

Adamas Pharmaceuticals Inc
Form 10-Q
May 13, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2015

or

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

For the transition period from to

Commission File No. 001-36399

ADAMAS PHARMACEUTICALS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

42-1560076
(I.R.S. Employer
Identification Number)

1900 Powell Street, Suite 750
Emeryville, CA
(Address of Principal Executive Offices)

94608
(Zip Code)

(510) 450-3500

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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
(Do not check if a
smaller reporting
company)

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

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Number of shares outstanding of the issuer's common stock, par value \$0.001 per share, as of May 6, 2015 was 17,823,046.

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ADAMAS PHARMACEUTICALS, INC.

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In this report, unless otherwise stated or the context otherwise indicates, references to the company, Adamas, we, us and our refer to Adamas Pharmaceuticals, Inc.

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****ADAMAS PHARMACEUTICALS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except share and per share data)

	March 31, 2015 (unaudited)	December 31, 2014
Assets		
Current assets		
Cash and cash equivalents	\$ 29,228	\$ 61,446
Marketable securities, current	85,263	60,912
Accounts receivable	485	524
Prepaid expenses and other current assets	540	645
Total current assets	115,516	123,527
Property and equipment, net	1,294	1,228
Marketable securities, non-current	30,495	36,364
Other assets	38	70
Total assets	\$ 147,343	\$ 161,189
Liabilities and stockholders equity		
Current liabilities		
Accounts payable	\$ 3,806	\$ 3,685
Accrued liabilities	4,161	8,595
Other current liabilities	138	265
Total current liabilities	8,105	12,545
Non-current liabilities	1,685	1,570
Total liabilities	9,790	14,115
Commitments and Contingencies (Note 7)		
Stockholders equity		
Common stock, \$0.001 par value - 100,000,000 shares authorized, 17,727,226 and 17,551,375 shares issued and outstanding at March 31, 2015 and December 31, 2014, respectively	22	22
Additional paid-in capital	160,135	157,581
Accumulated other comprehensive income (loss)	(53)	(180)
Accumulated deficit	(22,551)	(10,349)
Total stockholders equity	137,553	147,074
Total liabilities and stockholders equity	\$ 147,343	\$ 161,189

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

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ADAMAS PHARMACEUTICALS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

(in thousands except per share data)

	Three Months Ended March 31,	
	2015	2014
Revenue	\$ 226	\$ 176
Operating expenses		
Research and development	7,533	2,758
General and administrative	4,919	3,109
Total operating expenses	12,452	5,867
Loss from operations	(12,226)	(5,691)
Interest and other income (expense), net	78	(688)
Loss before income taxes	(12,148)	(6,379)
Income tax expense	(54)	(1)
Net loss	\$ (12,202)	\$ (6,380)
Net loss per share attributable to common stockholders:		
Basic	\$ (0.69)	\$ (0.67)
Diluted	\$ (0.69)	\$ (0.67)
Weighted average number of shares used in computing net loss attributable to common stockholders:		
Basic	17,643	9,525
Diluted	17,643	9,525

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

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ADAMAS PHARMACEUTICALS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(unaudited)

(in thousands)

	Three Months Ended		
	March 31,		
	2015		2014
Net loss	\$	(12,202)	\$ (6,380)
Unrealized gain on available-for-sale securities		127	
Comprehensive loss	\$	(12,075)	\$ (6,380)

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

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ADAMAS PHARMACUETICALS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(in thousands)

	Three Months Ended March 31,	
	2015	2014
Cash flows from operating activities		
Net loss	\$ (12,202)	\$ (6,380)
Adjustments to reconcile net loss to net cash provided by operating activities		
Depreciation and amortization	70	22
Stock-based compensation	2,142	1,047
Change in preferred stock warrant value		664
Net accretion of discounts and amortization of premiums of marketable securities	194	
Changes in assets and liabilities		
Accrued interest of marketable securities	(114)	
Prepaid expenses and other assets	138	(275)
Accounts receivable	39	(122)
Accounts payable	2	(2,052)
Accrued liabilities and other liabilities	(4,334)	311
Net cash used in operating activities	(14,065)	(6,785)
Cash flows from investing activities		
Purchases of property and equipment	(18)	(77)
Purchases of investments	(18,435)	
Net cash used in investing activities	(18,453)	(77)
Cash flows from financing activities		
Proceeds from issuance of common stock upon exercise of stock options	300	36
Proceeds from issuance of common and preferred stock upon exercise of warrants		1,013
Net cash provided by financing activities	300	1,049
Net decrease in cash and cash equivalents	(32,218)	(5,813)
Cash and cash equivalents at beginning of period	61,446	85,612
Cash and cash equivalents at end of period	\$ 29,228	\$ 79,799
Supplemental disclosure		
Cash paid for income taxes	\$ 4,691	\$
Accrued deferred offering costs	\$	\$ 1,940

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

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ADAMAS PHARMACEUTICALS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. THE COMPANY

Adamas Pharmaceuticals, Inc. (the Company) is a specialty pharmaceutical company focused on the development and commercialization of therapeutics targeting chronic disorders of the central nervous systems (CNS). The Company achieves this by enhancing the pharmacokinetic profiles of approved drugs to create novel therapeutics for use alone and in fixed-dose combination products. The Company's business strategy is twofold. The Company intends to develop and commercialize its wholly owned products directly. In addition, the Company may form partnerships with companies that have an already established CNS market presence. The Company is developing its lead wholly owned product candidate, ADS-5102, for a complication associated with the treatment of Parkinson's disease known as levodopa induced dyskinesia, or LID, and potentially as a treatment for one or more additional CNS indications. The Company successfully completed a Phase 2/3 clinical study in LID in 2013 and has initiated two Phase 3 registration trials and a separate open-label safety study in 2014 in support of the LID indication. Its late-stage therapeutics portfolio includes an approved product, Namenda XR® which Forest Laboratories, Inc. (Forest), a subsidiary of Actavis plc, developed and is responsible for marketing in the United States under a license from the Company and also includes a recently approved product, Namzaric™ (formerly MDX-8704), co-developed with Forest, which is expected to launch in the second quarter of 2015.

The Company was incorporated in the State of Delaware on November 15, 2000. The Company's headquarters and operations are located in Emeryville, California. The Company has four insignificant subsidiaries.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. The financial statements include all adjustments (consisting only of normal recurring adjustments) that we believe are necessary for a fair presentation of the periods presented. The condensed consolidated balance sheet at December 31, 2014 was derived from the audited consolidated financial statements, but does not include all disclosures required by GAAP. These interim financial results are not necessarily indicative of results to be expected for the full fiscal year or any other future period and should be read in conjunction with the audited consolidated financial statements and the related notes thereto for the year ended December 31, 2014, included in our Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission, or SEC.

Liquidity and Financial Condition

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To date, nearly all of the Company's resources have been dedicated to the research and development of its products, and the Company has not generated any commercial revenue from the sale of its products. The Company does not anticipate the generation of any commercial product revenue until it receives the necessary regulatory approvals to launch one of its products.

Based upon the current status of, and plans for, its product development, the Company believes that the existing cash, cash equivalents and marketable securities of \$145.0 million as of March 31, 2015 will be adequate to satisfy the Company's capital needs through at least the next twelve months. However, the process of developing and commercializing products requires significant research and development, preclinical testing and clinical trials, manufacturing arrangements, as well as regulatory approvals. These activities, together with the Company's general and administrative expenses, are expected to result in significant operating losses until the commercialization of the Company's products or partner collaborations generate sufficient revenue to cover expenses. While the Company had net income during 2014, it has not generated any commercial revenue from sales of its products. Under its license agreement with Forest, the Company received the final milestone payment in 2014, and is not entitled to receive any royalties for sales of Namenda XR and Namzaric until mid-2018 for sales of Namenda XR and five years after the launch of Namzaric. To achieve sustained profitability, the Company, alone or with others, must successfully develop its product candidates, obtain required regulatory approvals, and successfully manufacture and market its products.

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Use of Estimates

The preparation of the accompanying consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses in the consolidated financial statements and the accompanying notes. On an ongoing basis, management evaluates its estimates, including those related to revenue recognition, clinical trial accruals, fair value of assets and liabilities, income taxes, and stock-based compensation. Management bases its estimates on historical experience and on various other market-specific and relevant assumptions that management believes to be reasonable under the circumstances. Actual results may differ from those estimates.

Forward Stock Split

In March 2014, the Board of Directors of the Company and stockholders approved a forward stock split of the Company's common and preferred stock. As a result, common and preferred stock, stock options and warrants to purchase common and preferred stock were adjusted in the ratio of 2:1, effective March 24, 2014. All common and per share amounts presented in these condensed consolidated financial statements for all periods have been retroactively adjusted to reflect the 2-for-1 forward stock split. No fractional shares were issued.

Revenue Recognition

The Company recognizes revenue when all four of the following criteria have been met: (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred or services have been rendered, (iii) the fee is fixed or determinable and (iv) collectability is reasonably assured. Revenue under license and collaboration arrangements is recognized based on the performance requirements of the contract. Determinations of whether persuasive evidence of an arrangement exists and whether delivery has occurred or services have been rendered are based on management's judgments regarding the fixed nature of the fees charged for deliverables and the collectability of those fees. Should changes in conditions cause management to determine that these criteria are not met for any new or modified transactions, revenue recognized could be adversely affected.

The Company generates revenue from collaboration and license agreements for the development and commercialization of products. Collaboration and license agreements may include non-refundable upfront license fees, partial or complete reimbursement of research and development costs, contingent consideration payments based on the achievement of defined collaboration objectives and royalties on sales of commercialized products. The Company's performance obligations under the collaborations may include the license or transfer of intellectual property rights, obligations to provide research and development services and related materials and obligations to participate on certain development and/or commercialization committees with the collaborators.

On January 1, 2011, the Company adopted an accounting standards update that amends the guidance on accounting for new arrangements, or those materially modified, with multiple deliverables. This guidance eliminates the requirement for objective and reliable evidence of fair value of the undelivered items in order to consider a deliverable a separate unit of accounting. It also changes the allocation method such that the relative-selling-price method must be used to allocate arrangement consideration to the units of accounting in an arrangement. This guidance establishes the following estimation hierarchy that must be used in estimating selling price under the relative-selling-price method: (i) vendor-specific objective evidence of fair value of the deliverable, if it exists, (ii) third-party evidence of selling price, if vendor-specific

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objective evidence is not available or (iii) vendor's best estimate of selling price, if neither vendor-specific nor third-party evidence is available.

On January 1, 2011, the Company adopted an accounting standards update that provides guidance on revenue recognition using the milestone method. Payments that are contingent upon achievement of a substantive milestone are recognized in their entirety in the period in which the milestone is achieved. Milestones are defined as events that can only be achieved based on the Company's performance and there is substantive uncertainty about whether the event will be achieved at the inception of the arrangement. Events that are contingent only on the passage of time or only on counterparty performance are not considered milestones subject to this guidance. Further, the amounts received must relate solely to prior performance, be reasonable relative to all of the deliverables and payment terms within the agreement and commensurate with the Company's performance to achieve the milestone after commencement of the agreement.

Amounts related to research and development funding are recognized as the related services or activities are performed, in accordance with the contract terms. Payments may be made to or by the Company based on the number of full-time equivalent researchers assigned to the collaboration project and the related research and development expenses incurred.

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Clinical Trial Accruals

The Company's clinical trial accruals are based on estimates of patient enrollment and related costs at clinical investigator sites, as well as estimates for the services received and efforts expended pursuant to contracts with multiple research institutions and clinical research organizations (CROs) that conduct and manage clinical trials on the Company's behalf.

The Company estimates clinical trial expenses based on the services performed pursuant to contracts with research institutions and clinical research organizations that conduct and manage clinical trials on its behalf. In accruing service fees, the Company obtains the reported level of patient enrollment at each site and estimates the time period over which services will be performed and activity expended in each period. If the actual timing of the performance of services or the level of effort varies from the estimate, the Company will adjust the accrual accordingly. Payments made to third parties under these arrangements in advance of the receipt of the related services are recorded as prepaid expenses until the services are rendered.

Research and Development

Research and development (R&D) expenses include salaries, contractor and consultant fees, external clinical trial expenses performed by contract research organizations (CRO), licensing fees, acquired intellectual property with no alternative future use, and facility and administrative expense allocations. In addition, we fund R&D at research institutions under agreements that are generally cancelable at our option. Research costs typically consist of applied research and preclinical and toxicology work. Pharmaceutical manufacturing development costs consist of product formulation, chemical analysis, and the transfer and scale-up of manufacturing at our contract manufacturers. Clinical development costs include the costs of Phase 1, Phase 2, and Phase 3 clinical trials. These costs are a significant component of our research and development expenses.

We accrue costs for clinical trial activities performed by contract research organizations and other third parties based upon the estimated amount of work completed on each study as provided by the CRO. These estimates are reviewed for reasonableness by our internal clinical personnel, and we aim to match the accrual to actual services performed by the organizations as determined by patient enrollment levels and related activities. We monitor patient enrollment levels and related activities using available information; however, if we underestimate activity levels associated with various studies at a given point in time, we could be required to record significant additional R&D expenses in future periods when the actual activity level becomes known. We charge all such costs to R&D expenses. Non-refundable advance payments are capitalized and expensed as the related goods are delivered or services are performed.

Basic and Diluted Net Income Per Share Attributable to Common Stockholders

Basic net income per share attributable to common stockholders is based upon the weighted average number of common shares outstanding during the period. Diluted net income per share attributable to common stockholders is based upon the weighted average number of common shares outstanding and dilutive common stock equivalents outstanding during the period. Common stock equivalents are options granted under our stock awards plans and are calculated under the treasury stock method. Common equivalent shares from unexercised stock options and convertible preferred stock warrants are excluded from the computation when there is a loss as their effect is anti-dilutive, or if the exercise price of such options is greater than the average market price of the stock for the period.

Prior to April 10, 2014, the Company calculated its basic and diluted net income (loss) per share attributable to common stockholders in conformity with the two-class method required for companies with participating securities. Under the two-class method, the Company determined whether it had net income attributable to common stockholders, which includes the results of operations less current period convertible preferred stock non-cumulative dividends. If it was determined that the Company had net income attributable to common stockholders during a period, the related undistributed earnings were then allocated between common stock and the convertible preferred stock based on the weighted average number of shares outstanding during the period to determine the numerator for the basic net income per share attributable to common stockholders. In computing diluted net income attributable to common stockholders, undistributed earnings are re-allocated to reflect the potential impact of dilutive securities to determine the numerator for the diluted net income per share attributable to common stockholders.

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Stock-Based Compensation

The Company accounts for stock-based compensation of stock options granted to employees and directors and for employee stock purchase plan shares by estimating the fair value of stock-based awards using the Black-Scholes option-pricing model and amortizing the fair value of the stock-based awards granted over the applicable vesting period. All stock options awards to non-employees are accounted for at the fair value of the consideration received or the fair value of the equity instrument issued, as calculated using the Black-Scholes model. The measurement of nonemployee stock-based compensation is subject to periodic adjustment as the underlying equity instruments vest.

In order to estimate the value of share-based awards, the Company uses the Black-Scholes model, which requires the use of certain subjective assumptions. The most significant subjective assumptions are management's estimates of the expected volatility and the expected term of the award. In addition, judgment is also required in estimating the amount of share-based awards that are expected to be forfeited. If actual results differ significantly from any of these estimates, stock-based compensation expense and the Company's results of operations could be materially impacted.

Recent Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers*. The amendment in this ASU provides guidance on the revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The core principle of this update provides guidance to identify the performance obligations under the contract(s) with a customer and how to allocate the transaction price to the performance obligations in the contract. It further provides guidance to recognize revenue when (or as) the entity satisfies a performance obligation. This standard will replace most existing revenue recognition guidance when it becomes effective January 1, 2017. Early adoption is not permitted. We have not yet selected a transition method nor have we determined the effect of the standard on our consolidated financial position and results of operations.

3. FAIR VALUE MEASUREMENTS

In accordance with ASC 820-10, *Fair Value Measurements and Disclosures*, the Company determines the fair value of financial and non-financial assets and liabilities using the fair value hierarchy, which establishes three levels of inputs that may be used to measure fair value, as follows:

- Level 1 inputs which include quoted prices in active markets for identical assets or liabilities;

- Level 2 inputs which include observable inputs other than Level 1 inputs, such as quoted prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability. For available-for-sale securities, the Company reviews trading

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activity and pricing as of the measurement date. When sufficient quoted pricing for identical securities is not available, the Company uses market pricing and other observable market inputs for similar securities obtained from various third-party data providers. These inputs either represent quoted prices for similar assets in active markets or have been derived from observable market data; and

- Level 3 inputs which include unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the underlying asset or liability. Level 3 assets and liabilities include those whose fair value measurements are determined using pricing models, discounted cash flow methodologies or similar valuation techniques, as well as significant management judgment or estimation.

The following table represents the fair value hierarchy for the Company's financial assets and liabilities which require fair value measurement on a recurring basis (in thousands):

	Total	Fair Value Measurements at March 31, 2015		
		Level 1	Level 2	Level 3
Assets				
Money market	\$ 27,054	\$ 27,054		\$
Corporate debt	96,953		96,953	
U.S. Treasury notes	14,811		14,811	
Commercial paper	3,993		3,993	
Total	\$ 142,811	\$ 27,054	\$ 115,757	\$

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	Total	Fair Value Measurements at December 31, 2014		Level 3
		Level 1	Level 2	
Assets				
Money market	\$ 59,303	\$ 59,303	\$	\$
Corporate debt	85,311		85,311	
U.S. Treasury notes	11,965		11,965	
Total	\$ 156,579	\$ 59,303	\$ 97,276	\$

Money market funds are highly liquid investments and are actively traded. The pricing information on these investment instruments are readily available and can be independently validated as of the measurement date. This approach results in the classification of these securities as Level 1 of the fair value hierarchy.

Corporate debt and U.S. Treasury notes are measured at fair value using level 2 inputs. We review trading activity and pricing for these investments as of each measurement date. When sufficient quoted pricing for identical securities is not available, we use market pricing and other observable market inputs for similar securities obtained from various third party data providers. These inputs represent quoted prices for similar assets in active markets or these inputs have been derived from observable market data. This approach results in the classification of these securities as Level 2 of the fair value hierarchy.

There were no transfers between Level 1 and Level 2 during the three months ended March 31, 2015.

4. INVESTMENTS

The Company's investments consist of corporate debt and U.S. Treasury notes classified as available-for-sale securities.

The Company limits the amount of investment exposure as to institution, maturity, and investment type. To mitigate credit risk, the Company invests in investment grade corporate debt and United States treasury notes. Such securities are reported at fair value, with unrealized gains and losses excluded from earnings and shown separately as a component of accumulated other comprehensive income (loss) within stockholders equity. The Company may pay a premium or receive a discount upon the purchase of marketable securities. Interest earned and gains realized on marketable securities and amortization of discounts received and accretion of premiums paid on the purchase of marketable securities are included in investment income.

The following table is a summary of amortized cost, unrealized gain and loss, and the fair value of available-for-sale investments (in thousands):

	March 31, 2015			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	

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Investments:								
Corporate debt	\$	97,024	\$	12	\$	(83)	\$	96,953
U.S. Treasury notes		14,793		18				14,811
Commercial paper		3,993						3,993
	\$	115,810	\$	30	\$	(83)	\$	115,757
Reported as:								
Short-term investments	\$	85,308	\$	12	\$	(59)	\$	85,261
Long-term investments		30,502		18		(24)		30,496
Total	\$	115,810	\$	30	\$	(83)	\$	115,757

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	December 31, 2014			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Investments:				
Corporate debt	\$ 85,474	\$	\$ (163)	\$ 85,311
U.S. Treasury notes	11,982		(17)	11,965
	\$ 97,456	\$	\$ (180)	\$ 97,276
Reported as:				
Short-term investments	\$ 61,014	\$	\$ (104)	\$ 60,910
Long-term investments	36,442		(76)	36,366
Total	\$ 97,456	\$	\$ (180)	\$ 97,276

Short-term and long-term investments includes accrued interest of \$392,000 and \$241,000, respectively, as of March 31, 2015. Short-term and long-term investments includes accrued interest of \$309,000 and \$209,000, respectively, as of December 31, 2014. The Company has not incurred any realized gains or losses on investments for the three months ended March 31, 2015 and 2014. Investments are classified as short-term or long-term depending on the underlying investment's maturity date. Long-term investments have a maturity date range of greater than 12 months and a maximum of 22 months as of March 31, 2015.

5. COLLABORATION AND LICENSE AGREEMENTS

In November 2012, the Company granted Forest an exclusive license, with right to sublicense, certain of the Company's intellectual property rights relating to human therapeutics containing memantine in the United States. In connection with these rights, Forest markets Namenda XR and is expected to launch Namzaric in the second quarter of 2015 for the treatment of moderate to severe dementia related to Alzheimer's disease. Pursuant to the agreement, Forest made an upfront payment of \$65.0 million. The Company earned and received additional cash payments totaling \$95.0 million upon achievement by Forest of certain development and regulatory milestones. In addition, the Company may earn tiered royalty payments based on future net sales of Namenda XR and Namzaric.

The Company identified the following two non-contingent performance deliverables under the license agreement: (i) transfer of intellectual property rights, inclusive of the related technology know-how conveyance (license and know-how or license) and (ii) the obligation to participate on the Joint Development Committee (JDC). The Company concluded that the license and the know-how together represent a single deliverable, and therefore the two together have been accounted for as a single unit of accounting. There was no separate consideration identified in the agreement for the deliverables and there was no right of return under the agreement. The Company considered the provisions of the multiple-element arrangement guidance in determining whether the deliverables outlined above have standalone value. The transfer of license and know-how has standalone value separate from the obligation to participate on the JDC, as the agreement allows Forest to sublicense its rights to the acquired license to a third party. Further, the Company believes that Forest has research and development expertise with compounds similar to those licensed under the agreement and has the ability to engage other third parties to develop these compounds, allowing Forest to realize the value of the license and know-how without receiving the JDC participation.

The Company developed its best estimates of selling prices (BESP) for each deliverable in order to allocate the non-contingent arrangement consideration to the two units of accounting. Based on BESP analysis, value assigned to the obligation to participate on the JDC was a negligible amount. Accordingly, the entire upfront license fee of \$65.0 million was allocated to the transfer of license and technical know-how. Revenue recognition commenced upon delivery of the license and was recognized on a straight-line basis through the period of the transfer of the know-how. Forest was able to derive value from the license as the know-how was transferred. A straight-line pattern of revenue recognition is only acceptable when a more precise pattern cannot be discerned. The way in which the transfer of know-how occurred did not give rise to a

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more precise pattern of recognition, and the Company therefore recognized revenue on a straight-line basis over the period of the transfer of the know-how (from November 2012 to February 2013).

In November and December 2013, the Company received a total of \$40.0 million in milestone payments under its license agreement with Forest. The milestone payments were for the successful completion of studies that support the

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planned New Drug Application (NDA) filing with the FDA for Namzaric by Forest. In May 2014, the Company received an additional \$25.0 million milestone payment under the license agreement. This milestone payment was a result of the FDA s acceptance of the NDA for Namzaric. In December 2014, the Company received a final \$30.0 million milestone payment in connection with the FDA approval of Namzaric. These amounts have been recorded as revenue when received in the consolidated statements of operations and comprehensive income during 2013 and 2014, respectively.

Commencing in June 2018, the Company is entitled to receive low to mid-single digit royalties on net sales in the United States by Forest, its affiliates, or any of its sublicensees of controlled-release versions of memantine, such as Namenda XR, or any other product covered by the terms of the license agreement. Forest s obligation to pay royalties with respect to controlled-release versions of memantine covered by the agreement continue until the expiration of the Orange Book listed patents covering such products. In addition, commencing five years after the initial launch of a fixed-dose memantine-donepezil product in the United States, such as Namzaric, which Forest expects to launch in the second quarter of 2015, the Company is entitled to receive royalties at rates ranging from the low double digits to the mid-teens on the net sales by Forest, its affiliates, and any sublicensees of such products in the United States. Forest s obligation to pay royalties with respect to fixed-dose memantine-donepezil products continues until the later of (i) 15 years after the commercial launch of the first fixed-dose memantine-donepezil product by Forest in the United States or (ii) the expiration of the Orange Book listed patents for which Forest obtained rights from us covering such product. However, Forest s obligation to pay royalties for any product covered by the license is eliminated in any quarter where there is significant competition from generics.

6. WARRANTS TO PURCHASE COMMON STOCK

In conjunction with various financings between 2002 and 2012, the Company issued warrants to purchase 751,878 shares of convertible preferred stock and 127,780 shares of common stock. The relative fair value of these warrants was determined using the Black-Scholes model and was amortized to interest expense over the term of each loan, unless subsequently modified. As of both March 31, 2015 and December 31, 2014, warrants to purchase 7,116 shares of common stock were outstanding and zero warrants to purchase convertible preferred stock were outstanding, respectively.

Prior to the IPO in April 2014, the warrants were classified as a liability and remeasured to fair value each reporting period. The Company had estimated the fair value of these liabilities using the Black-Scholes model and assumptions that were based on the individual characteristics of the warrants on the valuation date, as well as the assumptions for expected volatility, expected life, dividends, and risk-free interest rate. Immediately prior to the completion of the Company s IPO in 2014, all of the warrants were either exercised for cash or automatically net exercised for a total issuance of 199,837 shares of common stock, pursuant to the terms of the warrants. Just prior to the exercises, all of the outstanding warrants, covering 220,004 shares, were remeasured using the intrinsic value of the warrant computed as the difference between the \$16.00 per share IPO price and the \$3.80 per share exercise price of the warrant. The remeasurement of the fair value of these warrants from December 31, 2013 through the date of the conversion to a common stock warrant and following the exercise resulted in a \$1.0 million expense recorded to other income (expense), net in the Company s consolidated statements of operations and comprehensive income. The resulting fair value of approximately \$27.9 million was reclassified as additional paid-in capital upon completion of the IPO.

The following table summarizes the outstanding warrants as of:

Number of Shares Outstanding	
March 31, 2015	December 31, 2014

Common stock warrants	7,116	7,116
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7. COMMITMENTS AND CONTINGENCIES

Lease Commitments

The Company leases approximately 12,500 square feet of office space in Emeryville, California. In May 2014, the Company amended its corporate lease agreement to increase the square footage leased from approximately 12,500 to approximately 18,500 square feet for an additional term of 65 months through April 30, 2020. The Company plans to take occupancy of the additional space by the end of the second quarter of 2015.

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As of March 31, 2015, future minimum lease payments under a non-cancelable facility operating lease including related office equipment were as follows (in thousands):

	March 31,	
	2015	
2015	\$	422
2016		624
2017		624
2018		634
2019		654
Thereafter		223
Total	\$	3,181

The Company's total rent expense for the three months ended March 31, 2015 and 2014 was approximately \$142,000 and \$58,000, respectively.

Contingencies

In the normal course of business, the Company enters into contracts and agreements that contain a variety of representations and warranties and provide for general indemnifications. The Company's exposure under these agreements is unknown, because it involves claims that may be made against the Company in the future, but have not yet been made. The Company accrues a liability for such matters when it is probable that future expenditures will be made and such expenditures can be reasonably estimated.

Indemnification

In accordance with the Company's amended and restated certificate of incorporation and amended and restated bylaws, the Company has indemnification obligations to its officers and directors for certain events or occurrences, subject to certain limits, while they are serving in such capacity. There have been no claims to date, and the Company has a directors and officers liability insurance policy that may enable it to recover a portion of any amounts paid for future claims.

Litigation

Several companies have submitted Abbreviated New Drug applications, or ANDAs, to the FDA requesting permission to manufacture and market generic versions of Namenda XR, on which the Company is entitled to receive royalties from Forest beginning in June 2018. In the notices, these companies allege that the patents associated with Namenda XR, some of which are owned by Forest or licensed by Forest from Merz Pharma GmbH & Co. KGaA and others of which are owned by the Company and licensed by the Company exclusively to Forest in the United States, are invalid, unenforceable and/or will not be infringed by the companies' manufacture, use, or sale of generic versions of Namenda XR. In January, February, and April 2014, the Company, Forest, Forest Laboratories Holdings Ltd., Merz Pharma GmbH & Co. KGaA, and Merz Pharmaceuticals GmbH (together Merz) filed lawsuits in the U.S. District Court for the District of Delaware for infringement of the

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relevant patents against all of these companies. The parties are collectively seeking judgment that (i) the defendants have infringed the patents at issue, (ii) the effective date of any approval of the defendants' ANDAs shall not be earlier than the expiration date of the last to expire of the relevant patents, including any extensions or exclusivities, (iii) the defendants be enjoined from commercially manufacturing, using, offering for sale, or selling in the United States, or importing into the United States, any products that infringe or induce or contribute to the infringement of the patents at issue prior to the expiration date of the last to expire of the patents, including extensions and exclusivities, and (iv) the Company, Forest, Forest Laboratories Holdings Ltd., and Merz be awarded monetary relief, in addition to any attorneys' fees, costs, and expenses relating to the actions. The trial is scheduled for February 2016. Because these lawsuits were filed within the requisite 45 day period provided in the U.S. Food, Drug and Cosmetic Act, there are stays preventing FDA approval of the ANDAs for 30 months or until a court decision adverse to the patents. The 30 month stays for these ANDAs will begin to expire in June 2016.

From November 2014 through May 2015, we and Forest have entered into a series of settlement agreements on undisclosed terms.

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From time to time, the Company may be party to legal proceedings, investigations, and claims in the ordinary course of its business. Other than the matters described above, the Company is not presently a party to any material legal proceedings.

8. STOCKHOLDERS EQUITY

Common Stock

The amended and restated certificate of incorporation authorizes the Company to issue 100,000,000 shares of common stock. Common stockholders are entitled to dividends as and when declared by the board of directors, subject to the rights of holders of all classes of stock outstanding having priority rights as to dividends. There have been no dividends declared to date. Each share of common stock is entitled to one vote.

The Company has classified all unvested shares of common stock issued upon the early exercise of stock options as employee deposits (a liability) as these options are not considered to be substantively exercised until vested. At March 31, 2015 and December 31, 2014, 3,000 and 13,000 shares of common stock, respectively, from early exercised options were unvested.

Shares reserved for Future Issuance

Shares of Company's common stock reserved for future issuance are as follows:

March 31, 2015	December 31, 2014
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