal recurring adjustments necessary to present fairly the condensed consolidated balance sheet as of September 30, 2012, and the results of operations, comprehensive loss for the three and nine months ended September 30, 2012 and 2011 and for the period from August 13, 1996 (inception) to September 30, 2012, and the consolidated statements of cash flows for the nine months ended September 30, 2012 and 2011 and for the period from August 13, 1996 (inception) to September 30, 2012, have been made. The interim results for the three months ended September 30, 2012 are not necessarily indicative of the results to be expected for the year ending December 31, 2012 or for any other year. Certain prior period amounts have been reclassified to conform to current period presentation. The condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the accompanying notes for the year ended December 31, 2011, included in the Company's Annual Report on Form 10-K filed with the SEC.

Recent Developments

Reverse Stock Split

On August 24, 2012, the Company effected a 1-for-7 reverse stock split of its shares of common stock in order to increase the per share trading price of the Company's shares of common stock to satisfy the \$1.00 minimum bid price requirement for continued listing on the NASDAQ Global Market. The Company received notification from NASDAQ that as of September 11, 2012, the Company evidenced a closing bid price of its common stock price in excess of the \$1.00 minimum requirement for at least 10 consecutive trading days. Accordingly, the Company has regained compliance with Listing Rule 5450(a)(1). All share and per share information presented in this Form 10-Q gives effect to the reverse stock split.

Termination and Settlement Agreement

On August 10, 2012, the Company entered into an agreement with Sinclair to terminate, effective September 30, 2012, the distribution agreements relating to the promotion and sale of Xclair®, Numoisyn® Lozenges and Numoisyn® Liquid. The termination agreement includes a minimum royalty arrangement based on future net revenues, under which Sinclair will pay the Company a minimum of approximately \$1.0 million in quarterly installments over the three years ending on September 30, 2015. The operating results associated with the promotion and sale of Xclair®, Numoisyn® Liquid and Numoisyn® Lozenges are classified within Income (loss) from discontinued operations, net of tax in the consolidated statements of operations for all periods presented, and the associated assets and liabilities are classified within current assets of discontinued operations, long-term assets of discontinued operations, and current liabilities of discontinued operations, as appropriate, in the condensed consolidated balance sheets for all applicable periods presented. See *Note 3 Discontinued Operations* for further details.

Preferred Stock Dividend

On September 12, 2012, the Company's Board of Directors decided not to declare a quarterly cash dividend on the Company's 6% Convertible Exchangeable Preferred Stock (Preferred Stock) with respect to the third quarter of 2012 that would have otherwise been payable on November 1, 2012.

Subsequent Developments

Grant Award

In November 2012, the Company was awarded a grant of approximately \$1.9 million from the UK Government's Biomedical Catalyst to complete an Investigational New Drug (IND) directed preclinical development of CYC065, a novel orally available, second generation, CDK inhibitor.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation

The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries for the indicated periods. All significant intercompany transactions and balances have been eliminated.

Use of Estimates

The preparation of financial statements in accordance with United States GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and related disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Critical estimates include estimated levels of product returns, and inputs used to determine stock-based compensation expense and the fair value of financial instruments, such as Economic Rights and other liabilities measured at fair value. Cyclacel reviews its estimates on an ongoing basis. The estimates are based on historical experience and on various other assumptions that the Company believes to be reasonable under the circumstances. Actual results may differ from these estimates.

Cash and Cash Equivalents

Cash equivalents are stated at cost, which is substantially the same as fair value. The Company considers all highly liquid investments with an original maturity of three months or less at the time of initial purchase to be cash equivalents. The objectives of the Company's cash management policy are to safeguard and preserve funds, to maintain liquidity sufficient to meet Cyclacel's cash flow requirements and to attain a market rate of return. Cash and cash equivalents includes cash, money market funds and commercial paper.

Fair Value of Financial Instruments

Financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities, Economic Rights, and other liabilities measured at fair value. The carrying amounts of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximate their respective fair values due to the nature of the accounts, notably their short maturities. Economic Rights and other liabilities measured at fair value employ applicable inputs as described in *Note 4 - Fair Value Measurements*.

Revenue Recognition

Collaboration, research and development, and grant revenue

Certain of the Company's revenues are earned from collaborative agreements. The Company recognizes revenue when persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; the fee is fixed or determinable; and collectability is reasonably assured. Determination of whether these criteria have been met is based on management's judgments regarding the nature of the research performed, the substance of the milestones met relative to those the Company must still perform, and the collectability of any related fees. Should changes in conditions cause management to determine these criteria are not met for certain future transactions, revenue recognized for any reporting period could be adversely affected. The Company had no such collaboration revenues for the three and nine months ended September 30, 2011 and 2012.

Research and development revenues, which are earned under agreements with third parties for contract research and development activities, are recorded as the related services are performed. Milestone payments are non-refundable and recognized as revenue when earned, as evidenced by achievement of the specified milestones and the absence of ongoing performance obligations. Any amounts received in advance of performance are recorded as deferred revenue. None of the revenues previously recognized are refundable if the relevant research effort is not successful. The Company had no such research and development revenue for the three and nine months ended September 30, 2011 and 2012.

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Grant revenues from government agencies and private research foundations are recognized as the related qualified research and development costs are incurred, up to the limit of the prior approval funding amounts. All grants earned and received are not refundable. The Company had deferred grant revenue of approximately \$10,000, which is included in accrued liabilities and other current liabilities, as of September 30, 2012. The Company had no such deferred revenue at December 31, 2011.

Clinical Trial Accounting

Data management and monitoring of the Company's clinical trials are performed with the assistance of contract research organizations (CROs) or clinical research associates (CRAs) in accordance with the Company's standard operating procedures. Typically, CROs and some CRAs bill monthly for services performed, and others bill based upon milestones achieved. For outstanding amounts, the Company accrues unbilled clinical trial expenses based on estimates of the level of services performed each period. Costs of setting up clinical trial sites for participation in the trials are expensed immediately as research and development expenses. Clinical trial costs related to patient enrollment are accrued as patients are entered into the trial and any initial payment made to the clinical trial site is recognized upon execution of the clinical trial agreements and expensed as research and development expenses.

Research and Development Expenditures

Research and development expenses consist primarily of costs associated with developing the Company's product candidates, including upfront fees and milestones paid to parties from whom the Company licenses certain intellectual property, compensation and other expenses for research and development personnel, supplies and development materials, costs for consultants and related contract research, facility costs, amortization of purchased technology and depreciation. Expenditures relating to research and development are expensed as incurred.

Foreign currency and currency translation

Transactions that are denominated in a foreign currency are remeasured into the functional currency at the current exchange rate on the date of the transaction. Any foreign currency-denominated monetary assets and liabilities are subsequently remeasured at current exchange rates, with gains or losses recognized as foreign exchange (losses)/gains in the statement of operations.

The assets and liabilities of the Company's international subsidiary are translated from its functional currency into United States dollars at exchange rates prevailing at the balance sheet date. Average rates of exchange during the period are used to translate the statement of operations, while historical rates of exchange are used to translate any equity transactions.

Translation adjustments arising on consolidation due to differences between average rates and balance sheet rates, as well as unrealized foreign exchange gains or losses arising from remeasurement of foreign-currency denominated intercompany loans that are of a long-term-investment nature, are recorded in other comprehensive income.

Fair Value Measurements

Inputs used to determine fair value of financial and non-financial assets and liabilities are categorized using a fair value hierarchy that prioritizes observable and unobservable inputs into three broad levels, from Level 1, for quoted prices (unadjusted) in active markets for identical assets or liabilities, to Level 3, for unobservable inputs (see *Note 4 - Fair Value Measurements*). Management reviews the categorization of fair value inputs on a periodic basis and may determine that it is necessary to transfer an input from one level of the fair value hierarchy to another based on changes in events or circumstances, such as a change in the observability of an input. Any such transfer will be recognized at the end of the reporting period.

Income Taxes

The Company accounts for income taxes under the liability method. Under this method, deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to

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affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amounts expected to be realized. The Company's management has established a full valuation allowance against its deferred tax assets based on the determination that it is not more likely than not that the Company will recognize the benefits of those assets.

The Company applies the guidance codified in ASC 740, *Income taxes* (ASC 740) related to accounting for uncertainty in income taxes. ASC 740 specifies the accounting for uncertainty in income taxes recognized in a company's financial statements by prescribing a minimum probability threshold a tax position is required to meet before being recognized in the financial statements.

The Company records income tax benefits related to research and development tax credits, which will be claimed from H. M. Revenue & Customs, the United Kingdom's taxation and customs authority, with respect to qualifying research and development costs incurred in the same accounting period.

Stock-based Compensation

The Company grants stock options, restricted stock units and restricted stock to officers, employees and directors under the Amended and Restated Equity Incentive Plan (2006 Plan), which was approved on March 16, 2006, as amended on May 21, 2007, and subsequently amended and restated on April 14, 2008. The Company has granted various types of awards under the 2006 Plan, which is described more fully in *Note 7 - Stock-Based Compensation Arrangements*. The Company accounts for these awards under ASC 718, *Compensation - Stock Compensation* (ASC 718).

ASC 718 requires measurement of compensation cost for all stock-based awards at fair value on the date of grant and recognition of compensation over the requisite service period for awards expected to vest. The fair value of restricted stock and restricted stock units is determined based on the number of awards granted and the quoted price of the Company's common stock on the date of grant. The determination of grant-date fair value for stock option awards is estimated using the Black-Scholes model, which includes variables such as the expected volatility of the Company's share price, the anticipated exercise behavior of its employees, interest rates, and dividend yields. These variables are projected based on the Company's historical data, experience, and other factors. Changes in any of these variables could result in material adjustments to the expense recognized for share-based payments. Such value is recognized as expense over the requisite service period, net of estimated forfeitures, using the straight-line attribution method. The estimation of stock awards that will ultimately vest requires judgment, and to the extent actual results or updated estimates differ from current estimates, such amounts are recorded as a cumulative adjustment in the period estimates are revised. The Company considers many factors when estimating expected forfeitures, including type of awards granted employee class, and historical experience. Actual results and future estimates may differ substantially from current estimates.

Segments

The Company has determined its reportable segments in accordance with ASC 280, *Segment Reporting* (ASC 280) and related disclosures about products, services, geographic areas and major customers. After considering its business activities and geographic reach, the Company has concluded that it operates in just one operating segment being the discovery, development and commercialization of novel, mechanism-targeted drugs to treat cancer and other serious disorders, with development operations in two geographic areas, namely the United States and the United Kingdom.

Table of Contents***Net Loss per Common Share***

The Company calculates net loss per common share in accordance with ASC Topic 260, *Earnings Per Share* (ASC 260). Basic and diluted net loss per common share was determined by dividing net loss applicable to common stockholders by the weighted average number of common shares outstanding during the period. All share and per share information presented gives effect to the reverse stock split, which occurred on August 24, 2012. The Company's potentially dilutive shares, which include outstanding common stock options, restricted stock, restricted stock units, convertible preferred stock, and common stock warrants, have not been included in the computation of diluted net loss per share for all periods as the result would be anti-dilutive.

	September 30, 2011	September 30, 2012
Stock options	447,025	480,415
Unvested restricted stock and restricted stock units	9,671	40,121
Convertible preferred stock	73,747	73,747
Contingently issuable common stock and common stock warrants associated with Economic Rights		435,187
Common stock warrants	834,800	1,973,431
Total shares excluded from calculation	1,365,243	3,002,901

Comprehensive Income (Loss)

In accordance with ASC 220, *Comprehensive Income* (ASC 220) all components of comprehensive income (loss), including net income (loss), are reported in the financial statements in the period in which they are recognized. ASC 220 defines comprehensive income (loss) as the change in equity during a period from transactions and other events and circumstances from non-owner sources. Net income (loss) and other comprehensive income (loss), including foreign currency translation adjustments, are reported, net of any related tax effect, to arrive at comprehensive income (loss). No taxes were recognized in relation to items of other comprehensive income.

Table of Contents**3. DISCONTINUED OPERATIONS**

On August 10, 2012, the Company entered into an agreement with Sinclair to terminate, effective September 30, 2012, the distribution agreements relating to the promotion and sale of Xclair®, Numoisyn® Lozenges and Numoisyn® Liquid.

Product revenue, cost of goods sold and selling, general and administrative costs related to the promotion and sales of the of Xclair®, Numoisyn® Liquid and Numoisyn® Lozenges have been reclassified from operating results from continuing operations to income (loss) from discontinued operations in the consolidated statement of operations for all periods presented as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,		Period from August 13, 1996 (inception) to September 30, 2012
	2011 (Unaudited)	2012 (Unaudited)	2011 (Unaudited)	2012 (Unaudited)	(Unaudited)
Product revenue	\$ 164	\$ 302	\$ 524	\$ 583	\$ 3,604
Cost of goods sold	(95)	(110)	(273)	(293)	(2,045)
Selling, general and administrative	(237)	(121)	(755)	(578)	(9,266)
Goodwill and intangible impairment					(5,187)
Interest expense					(110)
Gain on termination of distribution agreements		1,192		1,192	1,192
Income (loss) from discontinued operations, net of tax of \$0 for all periods presented	(168)	1,263	(504)	904	(11,812)

The approximately \$0.9 million present value of the estimated \$1.0 million of minimum royalty payments the Company will receive over the next three years ending September 30, 2015 arising from the termination and settlement agreement and the recognition of approximately \$0.3 million associated with a \$0.3 million product returns provision liability for which an offsetting asset has been recorded based on our rights under the termination and settlement agreement result in a \$1.2 million gain on termination of the distribution agreements for the three and nine months ended September 30, 2012.

The assets and liabilities associated with product promotion and sale have been classified within assets and liabilities of discontinued operations in the accompanying consolidated balance sheets:

	December 31, 2011 (Unaudited)	September 30, 2012 (Unaudited)
Current assets of discontinued operations:		
Inventory	\$ 182	\$ 423
Short term portion of minimum royalty arrangement receivable, net		336
Returns indemnification receivable		122
Accounts receivable	131	
Total current assets of discontinued operations	313	881

Long-term assets of discontinued operations:

Long-term portion of minimum royalty arrangement receivable, net

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	December 31, 2011 (Unaudited)	September 30, 2012 (Unaudited)
Total assets of discontinued operations	313	1,314
Current liabilities of discontinued operations:		
Accounts payable	\$ 46	\$
Returns provision	202	336
Accrued liabilities and other current liabilities	279	102
Total current liabilities of discontinued operations	\$ 527	\$ 438

4. FAIR VALUE MEASUREMENTS

As defined in ASC 820, *Fair Value Measurements and Disclosures* (ASC 820), fair value is based on the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In order to increase consistency and comparability in fair value measurements, ASC 820 establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into three broad levels, which are described below:

- Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs.
- Level 2: Inputs other than quoted prices within Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3: Unobservable inputs that are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible as well as considers counterparty credit risk in its assessment of fair value.

The fair value of the Company's financial assets and liabilities that are measured on a recurring basis were determined using the following inputs as of December 31, 2011:

	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
ASSETS				
Cash equivalents	19,894			19,894
Total assets	19,894			19,894
LIABILITIES				

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Other liabilities measured at fair value:		
Warrants liability	51	51
Scottish Enterprise agreement	20	20
Other liabilities measured at fair value	71	71
Total liabilities	71	71

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The fair value of the Company's financial assets and liabilities that are measured on a recurring basis were determined using the following inputs as of September 30, 2012:

	Level 1 \$000	Level 2 \$000	Level 3 \$000	Total \$000
ASSETS				
Cash equivalents		14,592		
Total assets		14,592		
LIABILITIES				
Economic rights			1,070	1,070
Other liabilities measured at fair value:				
Warrants liability				
Scottish Enterprise agreement			20	20
Other liabilities measured at fair value			20	20
Total liabilities			1,090	1,090

The following table reconciles the beginning and ending balances of Level 3 inputs for the nine months ended September 30, 2012:

	Level 3 \$000
Balance as of December 31, 2011	71
Sale of Economic Rights	1,097
Change in valuation of Economic Rights	(27)
Change in valuation of warrants liability	(51)
Balance as of September 30, 2012	1,090

Economic Rights

On March 22, 2012, the Company entered into a financing agreement with certain existing institutional stockholders. Under the terms of the agreement, investors received contractual rights to receive cash equal to 10% of any future litigation settlement related to the specified intellectual property, subject to a cap. In certain defined situations, the Company may have to issue either additional common shares or warrants (Collectively, the Economic Rights).

The Economic Rights are accounted for as a derivative financial instrument under ASC 815, *Derivative financial instruments* (ASC 815), and are measured at fair value. Changes in fair value are recognized in earnings. The fair value of the Economic Rights has been estimated using a decision-tree analysis method. This is an income-based method that incorporates the expected benefits, costs and probabilities of contingent outcomes under varying scenarios. Each scenario within the decision-tree is discounted to the present value using the company's credit adjusted risk-free rate and ascribed a weighted probability to determine the fair value.

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The Company has concluded the fair value of this liability was approximately \$1.1 million as of September 30, 2012, respectively. The fair value of the Economic Rights increased approximately \$63,000 million and decreased \$27,000 for the three months and nine months ended September 30, 2012, respectively. Decreases and increases in the valuation of Economic Rights are recognized in the consolidated statement of operations as gains and losses, respectively.

The most significant inputs in estimating the fair value of this liability are:

- (i) The Company's credit adjusted risk-free rate, which has been derived from the observable returns on debt for more developed pharmaceuticals companies, adjusted for the Company's risk profile.

- (ii) The amount of the return to the investors, which will vary depending on:
 - a. The outcome of the litigation, including consideration of whether the litigation may be resolved in a jury trial or settled out of court;
 - b. The amount of the settlement or award, which the Company has estimated predominantly based on observable royalty rates arising from the settlement of other cases of intellectual property litigation; and
 - c. The form of the settlement or award.

- (iii) The projected timing of the cash flows to the investors, which could vary between several months to several years depending upon whether the litigation is settled, when the court may decide the case, whether any appeal is made on any court decision and the form of any settlement or award.

- (iv) The number of contingent warrants that could be issued, which is based on a formula.

The decision-tree analysis model used to calculate the fair value of the derivative requires the probability of alternative scenarios to be determined at a series of decision points. Each scenario may contain more than one decision point resulting in further scenarios. Therefore, the probability estimates made by management at each decision point are a significant input to the valuation model.

All of these inputs are unobservable inputs, which have an interrelated effect on the fair value of the derivative. It is not possible to evaluate the impact on the fair value of each factor in combination. However, generally the fair value of the derivative liability will increase, (i) the higher the value of the expected settlement or award, (ii) the lower the discount rate employed and (iii) the more likely it is that a settlement or award will be made. The fair value of the derivative liability will decrease if the timing of settlement is delayed, the expected settlement decreases, or anticipated litigation costs increase. The impact on the fair value of the derivative liability related to the probability of whether the litigation is settled prior to the court hearing or whether a settlement award is made by the court and the form of the settlement will depend on the other

factors above and cannot be estimated in isolation.

The decision-tree analysis model has been performed by valuation specialists, based on inputs provided by the Company and other sources. At each reporting period, the inputs to the model will be evaluated to determine whether any adjustments are appropriate, and to reflect changes in the time value of the expected cash flows.

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The Company used the following assumptions to calculate the value of the Economic Rights:

	March 22, 2012		September 30, 2012	
Probability of unsuccessful/successful outcomes	25% - 75%		25% - 75%	
Amount of award or settlement (1)	\$10.0 million - \$20.0 million		\$10.0 million - \$20.0 million	
Discount rate	16%		16%	
Timing of cash flows	0.75	2.27 years	0.25	1.77 years
Royalty rate	6%		6%	
Litigation expenses	\$1.0 million	\$3.0 million	\$1.0 million	\$3.0 million

(1) Assumptions take into consideration the cap on the amount that the Company would have to pay investors in the event of an award or settlement.

Other Liabilities Measured at Fair ValueWarrants Liability

The Company issued warrants to purchase shares of common stock under the registered direct financing completed in February 2007. These warrants are being accounted for as a liability in accordance with ASC 815. At the date of the transaction, the fair value of the warrants of \$6.8 million was determined utilizing the Black-Scholes option pricing model utilizing the following assumptions: risk free interest rate 4.68%, expected volatility 85%, expected dividend yield 0%, and a remaining contractual life of 7 years. As of September 30, 2012, the fair value of the warrants is nil based on the high exercise price of the warrants relative to the Company's stock price at September 30, 2012 and the term of 1.38 years. The fair value of the warrant is remeasured each reporting period, with a gain or loss recognized in the consolidated statement of operations. Such gains or losses will continue to be reported until the warrants are exercised or expired. The Company used the Black-Scholes option-pricing model to value the warrants.

The Company recognized the change in the value of warrants as a gain on the consolidated statement of operations of \$0.4 million and approximately \$1,000 for the three months ended September 30, 2011 and 2012, respectively. The Company recognized a gain of \$0.6 million and approximately \$51,000 for the nine months ended September 30, 2011 and 2012, respectively.

Scottish Enterprise Agreement

On June 22, 2009, the Company amended the Agreement with Scottish Enterprise ("SE") (the "Amendment"), in order to allow the Company to implement a reduction of the Company's research operations located in Scotland in exchange for the parties' agreement to modify the payment terms of the Agreement in the principal amount of £5 million (approximately \$8.0 million at December 31, 2009), which SE had previously entered into with the Company. The Agreement provided for repayment of up to £5 million in the event the Company significantly reduced its Scottish research operations. Pursuant to the terms of the Amendment, in association with Cyclacel's material reduction in staff at its Scottish

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research facility, the parties agreed to a modified payment of £1 million (approximately \$1.7 million at June 22, 2009) payable in two equal tranches. On July 1, 2009, the first installment of £0.5 million (approximately \$0.8 million) was paid and the remaining amount of £0.5 million (approximately \$0.8 million) was paid on January 6, 2010. In addition, should a further reduction below current minimum staff levels be effectuated before July 2014 without SE's prior consent, the Company may be obligated to pay up to £4 million to SE, which will be calculated as a maximum of £4 million (approximately \$6.2 million at December 31, 2011 and \$6.5 million at September 30, 2012) less the market value of the shares held by SE at the time staffing levels in Scotland fall below the prescribed minimum levels. If the Company were to have reduced staffing levels below the prescribed levels, the amount potentially payable to SE would have been approximately

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£3.8 million (approximately \$5.9 million) and approximately £3.8 million (approximately \$6.2 million) at December 31, 2011 and September 30, 2012, respectively.

This arrangement is accounted for as a liability under ASC Topic 480, *Distinguishing Liabilities from Equity* (ASC 480), and is measured at fair value. Changes in fair value are recognized in earnings. Due to the nature of the associated contingency and the likelihood of occurrence, the Company has concluded the fair value of this liability was approximately \$20,000 at December 31, 2011 and September 30, 2012, respectively. The most significant inputs in estimating the fair value of this liability are the probabilities that staffing levels fall below the prescribed minimum and that the Company is unable or unwilling to replace such employees within the prescribed time period. At both December 31, 2011 and September 30, 2012, the Company used a scenario analysis model to arrive at the fair value of the Scottish Enterprise Agreement and assumed a 30% probability of falling below a minimum staffing level and a 1% probability that the occurrence of such an event would not be cured within the prescribed time period. At each reporting period, the inputs used to determine the fair value of the liability will be evaluated to determine whether adjustments are appropriate. Changes in the value of this liability are recorded in the consolidated statement of operations.

5. PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets consist of the following:

	December 31, 2011	September 30, 2012
	(\$000s)	
Research and development tax credit receivable	541	732
Prepayments	317	318
Other current assets	211	185
Total prepaid expenses and other current assets	1,069	1,235

6. ACCRUED LIABILITIES AND OTHER CURRENT LIABILITIES

Accrued and other current liabilities consisted of the following:

	December 31, 2011	September 30, 2012
	(\$000s)	
Accrued research and development.	3,621	3,335
Other current liabilities	562	792
	4,183	4,127

During the nine months ended September 30, 2012, the Company recorded out of period reversals of pre-clinical expense accruals of \$0.4 million as a decrease to accrued liabilities and other current liabilities on the consolidated balance sheets and as a decrease to research and development expenses on the consolidated statements of operations.

7. STOCK BASED COMPENSATION

All share and per share information presented gives effect to the reverse stock split, which occurred on August 24, 2012.

Stock based compensation has been in the consolidated statement of operations for the three and six months ended September 30, 2011 and 2012 as shown in the following table:

	For the three months ended September 30,		For the nine months ended September 30,	
	2011	2012	2011	2012
	(\$000s)			
Research and development	39	16	130	49
General and administrative	171	59	515	202
Income (loss) from discontinued operations, net of tax	11	1	32	36
Stock-based compensation costs before income taxes	221	76	677	287

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At the Company's annual shareholder meeting on May 23, 2012, the stockholders approved and amended the number of shares reserved under the 2006 Plan to 10,000,000 shares of the Company's common stock, up from 5,200,000 shares. Stock option awards granted under the 2006 Plan have a maximum life of 10 years and generally vest over a four-year period from the date of grant.

A summary of activity for the options under the Company's 2006 Plan for the nine months ended September 30, 2012 is as follows:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (years)	Aggregate Intrinsic Value (\$000s)
Options outstanding at December 31, 2011	502,253	\$ 26.11	6.44	140
Granted	33,571			