

Regulus Therapeutics Inc.
Form S-1
June 26, 2013
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As filed with the Securities and Exchange Commission on June 26, 2013

Registration No. 333-

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

FORM S-1
REGISTRATION STATEMENT
UNDER
THE SECURITIES ACT OF 1933

Regulus Therapeutics Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of

2834
(Primary Standard Industrial

26-4738379
(I.R.S. Employer

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Incorporation or Organization)

Classification Code Number)

Identification Number)

3545 John Hopkins Ct.

Suite 210

San Diego, CA 92121

(858) 202-6300

(Address, Including Zip Code, and Telephone Number, Including Area Code, of Registrant's Principal Executive Offices)

Kleanthis G. Xanthopoulos, Ph.D.

President and Chief Executive Officer

Regulus Therapeutics Inc.

3545 John Hopkins Court

Suite 210

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(858) 202-6300

(Name, Address, Including Zip Code, and Telephone Number, Including Area Code, of Agent for Service)

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Approximate date of commencement of proposed sale to the public:

As soon as practicable after the effective date of this registration statement.

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If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, as amended (the Securities Act), check the following box. "

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. "

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

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

CALCULATION OF REGISTRATION FEE

Title of each class of securities to be registered	Proposed maximum aggregate offering price (1)	Amount of registration fee
Common Stock, \$0.001 par value per share	\$57,500,000	\$7,843.00

(1) Estimated solely for the purpose of calculating the amount of the registration fee in accordance with Rule 457(o) under the Securities Act. Includes the offering price of shares that the underwriters have the option to purchase to cover over-allotments, if any.

The Registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment that specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

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The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and we are not soliciting offers to buy these securities in any jurisdiction where the offer or sale is not permitted.

SUBJECT TO COMPLETION, DATED JUNE 26, 2013

Shares

Common Stock

Regulus Therapeutics Inc. is offering _____ shares of its common stock. Our common stock is listed on The NASDAQ Global Market under the symbol RGLS. On _____, 2013, the last reported sale price of our common stock on The NASDAQ Global Market was \$ _____ per share.

We are an emerging growth company as that term is used in the Jumpstart Our Business Startups Act of 2012 and, as such, have elected to comply with certain reduced public company reporting requirements for this prospectus and future filings.

Investing in our common stock involves substantial risks. See Risk factors beginning on page 12.

PRICE \$ A SHARE

	Per Share	Total
Public offering price	\$	\$
Underwriting discounts and commissions	\$	\$
Proceeds, before expenses, to us	\$	\$

We have granted the underwriters an option for 30 days from the date of this prospectus to purchase up to _____ of additional shares of our common stock to cover over-allotments. If the underwriters exercise the option in full, the total underwriting discounts and commissions payable by us will be \$ _____, and the total proceeds to us, before expenses, will be \$ _____.

The Securities and Exchange Commission and state securities regulators have not approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The underwriters expect to deliver the shares of common stock to purchasers on _____, 2013.

Lazard Capital Markets

Cowen and Company

BMO Capital Markets

Needham & Company

Wedbush PacGrow Life Sciences

The date of this prospectus is _____, 2013

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You should rely only on the information contained in this prospectus and in any free writing prospectus that we may have provided to you in connection with this offering. Neither we nor any of the underwriters has authorized anyone to provide you with information different from, or in addition to, that contained in this prospectus or any such free writing prospectus. If anyone provides you with different or inconsistent information, you should not rely on it. Neither we nor any of the underwriters is making an offer to sell or seeking offers to buy shares of our common stock in any jurisdiction where or to any person to whom the offer or sale is not permitted. The information in this prospectus is accurate only as of the date on the front cover of this prospectus and the information in any free writing prospectus that we may have provided to you in connection with this offering is accurate only as of the date of that free writing prospectus. Our business, financial condition, results of operations and future growth prospects may have changed since those dates.

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For investors outside the United States: neither we nor any of the underwriters has done anything that would permit this offering or possession or distribution of this prospectus or any free writing prospectus we may provide to you in connection with this offering in any jurisdiction where action for that purpose is required, other than in the United States. You are required to inform yourselves about and to observe any restrictions relating to this offering and the distribution of this prospectus and any such free writing prospectus outside of the United States.

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*This summary provides an overview of selected information contained elsewhere in this prospectus or incorporated by reference into this prospectus from our Annual Report on Form 10-K for the year ended December 31, 2012 and our other filings with the Securities and Exchange Commission listed in the section of this prospectus entitled "Incorporation of certain information by reference" and does not contain all of the information you should consider before investing in our common stock. You should carefully read this prospectus, the registration statement of which this prospectus is a part and the information incorporated by reference herein in their entirety before investing in our common stock, including the information discussed under "Risk factors" in this prospectus and in our Annual Report on Form 10-K for the year ended December 31, 2012 and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2013 incorporated by reference herein, along with our financial statements and notes thereto that are incorporated by reference herein. Unless otherwise indicated herein, the terms *Regulus*, *we*, *our*, *us*, or *the Company* refer to Regulus Therapeutics Inc.*

OVERVIEW

We are a biopharmaceutical company focused on discovering and developing first-in-class drugs that target *microRNAs* to treat a broad range of diseases. We were formed in 2007 when Alnylam Pharmaceuticals, Inc., or Alnylam, and Isis Pharmaceuticals, Inc., or Isis, contributed significant intellectual property, know-how and financial and human capital to pursue the development of drugs targeting *microRNAs* pursuant to a license and collaboration agreement. *microRNAs* are recently discovered, naturally occurring ribonucleic acid, or RNA, molecules that play a critical role in regulating key biological pathways. Scientific research has shown that the improper balance, or dysregulation, of *microRNAs* is directly linked to many diseases. We believe we have assembled the leading position in the *microRNA* field, including expertise in *microRNA* biology and oligonucleotide chemistry, a broad intellectual property estate, key opinion leaders and disciplined drug discovery and development processes. We refer to these assets as our *microRNA* product platform. We are using our *microRNA* product platform to develop chemically modified, single-stranded oligonucleotides that we call anti-miRs. We use these anti-miRs to modulate *microRNAs* and by doing so return diseased cells to their healthy state. We believe *microRNAs* may be transformative in the field of drug discovery and that anti-miRs may become a new and major class of drugs with broad therapeutic application much like small molecules, biologics and monoclonal antibodies.

We are currently optimizing anti-miRs in several distinct programs, both independently and with our strategic alliance partners, AstraZeneca AB, or AstraZeneca, GlaxoSmithKline plc, or GSK, and Sanofi. We also have a collaboration agreement with Biogen Idec MA Inc., or Biogen Idec, to evaluate the potential use of *microRNA* signatures as a biomarker for human patients with multiple sclerosis. Under these strategic alliances, we are eligible to receive up to approximately \$1.3 billion in milestone payments upon successful commercialization of *microRNA* therapeutics for the programs contemplated by our agreements. These payments include up to \$42.0 million upon achievement of preclinical and IND milestones, up to \$272.0 million upon achievement of clinical development milestones, up to \$305.0 million upon achievement of regulatory milestones and up to \$670.0 million upon achievement of commercialization milestones.

We are currently executing on our "Road to the Clinic" strategy which sets forth certain corporate goals that seek to advance our *microRNA* therapeutic pipeline towards the clinic. Specifically, we set the goal of nominating two *microRNA* candidates for clinical development in 2013. In May 2013, we announced our first clinical candidate, RG-101, for which we have full ownership and commercial rights. RG-101 is a GalNAc-conjugated *microRNA* anti-miR, which targets *microRNA*-122, for the treatment of patients with chronic hepatitis C virus infection, or HCV. We expect to submit our first investigational new drug

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application, or IND, to the U.S. Food and Drug Administration, or FDA, or equivalent foreign regulatory filing with foreign regulatory authorities, as applicable, for RG-101 in the first half of 2014. We anticipate that we will nominate a second clinical development candidate by the end of 2013.

POTENTIAL OF *microRNA* BIOLOGY

RNA plays an essential role in the process used by cells to encode and translate genetic information from DNA to proteins. RNA is comprised of subunits called nucleotides and is synthesized from a DNA template by a process known as transcription. Transcription generates different types of RNA, including messenger RNAs that carry the information for proteins in the sequence of their nucleotides. In contrast, *microRNAs* are small RNAs that do not code for proteins but rather are responsible for regulating gene expression by affecting the translation of target messenger RNAs. By interacting with many messenger RNAs, a single *microRNA* can regulate several genes that are instrumental for the normal function of a biological pathway. More than 500 *microRNAs* have been identified to date in humans, each of which is believed to interact with a specific set of genes that control key aspects of cell biology. Since most diseases are multi-factorial and involve multiple targets in a pathway, the ability to modulate gene networks by targeting a single *microRNA* provides a new therapeutic approach for treating complex diseases.

We believe that *microRNA* therapeutics have the potential to become a new and major class of drugs with broad therapeutic application for the following reasons:

- Ø *microRNAs* are a recent discovery in biology and, up until now, have not been a focus of pharmaceutical research;
- Ø *microRNAs* play a critical role in regulating biological pathways by controlling the translation of many target genes;
- Ø *microRNA* therapeutics target entire disease pathways which may result in more effective treatment of complex multi-factorial diseases;
- Ø *microRNA* therapeutics can be produced with a more efficient rational drug design process; and
- Ø *microRNA* therapeutics may be synergistic with other therapies because of their different mechanism of action.

OUR *microRNA* PRODUCT PLATFORM

We are the leading company in the field of *microRNA* therapeutics. Backed by our founding companies, Alnylam and Isis, we are uniquely positioned to leverage oligonucleotide technologies that have been proven in clinical trials. Central to achieving our goals is the know-how that we have accumulated in oligonucleotide design and how the specific chemistries behave in the clinical setting. We refer to this collective know-how, proprietary technology base, and its systematic application as our *microRNA* product platform.

We view the following as providing a competitive advantage for our *microRNA* product platform:

- Ø a mature platform selectively producing multiple development candidates advancing to the clinic;
- Ø scientific advisors who are pioneers in the *microRNA* field;
- Ø access to proven RNA therapeutic technologies through our founding companies, as well as approximately 900 patents and patent applications relating to oligonucleotide technologies;

Ø a leading *microRNA* intellectual property estate with access to over 170 patents and patent applications covering compositions and therapeutic uses;

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Ø development expertise and financial resources provided by our three major strategic alliances with AstraZeneca, GSK and Sanofi; and

Ø over 30 academic collaborations that help us identify new *microRNA* targets and support our early stage discovery efforts. The disciplined approach we take for the discovery and development of *microRNA* therapeutics is as important as the assets assembled to execute our plans and is based on the following four steps:

Step 1 - Evaluation of microRNA therapeutic opportunities

The initiation of our *microRNA* discovery and development efforts is based on rigorous scientific and business criteria, including:

Ø existence of significant scientific evidence to support the role of a specific *microRNA* in a disease;

Ø availability of predictive preclinical disease models to test our *microRNA* development candidates;

Ø ability to effectively deliver anti-miRs to the diseased cells or tissues; and

Ø existence of a reasonable unmet medical need and commercial opportunity.

Step 2 - Identification of microRNA targets

We identify *microRNA* targets through bioinformatic analysis of public and proprietary *microRNA* expression profiling data sets from samples of diseased human tissues. The analysis of such data sets can immediately highlight a potential role for specific *microRNAs* in the disease being studied. Further investigation of animal models that are predictive of human diseases in which those same *microRNAs* are also dysregulated provides additional data to support a new program. We have applied this strategy successfully in our existing programs and we believe that this approach will continue to help us identify clinically relevant *microRNA* targets.

Step 3 - Validation of microRNA targets

Our validation strategy is based on two distinct steps. First, using genetic tools, we determine whether up-regulation, or overproduction, of the *microRNA* in healthy animals can create the specific disease state and inhibition of the *microRNA* can lead to a therapeutic benefit. Second, using animal models predictive of human diseases, we determine whether pharmacological modulation of the up-regulated *microRNA* target with our anti-miRs can also lead to a therapeutic benefit. This validation process enables us to prioritize the best *microRNA* targets that appear to be key drivers of disease and not simply correlating markers.

Step 4 - Optimization of microRNA development candidates

We have developed a proprietary process that allows us to rapidly generate an optimized development candidate. Unlike traditional drug classes, such as small molecules, in which thousands of compounds must be screened to identify prospective leads, the fact that anti-miRs are mirror images of their target *microRNAs* allows for a more efficient rational design process. The optimization process incorporates our extensive knowledge base around oligonucleotide chemistry and anti-miR design to efficiently synthesize a starting pool of rationally designed anti-miRs to be evaluated in a series of proven assays and models. We also enhance our anti-miRs for distribution to the tissues where the specific *microRNA* target is causing disease.

OUR INITIAL DEVELOPMENT CANDIDATES

We are developing single-stranded oligonucleotides, which are chemically synthesized chains of nucleotides that are mirror images of specific target *microRNAs*. We incorporate proprietary chemical modifications to enhance drug properties such as potency, stability and tissue distribution. We refer to

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these chemically modified oligonucleotides as anti-miRs. Each anti-miR is designed to bind with and inhibit a specific *microRNA* target that is up-regulated in a cell and that is involved in the disease state. In binding to the *microRNA*, anti-miRs correct the dysregulation and return diseased cells to their healthy state. We have demonstrated therapeutic benefits of our anti-miRs in at least 20 different preclinical models of human diseases.

We have identified and validated several *microRNA* targets across a number of disease categories and are working independently and with our strategic alliance partners to optimize anti-miR development candidates. We expect that anti-miR development candidates will be easily formulated in saline solution and administered systemically or locally depending on the therapeutic indication. Our distinct therapeutic development programs are shown in the table below:

<i>microRNA target</i>	anti-miR program	Commercial rights
miR-122	RG-101 for HCV	Regulus*
miR-221	Hepatocellular carcinoma	Regulus
miR-10b	Glioblastoma	Regulus
miR-21	Hepatocellular carcinoma	Sanofi
miR-21	Kidney fibrosis	Sanofi
miR-33	Atherosclerosis	AstraZeneca

* With the exception of RG-101, commercial rights for miR-122 target licensed to GSK.

One aspect of our strategy is to pursue a balanced approach between product candidates that we develop ourselves and those that we develop with partners. We intend to focus our own resources on proprietary product opportunities in therapeutic areas where development and commercialization activities are appropriate for our size and financial resources, which we anticipate will include niche indications and orphan diseases. In therapeutic areas where costs are more significant, development timelines are longer or markets are too large for our capabilities, we will seek to secure partners with requisite expertise and resources.

Our approach has been validated to date by the following strategic alliances and collaborations with large pharmaceutical companies:

- Ø In April 2008, we formed a strategic alliance with GSK to discover and develop *microRNA* therapeutics for immuno-inflammatory diseases. In February 2010, we and GSK expanded the alliance to include potential *microRNA* therapeutics for the treatment of HCV. In June 2013, we amended our agreement with GSK and agreed that RG-101 is fully-owned by us and that miR-122 remains a collaboration target under the agreement.
- Ø In June 2010, we formed a strategic alliance with Sanofi to discover and develop *microRNA* therapeutics for fibrotic diseases. In July 2012, we expanded the alliance to include potential *microRNA* therapeutics in oncology. The original research term for this strategic alliance expired in June 2013, upon which we and Sanofi entered into an option agreement pursuant to which we granted Sanofi an exclusive right to negotiate the co-development and commercialization of certain of our unencumbered *microRNA* programs through December 2013, for which Sanofi has agreed to pay us an upfront option fee of \$2.5 million, \$1.25 million of which is creditable against future amounts payable by Sanofi to us. In addition, Sanofi granted us an exclusive option, which also expires in December 2013 to negotiate the co-development and commercialization of miR-21.
- Ø In August 2012, we formed a strategic alliance with AstraZeneca to discover and develop *microRNA* therapeutics for cardiovascular diseases, metabolic diseases and oncology.
- Ø In August 2012, we entered into a collaboration agreement with Biogen Idec to evaluate the potential use of *microRNA* signatures as a biomarker for human patients with multiple sclerosis. In June 2013, we and Biogen Idec amended the collaboration agreement to update the research plan and criteria for success.

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OUR STRATEGY

We are building the leading biopharmaceutical company focused on the discovery and development of first-in-class, targeted drugs based on our proprietary *microRNA* product platform. The key elements of our strategy are to:

- Ø *Rapidly advance our initial programs into clinical development.* We are currently optimizing our proprietary and partnered anti-miRs for development candidate selection. Under our Road to the Clinic strategy, we have nominated our fully-owned compound, RG-101, for the treatment of HCV as our first clinical candidate and expect to submit our first IND, or equivalent foreign regulatory filing, for RG-101 in the first half of 2014. We anticipate that we will nominate a second clinical candidate by the end of 2013.
- Ø *Focus our resources on developing drugs for niche indications or orphan diseases.* We believe that *microRNA* therapeutics have utility in almost every disease state as they regulate pathways, not single targets. We intend to focus on proprietary product opportunities in niche therapeutic areas where the development and commercialization activities are appropriate for our size and financial resources.
- Ø *Selectively form strategic alliances to augment our expertise and accelerate development and commercialization.* We have established strategic alliances with AstraZeneca, GSK and Sanofi and we will continue to seek partners who can bring therapeutic expertise, development and commercialization capabilities and funding to allow us to maximize the potential of our *microRNA* product platform.
- Ø *Selectively use our microRNA product platform to develop additional targets.* We have identified several other *microRNA* targets with potential for therapeutic modulation and will apply our rigorous scientific and business criteria to develop them.
- Ø *Develop microRNA biomarkers to support therapeutic product candidates.* We believe that *microRNA* biomarkers may be used to select optimal patient segments in clinical trials, to develop companion diagnostics, and to monitor disease progression or relapse. We believe these *microRNA* biomarkers can be applied toward drugs that we develop and drugs developed by other companies, including small molecules and monoclonal antibodies.
- Ø *Maintain scientific and intellectual leadership in the microRNA field.* We will continue to conduct research in the *microRNA* field to better understand this new biology and characterize the specific mechanism of action for our future drugs. This includes building on our strong network of key opinion leaders and securing additional intellectual property rights to broaden our existing proprietary asset estate.

OUR LEADERSHIP

Our management has more than 50 years of collective experience leading the discovery and development of innovative therapeutics, including significant operational and financial experience with emerging biotechnology companies, which we believe is the ideal combination of talent to execute our strategy. In addition, our experienced board of directors, which includes representatives of our founding companies, Alnylam and Isis, provides significant support and guidance in all aspects of our business.

Our executive officers are:

- Ø Kleanthis G. Xanthopoulos, Ph.D., our President and Chief Executive Officer, is an entrepreneur who has been involved in founding several companies, including Anadys Pharmaceuticals, Inc. (acquired by F. Hoffmann-La Roche Inc. in 2011), which he started as President and Chief Executive Officer.

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Ø Neil W. Gibson, Ph.D., our Chief Scientific Officer, is a leading scientist focused on cancer research and drug development who previously served as Chief Scientific Officer of the Oncology Research Unit at Pfizer Inc. and as Chief Scientific Officer of OSI Pharmaceuticals, Inc. He was involved in the development of several commercial cancer drugs including Xalkori® (crizotinib), Nexavar® (sorafenib) and Tarceva® (erlotinib).

Our executive team is supported by the following key personnel:

Ø Mary Glanville, our Senior Vice President of Human Capital, is an accomplished human resources executive in the life sciences industry who previously served in management roles at Anadys Pharmaceuticals, Inc. (acquired by F. Hoffman-La Roche Inc. in 2011), Inflazyme Inc. and Inex Pharmaceuticals Corp.

Ø Victor Knopov, Ph.D., our Vice President, Pharmaceutical Development, is a leader in oligonucleotide drug delivery and pharmaceutical development who has held positions at Nitto Denko Technical Corporation, Bio-Medics, Inc., EnGene, Inc., Marina Biotech, Inc. and Inex Pharmaceuticals Corporation. Dr. Knopov has extensive knowledge of Chemistry, Manufacturing and Control, or CMC, development for various technology platforms including commercial production of enzymes, anticancer liposomal products as well as advanced delivery systems for antisense, plasmids and siRNA based on lipids, polymer nanoparticles and conjugated systems.

Ø Daniel R. Chevallard, CPA, our Vice President, Finance and Accounting, is a corporate finance leader with public accounting expertise who previously held senior roles in corporate finance, accounting and financial reporting as a corporate controller and Senior Director, Finance at Prometheus Laboratories Inc. and who was a senior financial auditor at Ernst & Young LLP.

Our executive team, key personnel and board of directors are supported by our scientific advisory board members, who are renowned pioneers in the *microRNA* field:

Ø David Baltimore, Ph.D., Chairman of our scientific advisory board and Professor of Biology at the California Institute of Technology, received the Nobel Prize in 1975 and is highly regarded as a pioneer in virology and immunology, with his current research investigating the role of *microRNAs* in immunity. Dr. Baltimore is also a member of our board of directors.

Ø David Bartel, Ph.D., Professor of Biology at the Massachusetts Institute of Technology and the Whitehead Institute for Biomedical Research and an investigator at the Howard Hughes Medical Institute, studies *microRNA* genomics, target recognition and regulatory functions.

Ø Gregory Hannon, Ph.D., Professor at the Cold Spring Harbor Laboratory and an investigator at the Howard Hughes Medical Institute, has identified and characterized many of the major biogenesis and effector complexes for *microRNA* biology.

Ø Markus Stoffel, M.D., Ph.D., Professor of Metabolic Diseases at the Swiss Federal Institute of Technology, is focused on *microRNA* research and the regulation of glucose and lipid metabolism.

Ø Thomas Tuschl, Ph.D., Professor and Head of the Laboratory for RNA Molecular Biology at the Rockefeller University and an investigator at the Howard Hughes Medical Institute, discovered many of the mammalian *microRNA* genes and has developed methods for characterization of small RNAs.

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RISKS ASSOCIATED WITH OUR BUSINESS

Our business and ability to execute our business strategy are subject to a number of risks of which you should be aware before you decide to buy our common stock. In particular, you should consider the following risks, which are discussed more fully in the section entitled "Risk factors" in this prospectus and in our Annual Report on Form 10-K for the year ended December 31, 2012 and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2013, incorporated by reference herein.

- Ø We have never generated any revenue from product sales and may never become profitable. Even if this offering is successful, we may need to raise additional funds to support our operations and such funding may not be available to us on acceptable terms, or at all.

- Ø The approach we are taking to discover and develop drugs is novel and may never lead to marketable products.

- Ø All of our programs are still in preclinical development. Preclinical testing and clinical trials of our future product candidates may not be successful. If we are unable to successfully complete preclinical testing and clinical trials of our product candidates or experience significant delays in doing so, our business will be materially harmed.

- Ø We will depend on our strategic alliances for the development and eventual commercialization of certain future *microRNA* product candidates. If these strategic alliances are unsuccessful or are terminated, we may be unable to commercialize certain product candidates or generate future revenue from our development programs.

- Ø If we are unable to obtain or protect intellectual property rights related to our future products and product candidates, we may not be able to effectively develop or commercialize any of our product candidates or otherwise compete effectively in our markets.

- Ø We will need to expand our organization and we may experience difficulties in managing this growth, which could disrupt our operations.

- Ø Our future success depends on our ability to retain key executives and to attract, retain and motivate qualified personnel and our failure to do so might impede the progress of our research, development and commercialization objectives.

CORPORATE INFORMATION

We were originally formed as a limited liability company under the name Regulus Therapeutics LLC in the State of Delaware in September 2007. In January 2009, we converted Regulus Therapeutics LLC to a Delaware corporation and changed our name to Regulus Therapeutics Inc. Our principal executive offices are located at 3545 John Hopkins Court, Suite 210, San Diego, California 92121, and our telephone number is (858) 202-6300. Our corporate website address is www.regulusrx.com. Information contained on or accessible through our website is not a part of this prospectus, and the inclusion of our website address in this prospectus is an inactive textual reference only.

We use "Regulus Therapeutics" as a trademark in the United States and other countries. We have filed for registration of this trademark in the United States and have registered it in the European Union and Switzerland. This prospectus contains references to our trademarks and to trademarks belonging to other entities. Solely for convenience, trademarks and trade names referred to in this prospectus, including logos, artwork and other visual displays, may appear without the ® or symbols, but such references are not intended to indicate, in any way, that we will not assert, to the fullest extent under applicable law, our rights or the rights of the applicable licensor to these trademarks and trade names. We do not intend our use or display of other companies' trade names or trademarks to imply a relationship with, or endorsement or sponsorship of us by, any other companies.

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We are an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012. We will remain an emerging growth company until the earlier of (a) December 31, 2017, (b) the last day of the fiscal year in which we have total annual gross revenue of at least \$1.0 billion, or (c) the last day of the fiscal year in which we are deemed to be a large accelerated filer, which means the market value of our common stock that is held by non-affiliates exceeds \$700.0 million as of the prior June 30th and (d) the date on which we have issued more than \$1.0 billion in non-convertible debt during the prior three-year period. We refer to the Jumpstart Our Business Startups Act of 2012 herein as the JOBS Act, and references herein to emerging growth company shall have the meaning associated with it in the JOBS Act.

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The offering

Common stock offered by us	shares
Common stock to be outstanding after this offering	shares
Over-allotment option	The underwriters have an option for a period of 30 days to purchase up to additional shares of our common stock to cover over-allotments.
Use of proceeds	We intend to use the net proceeds of this offering for preclinical and clinical development of our proprietary compound, RG-101, and our other initial <i>microRNA</i> development candidates, for the identification and validation of additional <i>microRNA</i> targets and for other general corporate purposes. See Use of proceeds.
Risk factors	You should read the Risk factors section of this prospectus for a discussion of certain factors to consider carefully before deciding to purchase any shares of our common stock.
NASDAQ Global Market symbol	RGLS
The number of shares of our common stock to be outstanding after this offering is based on 35,965,371 shares of common stock outstanding as of March 31, 2013, and excludes:	
Ø	4,742,780 shares of common stock issuable upon the exercise of outstanding stock options as of March 31, 2013, at a weighted average exercise price of \$2.24 per share;
Ø	2,191,925 shares of common stock reserved for future issuance under our 2012 equity incentive plan, or the 2012 Plan, plus any future increases in the number of shares of common stock reserved for issuance under the 2012 Plan pursuant to the evergreen provision; and
Ø	481,274 shares of common stock reserved for future issuance under our 2012 employee stock purchase plan, or the ESPP, plus any future increases in the number of shares of common stock reserved for issuance under the ESPP pursuant to the evergreen provision.
Unless otherwise indicated, all information contained in this prospectus, and the number of shares of common stock outstanding as of March 31, 2013 assumes no exercise by the underwriters of their over-allotment option to purchase up to an additional _____ shares of our common stock.	

Table of Contents**Summary financial data**

The following table summarizes our financial data. We derived the summary statement of operations data for the years ended December 31, 2010, 2011 and 2012 from our audited financial statements and related notes incorporated by reference in this prospectus. We derived the summary statement of operations data for the three months ended March 31, 2012 and 2013 and balance sheet data as of March 31, 2013 from our unaudited financial statements and related notes incorporated by reference in this prospectus. Our historical results are not necessarily indicative of the results that may be expected in the future and results of interim periods are not necessarily indicative of the results for the entire year. The summary financial data should be read together with our financial statements and related notes incorporated by reference in this prospectus, Selected financial data and Management's discussion and analysis of financial condition and results of operations appearing elsewhere or incorporated by reference in this prospectus.

Statement of operations data	Year ended December 31,			Three months ended March 31,	
	2010	2011	2012	2012	2013
	(in thousands, except share and per share data)				
	(unaudited)				
Revenues:					
Revenue under strategic alliances and collaborations	\$ 8,112	\$ 13,767	\$ 12,700	\$ 3,344	\$ 3,238
Grant revenue	489	22			
Total revenues	8,601	13,789	12,700	3,344	3,238
Operating expenses:					
Research and development	20,178	17,289	20,342	4,603	6,883
General and administrative	3,921	3,637	4,932	921	1,905
Total operating expenses	24,099	20,926	25,274	5,524	8,788
Loss from operations	(15,498)	(7,137)	(12,574)	(2,180)	(5,550)
Other expense, net	(91)	(259)	(4,844)	(66)	(1,689)
Loss before income taxes	(15,589)	(7,396)	(17,418)	(2,246)	(7,239)
Income tax (benefit) expense	(30)	206	(10)	1	(10)
Net loss	\$ (15,559)	\$ (7,602)	\$ (17,408)	\$ (2,247)	\$ (7,229)
Net loss per share, basic and diluted ⁽¹⁾		\$ (85.82)	\$ (2.12)	\$ (13.06)	\$ (0.20)
Shares used to compute basic and diluted net loss per share ⁽¹⁾		88,582	8,212,538	171,998	35,872,606

(1) See Note 2 of our Notes to Financial Statements incorporated by reference in this prospectus for an explanation of the method used to calculate the basic and diluted net loss per common share and the number of shares used in the computation of the share and per share data. No share or per share data have been presented for 2010 since we had no common shares outstanding during that year.

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The unaudited as adjusted balance sheet data set forth below give effect to our issuance and sale of shares of our common stock in this offering at an assumed public offering price of \$ _____ per share, which is the last reported sale price of our common stock as reported on The NASDAQ Global Market on _____, 2013, after deducting estimated underwriting discounts and commissions and estimated offering expenses payable by us.

Balance sheet data	As of March 31, 2013	
	Actual	Pro forma as adjusted ⁽¹⁾
	(unaudited, in thousands)	
Cash, cash equivalents and short-term investments	\$ 90,715	\$ _____
Working capital	79,076	_____
Total assets	97,027	_____
Convertible notes payable	11,895	11,895
Accumulated deficit	(67,648)	_____
Total stockholders' equity	55,867	_____

(1) Each \$1.00 increase (decrease) in the assumed public offering price of \$ _____ per share, the last reported sale price of our common stock on The NASDAQ Global Market on _____, 2013, would increase (decrease) the as adjusted amount of cash and cash equivalents, working capital, total assets and total stockholders' equity by approximately \$ _____ million, assuming the number of shares offered by us, as set forth on the cover page of this prospectus, remains the same and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. We may also increase or decrease the number of shares we are offering. Each increase of shares in the number of shares offered by us would increase the as adjusted amount of cash and cash equivalents, working capital, total assets and total stockholders' equity by approximately \$ _____ million, assuming that the assumed public offering price remains the same, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. Similarly, each decrease of shares in the number of shares offered by us would decrease the as adjusted amount of cash and cash equivalents, working capital, total assets and total stockholders' equity by approximately \$ _____ million, assuming that the assumed public offering price remains the same, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. The as adjusted information discussed above is illustrative only and will be adjusted based on the actual public offering price and other terms of this offering determined at pricing.

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Risk factors

A purchase of shares of our common stock is an investment in our securities and involves a high degree of risk. You should carefully consider the risks and uncertainties and all other information contained in or incorporated by reference in this prospectus, including the risks and uncertainties discussed under Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2012 and our Quarterly Report on Form 10-Q for the quarter ended March 31, 2013. All of these risk factors are incorporated by reference herein in their entirety. If any of these risks actually occur, our business, financial condition and results of operations would likely suffer. In that case, the market price of our common stock could decline, and you may lose part or all of your investment in our company. Additional risks of which we are not presently aware or that we currently believe are immaterial may also harm our business and results of operations.

RISKS RELATED TO THIS OFFERING AND OWNERSHIP OF OUR COMMON STOCK

The market price of our common stock may be highly volatile, and you may not be able to resell your shares at or above the public offering price.

The trading price of our common stock is likely to continue to be volatile. Since shares of our common stock were sold in our initial public offering in October 2012 at a price of \$4.00 per share, our closing stock price as reported on The NASDAQ Global Market has ranged from \$4.02 to \$, through , 2013.

Our stock price could be subject to wide fluctuations in response to a variety of factors, including the following:

- Ø adverse results or delays in preclinical testing or clinical trials;
- Ø inability to obtain additional funding;
- Ø any delay in filing an IND or NDA for any of our future product candidates and any adverse development or perceived adverse development with respect to the FDA's review of that IND or NDA;
- Ø failure to maintain our existing strategic alliances or enter into new alliances;
- Ø failure of our strategic alliance partners to elect to develop and commercialize product candidates under our alliance agreements or the termination of any programs under our alliance agreements;
- Ø failure by us or our licensors and strategic alliance partners to prosecute, maintain or enforce our intellectual property rights;
- Ø failure to successfully develop and commercialize our future product candidates;

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- ∅ changes in laws or regulations applicable to our preclinical and clinical development activities, product candidates or future products;
- ∅ inability to obtain adequate product supply for our future product candidates or the inability to do so at acceptable prices;
- ∅ adverse regulatory decisions;
- ∅ introduction of new products, services or technologies by our competitors;
- ∅ failure to meet or exceed financial projections we may provide to the public;
- ∅ failure to meet or exceed the estimates and projections of the investment community;

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Risk factors

- Ø the perception of the pharmaceutical industry by the public, legislatures, regulators and the investment community;
- Ø announcements of significant acquisitions, strategic partnerships, joint ventures or capital commitments by us, our strategic alliance partners or our competitors;
- Ø disputes or other developments relating to proprietary rights, including patents, litigation matters and our ability to obtain patent protection for our technologies;
- Ø additions or departures of key scientific or management personnel;
- Ø significant lawsuits, including patent or stockholder litigation;
- Ø changes in the market valuations of similar companies;
- Ø sales of our common stock by us or our stockholders in the future; and
- Ø trading volume of our common stock.

In addition, companies trading in the stock market in general, and The NASDAQ Global Market in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of these companies. Broad market and industry factors may negatively affect the market price of our common stock, regardless of our actual operating performance.

Our principal stockholders and management own a significant percentage of our stock and will be able to exert significant control over matters subject to stockholder approval.

Our executive officers, directors, 5% stockholders and their affiliates beneficially own approximately 86% of our voting stock before this offering and, upon closing of this offering, that same group will beneficially own approximately % of our outstanding voting stock. Therefore, even after this offering, these stockholders will have the ability to influence us through this ownership position. These stockholders may be able to determine all matters requiring stockholder approval. For example, these stockholders, acting together, may be able to control elections of directors, amendments of our organizational documents, or approval of any merger, sale of assets, or other major corporate transaction. This may prevent or discourage unsolicited acquisition proposals or offers for our common stock that you may believe are in your best interest as one of our stockholders.

Even if this offering is successful, we may need to raise additional funding, which may not be available on acceptable terms, or at all.

Developing pharmaceutical products, including conducting preclinical studies and clinical trials, is expensive. We expect our research and development expenses to substantially increase in connection with our ongoing activities, particularly as we advance our product candidates toward clinical programs. If we are unable to successfully complete this offering, we will need to seek alternative financing or change our operational plans to continue as a going concern. Even if this offering is successful, we may need to raise additional funds to support our

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operations and such funding may not be available to us on acceptable terms, or at all.

We estimate that the net proceeds from this offering will be approximately \$ million. We expect that the net proceeds from this offering and our existing cash and cash equivalents, together with interest, will be sufficient to fund our current operations through at least the end of 2016. However, changing circumstances may cause us to consume capital more rapidly than we currently anticipate. For example, as we move our lead compounds through toxicology and other preclinical studies, also referred to as

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Risk factors

nonclinical studies, required to file an investigational new drug application, or IND, and as we conduct clinical development of RG-101 and any other future product candidates, we may have adverse results requiring that we find new product candidates. Additionally, our strategic alliance partners may not elect to pursue the development and commercialization of any of our *microRNA* product candidates that are subject to their respective strategic alliance agreements with us. Any of these events may increase our development costs more than we expect. We may need to raise additional funds or otherwise obtain funding through strategic alliances if we choose to initiate clinical trials for new product candidates other than programs currently partnered. In any event, we will require additional capital to obtain regulatory approval for, and to commercialize, future product candidates. Raising funds in the current economic environment, when the capital markets have been affected by the global recession, may present additional challenges.

If we are required to secure additional financing, such additional fundraising efforts may divert our management from our day-to-day activities, which may adversely affect our ability to develop and commercialize future product candidates. In addition, we cannot guarantee that future financing will be available in sufficient amounts or on terms acceptable to us, if at all. If we are unable to raise additional capital when required or on acceptable terms, we may be required to:

- Ø significantly delay, scale back or discontinue the development or commercialization of any future product candidates;
- Ø seek strategic alliances for research and development programs at an earlier stage than otherwise would be desirable or on terms that are less favorable than might otherwise be available; or
- Ø relinquish or license on unfavorable terms, our rights to technologies or any future product candidates that we otherwise would seek to develop or commercialize ourselves.

If we are required to conduct additional fundraising activities and we are unable to raise additional capital in sufficient amounts or on terms acceptable to us, we will be prevented from pursuing development and commercialization efforts, which will have a material adverse effect on our business, operating results and prospects.

We are an emerging growth company, and we cannot be certain if the reduced reporting requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012, or the JOBS Act. For as long as we continue to be an emerging growth company, we may take advantage of exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies, including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in this prospectus and our periodic reports and proxy statements and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and stockholder approval of any golden parachute payments not previously approved. We could be an emerging growth company through December 31, 2017, although circumstances could cause us to lose that status earlier, including if the market value of our common stock held by non-affiliates exceeds \$700.0 million as of any June 30 before that time or if we have total annual gross revenue of \$1.0 billion or more during any fiscal year before that time, in which cases we would no longer be an emerging growth company as of the following December 31 or, if we issue more than \$1.0 billion in non-convertible debt during any three year period before that time, we would cease to be an emerging growth company immediately. Even after we no longer qualify as an emerging growth company, we may still qualify as a smaller reporting company which would allow us to take

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Risk factors

advantage of many of the same exemptions from disclosure requirements including not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act and reduced disclosure obligations regarding executive compensation in this prospectus and our periodic reports and proxy statements. We cannot predict if investors will find our common stock less attractive because we may rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

Under the JOBS Act, emerging growth companies can also delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this exemption from new or revised accounting standards and, therefore, will be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

Sales of a substantial number of shares of our common stock in the public market by our existing stockholders could cause our stock price to fall.

Sales of a substantial number of shares of our common stock in the public market or the perception that these sales might occur could depress the market price of our common stock and could impair our ability to raise capital through the sale of additional equity securities. We are unable to predict the effect that sales may have on the prevailing market price of our common stock.

We, along with our directors and executive management team have agreed that for a period of 90 days after the date of this prospectus, subject to specified exceptions, we or they will not offer, sell, contract to sell, pledge or otherwise dispose of, directly or indirectly, any shares of our common stock or securities convertible into or exchangeable or exercisable for any shares of our common stock. Subject to certain limitations, approximately 140,327 shares will become eligible for sale upon expiration of such lock-up period, as calculated and described in more detail in the section entitled Shares eligible for future sale. In addition, shares issued or issuable upon exercise of options vested as of the expiration of the lock-up period will be eligible for sale at that time. Sales of stock by these stockholders could have a material adverse effect on the trading price of our common stock.

An additional 26,515,110 shares of our common stock are subject to lock-up agreements that were entered into in connection with our initial public offering, which lock-up agreements expire on October 4, 2013.

Certain holders of our securities are entitled to rights with respect to the registration of their shares under the Securities Act of 1933, as amended, or the Securities Act, subject to the applicable lock-up arrangement described above. Registration of these shares under the Securities Act would result in the shares becoming freely tradable without restriction under the Securities Act, except for shares held by our affiliates as defined in Rule 144 under the Securities Act. Any sales of securities by these stockholders could have a material adverse effect on the trading price of our common stock.

Future sales and issuances of our common stock or rights to purchase common stock, including pursuant to our equity incentive plans, could result in additional dilution of the percentage ownership of our stockholders and could cause our stock price to fall.

We expect that significant additional capital will be needed in the future to continue our planned operations. To the extent we raise additional capital by issuing equity securities, our stockholders may experience substantial dilution. We may sell common stock, convertible securities or other equity securities in one or more transactions at prices and in a manner we determine from time to time. If we sell common stock, convertible securities or other equity securities in more than one transaction, investors may be materially diluted by subsequent sales. These sales may also result in material dilution to our existing stockholders, and new investors could gain rights superior to our existing stockholders.

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Risk factors

Pursuant to our 2012 equity incentive plan, or the 2012 Plan, our management is authorized to grant stock options and other equity-based awards to our employees, directors and consultants. The number of shares available for future grant under the 2012 Plan will automatically increase each year by up to 4% of all shares of our capital stock outstanding as of December 31 of the prior calendar year, subject to the ability of our board of directors to take action to reduce the size of the increase in any given year. Any such increase, of the maximum amount or a lesser amount, will cause our stockholders to experience additional dilution, which could cause our stock price to fall. Currently, we plan to register the increased number of shares available for issuance under the 2012 Plan each year.

We have broad discretion in the use of the net proceeds from this offering and may not use them effectively.

Our management will have broad discretion in the application of the net proceeds from this offering, including for any of the purposes described in the section entitled "Use of proceeds," and you will not have the opportunity as part of your investment decision to assess whether the net proceeds are being used appropriately. Because of the number and variability of factors that will determine our use of the net proceeds from this offering, their ultimate use may vary substantially from their currently intended use. The failure by our management to apply these funds effectively could harm our business. Pending their use, we may invest the net proceeds from this offering in short-term, investment-grade, interest-bearing securities. These investments may not yield a favorable return to our stockholders.

Our ability to use our net operating loss carryforwards and certain other tax attributes may be limited.

Under Section 382 of the Internal Revenue Code of 1986, as amended, if a corporation undergoes an ownership change, generally defined as a greater than 50% change (by value) in its equity ownership over a three year period, the corporation's ability to use its pre-change net operating loss carryforwards, or NOLs, and other pre-change tax attributes (such as research tax credits) to offset its post-change income may be limited. We believe that, with our initial public offering and other transactions that have occurred over the past three years, we may have triggered an ownership change limitation. We may also experience ownership changes in the future as a result of subsequent shifts in our stock ownership. As a result, if we earn net taxable income, our ability to use our pre-change net operating loss carryforwards to offset U.S. federal taxable income may be subject to limitations, which could potentially result in increased future tax liability to us. In addition, at the state level, there may be periods during which the use of NOLs is suspended or otherwise limited, which could accelerate or permanently increase state taxes owed.

We do not intend to pay dividends on our common stock so any returns will be limited to the value of our stock.

We have never declared or paid any cash dividends on our common stock. We currently anticipate that we will retain future earnings for the development, operation and expansion of our business and do not anticipate declaring or paying any cash dividends for the foreseeable future. Any return to stockholders will therefore be limited to the appreciation of their stock.

RISKS RELATED TO OUR INTELLECTUAL PROPERTY

Third-party claims of intellectual property infringement may prevent or delay our development and commercialization efforts.

Our commercial success depends in part on our avoiding infringement of the patents and proprietary rights of third parties. There is a substantial amount of litigation, both within and outside the United States,

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Risk factors

involving patent and other intellectual property rights in the biotechnology and pharmaceutical industries, including patent infringement lawsuits, interferences, oppositions and inter partes reexamination proceedings before the U.S. Patent and Trademark Office and corresponding foreign patent offices. Numerous U.S. and foreign issued patents and pending patent applications, which are owned by third parties, exist in the fields in which we and our strategic alliance partners are pursuing development candidates. For example, we are aware that Santaris Pharma A/S, or Santaris, has patents and patent applications in the *microRNA* therapeutics space, including patents and patent applications related to targeting *microRNAs*, such as miR-122, for the treatment of disease. As the biotechnology and pharmaceutical industries expand and more patents are issued, the risk increases that our future product candidates may be subject to claims of infringement of the patent rights of third parties.

Third parties may assert that we are employing their proprietary technology without authorization. There may be third-party patents or patent applications with claims to materials, formulations, methods of manufacture or methods for treatment related to the use or manufacture of our future product candidates. Because patent applications can take many years to issue, there may be currently pending patent applications which may later result in issued patents that our future product candidates may infringe. In addition, third parties may obtain patents in the future and claim that use of our technologies infringes upon these patents. If any third-party patents were held by a court of competent jurisdiction to cover the manufacturing process of any of our future product candidates, any molecules formed during the manufacturing process or any final product itself, the holders of any such patents may be able to block our ability to commercialize such product candidate unless we obtained a license under the applicable patents, or until such patents expire. Similarly, if any third-party patents were held by a court of competent jurisdiction to cover aspects of our formulations, processes for manufacture or methods of use, including combination therapy, the holders of any such patents may be able to block our ability to develop and commercialize the applicable product candidate unless we obtained a license or until such patent expires. In either case, such a license may not be available on commercially reasonable terms or at all.

Parties making claims against us may obtain injunctive or other equitable relief, which could effectively block our ability to further develop and commercialize one or more of our future product candidates. Defense of these claims, regardless of their merit, would involve substantial litigation expense and would be a substantial diversion of employee resources from our business. In the event of a successful claim of infringement against us, we may have to pay substantial damages, including treble damages and attorneys' fees for willful infringement, pay royalties, redesign our infringing products or obtain one or more licenses from third parties, which may be impossible or require substantial time and monetary expenditure.

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Special note regarding forward-looking statements

This prospectus contains forward-looking statements. The forward-looking statements are contained principally in the sections entitled Prospectus summary, Risk factors, Management's discussion and analysis of financial condition and results of operations and Business in this prospectus or incorporated by reference herein. These statements relate to future events or to our future financial performance and involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by the forward-looking statements. Forward-looking statements include, but are not limited to, statements about:

- ∅ the initiation, cost, timing, progress and results of our research and development activities, preclinical studies and future clinical trials;
- ∅ our ability to obtain and maintain regulatory approval of our future product candidates, and any related restrictions, limitations, and/or warnings in the label of an approved product candidate;
- ∅ our ability to obtain funding for our operations;
- ∅ our plans to research, develop and commercialize our future product candidates;
- ∅ our strategic alliance partners' election to pursue development and commercialization;
- ∅ our ability to attract collaborators with development, regulatory and commercialization expertise;
- ∅ our ability to obtain and maintain intellectual property protection for our future product candidates;
- ∅ the size and growth potential of the markets for our future product candidates, and our ability to serve those markets;
- ∅ our ability to successfully commercialize our future product candidates;
- ∅ the rate and degree of market acceptance of our future product candidates;
- ∅ our ability to develop sales and marketing capabilities, whether alone or with potential future collaborators;

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- Ø regulatory developments in the United States and foreign countries;
- Ø the performance of our third-party suppliers and manufacturers;
- Ø the success of competing therapies that are or become available;
- Ø the loss of key scientific or management personnel;
- Ø our expectations regarding the time during which we will be an emerging growth company under the JOBS Act;
- Ø our use of the proceeds from this offering; and
- Ø the accuracy of our estimates regarding expenses, future revenues, capital requirements and need for additional financing.

In some cases, you can identify these statements by terms such as anticipate, believe, could, estimate, expect, intend, may, plan, predict, project, should, will, would or the negative of those terms, and similar expressions. These forward-looking statements reflect our management's beliefs and views with respect to future events and are based on estimates and assumptions as of the date of this prospectus and are subject to risks and uncertainties. We discuss many of these risks in greater detail under the heading Risk factors. Moreover, we operate in a very

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Special note regarding forward-looking statements

competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. Given these uncertainties, you should not place undue reliance on these forward-looking statements. The Private Securities Litigation Reform Act of 1995 and Section 27A of the Securities Act of 1933, as amended, do not protect any forward-looking statements that we make in connection with this offering.

You should read this prospectus and the documents that we reference in this prospectus and have filed as exhibits to the registration statement, of which this prospectus is a part, completely and with the understanding that our actual future results may be materially different from what we expect. We qualify all of the forward-looking statements in this prospectus by these cautionary statements.

Except as required by law, we assume no obligation to update these forward-looking statements publicly, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future.

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Use of proceeds

We estimate that we will receive net proceeds of approximately \$ million (or approximately \$ million if the underwriters over-allotment option is exercised in full) from the sale of the shares of common stock offered by us in this offering, after deducting the underwriting discounts and commissions and estimated offering expenses payable by us.

We intend to use the net proceeds of this offering for preclinical and clinical development of our proprietary compound, RG-101, and our other initial *microRNA* development candidates, for the identification and validation of additional *microRNA* targets, and for capital expenditures, working capital and other general corporate purposes. We may also use a portion of the net proceeds to in-license, acquire or invest in complementary *microRNA* businesses, technologies, products or assets. However, we have no current commitments or obligations to do so. We cannot currently allocate specific percentages of the net proceeds that we may use for the purposes specified above. Accordingly, we will have broad discretion in the use of the net proceeds from this offering and could spend the proceeds in ways that do not improve our results of operations or enhance the value of our stock. Pending their use, we plan to invest the net proceeds from this offering in short- and intermediate-term, interest-bearing obligations, investment-grade instruments, certificates of deposit or direct or guaranteed obligations of the U.S. government.

Table of Contents**Price range of our common stock**

Our common stock has been listed on the NASDAQ Global Market since October 4, 2012 under the symbol RGLS . Prior to that date, there was no public market for our common stock. Shares sold in our initial public offering on October 4, 2012 were priced at \$4.00 per share.

On _____, 2013, the closing price for our common stock as reported on the NASDAQ Global Market was \$ _____ per share. The following table sets forth the ranges of high and low sales prices per share of our common stock as reported on the NASDAQ Global Market for the period indicated. Such quotations represent inter-dealer prices without retail markup, markdown or commission and may not necessarily represent actual transactions.

Year Ended December 31, 2012	High	Low
Fourth Quarter (from October 4, 2012)	\$6.49	\$4.02
Year Ended December 31, 2013	High	Low
First Quarter	\$7.89	\$4.67
Second Quarter	\$	\$
Third Quarter (through _____, 2013)	\$	\$

As of _____, 2013, there were _____ stockholders of record, which excludes stockholders whose shares were held in nominee or street name by brokers. The actual number of common stockholders is greater than the number of record holders, and includes stockholders who are beneficial owners, but whose shares are held in street name by brokers and other nominees. This number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

Table of Contents**Equity compensation plan information**

The following table provides certain information with respect to all of our equity compensation plans in effect as of December 31, 2012:

Plan Category	Number of securities	Weighted-average	Number of securities
	to be issued upon		remaining available for
	exercise of	exercise price of	issuance under
	outstanding	outstanding options	equity
	restricted stock		compensation plans
	units and rights		(excluding securities
	(a)		reflected in column
			(a))
Equity compensation plans approved by security holders ⁽¹⁾	4,719,799	\$ 2.11	1,485,711
Equity compensation plans not approved by security holders			
Total	4,719,799	\$ 2.11	1,485,711

(1) Available for the grant of future rights under our 2012 equity incentive plan, or 2012 Plan, and 2012 employee stock purchase plan, or ESPP, as of December 31, 2012, excluding future increases in the number of shares of common stock reserved for issuance under the 2012 Plan and ESPP pursuant to the evergreen provisions therein

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Dividend policy

We have never declared or paid any cash dividends on our common stock. We currently intend to retain all available funds and any future earnings to support our operations and finance the growth and development of our business. We do not intend to pay cash dividends on our common stock for the foreseeable future. Any future determination related to our dividend policy will be made at the discretion of our board of directors and will depend upon, among other factors, our results of operations, financial condition, capital requirements, contractual restrictions, business prospects and other factors our board of directors may deem relevant.

Table of Contents**Capitalization**

The following table sets forth our cash, cash equivalents and short-term investments, and our capitalization as of March 31, 2013:

Ø on an actual basis;

Ø on a pro forma as adjusted basis to reflect the sale by us of _____ shares of our common stock in the offering at an assumed public offering price of \$ _____ per share (the last reported sale price of our common stock, as reported on The NASDAQ Global Market on _____, 2013), after deducting the underwriting discounts and commissions and estimated offering costs payable by us.

You should read this table together with Management's discussion and analysis of financial condition and results of operations and our financial statements and the related notes appearing elsewhere in this prospectus or incorporated by reference herein.

	As of March 31, 2013	
	Actual	Pro forma as adjusted ⁽¹⁾
	(unaudited, in thousands, except share and per share data)	
Cash, cash equivalents and short-term investments	\$ 90,715	
Convertible notes payable ⁽²⁾	11,895	11,895
Convertible preferred stock; \$0.001 par value: 10,000,000 shares authorized, no shares issued or outstanding, actual; 10,000,000 shares authorized, no shares issued or outstanding, pro forma as adjusted		
Stockholders' equity:		
Common stock; \$0.001 par value:		
200,000,000 shares authorized, 35,965,371 shares issued and outstanding, actual; 200,000,000 shares authorized and _____ shares issued and outstanding, pro forma as adjusted	36	
Additional paid-in capital	123,576	
Accumulated other comprehensive loss	(37)	(37)
Accumulated deficit	(67,648)	(67,648)
Total stockholders' equity	55,867	
Total capitalization	\$ 67,762	

(1) Each \$1.00 increase (decrease) in the assumed public offering price of \$ per share, the last reported sale price of our common stock on The NASDAQ Global Market on _____, 2013, would increase (decrease) the as adjusted amount of cash and cash equivalents, working capital, total assets and total stockholders' equity by approximately \$ _____ million, assuming the number of shares offered by us, as set forth on the cover page of this prospectus, remains

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the same and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. We may also increase or decrease the number of shares we are offering. Each increase of shares in the number of shares offered by us would increase the as adjusted amount of cash and cash equivalents, working capital, total assets and total stockholders' equity by approximately \$ million, assuming that the assumed public offering price remains the same, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. Similarly, each decrease of shares in the number of shares offered by us would decrease the as adjusted amount of cash and cash equivalents, working capital, total assets and total stockholders' equity by approximately \$ million, assuming that the assumed public offering price remains the same, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. The as adjusted information discussed above is illustrative only and will be adjusted based on the actual public offering price and other terms of this offering determined at pricing.

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Capitalization

- (2) *In October 2012, in conjunction with our initial public offering, the promissory note we issued to Glaxo Group Limited, or GSK, in 2010 was amended and restated with a principal amount of \$5.4 million. This amended note had a maturity date of three years from the anniversary of the agreement, or October 2015. At GSK's option, this note shall be convertible into shares of our common stock at any time prior to the maturity date with a conversion equal to the quotient of all outstanding principal and interest divided by the initial public offering price of \$4.00 per share. The value attributed to the convertible note payable in the table above reflects the fair value of the note, including the conversion option. The outstanding principal of the convertible note payable as of March 31, 2013 was \$5.4 million, which would result in total capitalization of \$74.2 million, on a pro forma basis.*

The number of shares of common stock shown as issued and outstanding on a pro forma as adjusted basis in the table is based on the number of shares of our common stock outstanding as of March 31, 2013, and excludes:

- Ø 4,742,780 shares of common stock issuable upon the exercise of outstanding stock options as of March 31, 2013, at a weighted average exercise price of \$2.24 per share;
- Ø 2,191,925 shares of common stock reserved for future issuance under our 2012 equity incentive plan, or the 2012 Plan, plus any future increases in the number of shares of common stock reserved for issuance under the 2012 Plan pursuant to the evergreen provision; and
- Ø 481,274 shares of common stock reserved for future issuance under our 2012 employee stock purchase plan, or the ESPP, plus any future increases in the number of shares of common stock reserved for issuance under the ESPP pursuant to the evergreen provision.

Table of Contents**Dilution**

If you invest in our common stock in this offering, your ownership interest will be immediately diluted to the extent of the difference between the public offering price per share and the pro forma as adjusted net tangible book value per share of our common stock after this offering.

Our historical net tangible book value per share is determined by dividing our total tangible assets less total liabilities by the actual number of outstanding shares of our common stock. The historical net tangible book value of our common stock as of March 31, 2013 was \$54.7 million, or \$1.52 per share.

After giving effect to the sale of _____ shares of our common stock offered by us at an assumed public offering price of \$ _____ per share (the last reported sale price of our common stock on The NASDAQ Global Market on _____, 2013), after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us, our net tangible book value as of March 31, 2013, would have been approximately \$ _____ million, or \$ _____ per share of common stock. This represents an immediate increase in net tangible book value of \$ _____ per share to existing stockholders and an immediate dilution of \$ _____ per share to new investors purchasing shares of common stock in this offering at the assumed public offering price.

The following table illustrates this dilution on a per share basis:

Assumed offering price per share	\$
Historical net tangible book value per share as of March 31, 2013	\$ 1.52
Increase in net tangible book value per share attributable to new investors	
Pro forma net tangible book value per share after the offering	
Dilution per share to new investors	\$

Each \$1.00 increase (decrease) in the assumed public offering price of \$ _____ per share would increase (decrease) our as adjusted net tangible book value after this offering by approximately \$ _____ million, or approximately \$ _____ per share, and the dilution per share to new investors by approximately \$ _____ per share, assuming that the number of shares offered by us, as set forth on the cover page of this prospectus, remains the same and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. We may also increase or decrease the number of shares we are offering. An increase of shares in the number of shares offered by us would increase our as adjusted net tangible book value after this offering by approximately \$ _____ million, or \$ _____ per share, and the dilution per share to new investors would be \$ _____ per share, assuming that the assumed public offering price remains the same, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. Similarly, a decrease of shares in the number of shares offered by us would decrease our as adjusted net tangible book value after this offering by approximately \$ _____ million, or \$ _____ per share, and the dilution per share to new investors would be \$ _____ per share, assuming that the assumed public offering price remains the same, and after deducting the estimated underwriting discounts and commissions and estimated offering expenses payable by us. The information discussed above is illustrative only and will adjust based on the actual public offering price and other terms of this offering determined at pricing.

If the underwriters exercise in full their option to purchase up to additional shares of common stock at the assumed public offering price of \$ _____ per share, the as adjusted net tangible book value after this offering would be \$ _____ per share, representing an increase in net tangible book value of \$ _____ per share to existing stockholders and immediate dilution in net tangible book value of \$ _____ per share to investors purchasing our common stock in this offering at the assumed public offering price.

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Dilution

The number of shares of our common stock to be outstanding after this offering is based on 35,965,371 shares of common stock outstanding as of March 31, 2013, and excludes:

- Ø 4,742,780 shares of common stock issuable upon the exercise of outstanding stock options as of March 31, 2013, at a weighted average exercise price of \$2.24 per share;
- Ø 2,191,925 shares of common stock reserved for future issuance under our 2012 equity incentive plan, or the 2012 Plan, plus any future increases in the number of shares of common stock reserved for issuance under the 2012 Plan pursuant to the evergreen provision; and
- Ø 481,274 shares of common stock reserved for future issuance under our 2012 employee stock purchase plan, or the ESPP, plus any future increases in the number of shares of common stock reserved for issuance under the ESPP pursuant to the evergreen provision.

Table of Contents**Selected financial data**

The following selected financial data should be read together with our financial statements and accompanying notes and Management's discussion and analysis of financial condition and results of operations appearing elsewhere in this prospectus or incorporated by reference herein. The selected financial data in this section are not intended to replace our financial statements and the related notes. Our historical results are not necessarily indicative of our future results.

The selected statement of operations data for the years ended December 31, 2010, 2011 and 2012 and the selected balance sheet data as of December 31, 2011 and 2012 are derived from our audited financial statements incorporated by reference in this prospectus. The selected statement of operations data for the three months ended March 31, 2012 and 2013 and the selected balance sheet data as of March 31, 2013 are derived from our unaudited financial statements incorporated by reference in this prospectus. The unaudited financial statements have been prepared on a basis consistent with our audited financial statements included in this prospectus and include, in our opinion, all adjustments, consisting of normal recurring adjustments necessary for the fair presentation of the financial information in those statements.

Statement of operations data	2010	Year ended December 31, 2011	2012 (in thousands, except share and per share data)	Three months ended March 31, 2012 (unaudited)	2013
Revenues:					
Revenue under strategic alliances and collaborations	\$ 8,112	\$ 13,767	\$ 12,700	\$ 3,344	\$ 3,238
Grant revenue	489	22			
Total revenues	8,601	13,789	12,700	3,344	3,238
Operating expenses:					
Research and development	20,178	17,289	20,342	4,603	6,883
General and administrative	3,921	3,637	4,932	921	1,905
Total operating expenses	24,099	20,926	25,274	5,524	8,788
Loss from operations	(15,498)	(7,137)	(12,574)	(2,180)	(5,550)
Other expense, net	(91)	(259)	(4,844)	(66)	(1,689)
Loss before income taxes	(15,589)	(7,396)	(17,418)	(2,246)	(7,239)
Income tax (benefit) expense	(30)	206	(10)	1	(10)
Net loss	\$ (15,559)	\$ (7,602)	\$ (17,408)	\$ (2,247)	\$ (7,229)
Net loss per share, basic and diluted ⁽¹⁾		\$ (85.82)	\$ (2.12)	\$ (13.06)	\$ (0.20)
Shares used to compute basic and diluted net loss per share ⁽¹⁾		88,582	8,212,538	171,998	35,872,606

(1)

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See Note 2 of our Notes to Financial Statements incorporated by reference in this prospectus for an explanation of the method used to calculate the basic and diluted net loss per common share and the number of shares used in the computation of the share and per share data. No share or per share data have been presented for 2010 since we had no common shares outstanding during that year.

Table of Contents**Selected financial data**

Balance sheet data	As of December 31,		As of March 31,
	2011	2012	2013
			(unaudited)
		(in thousands)	
Cash, cash equivalents and short-term investments	\$ 38,144	\$ 98,100	\$ 90,715
Working capital	25,816	86,161	79,076
Total assets	42,881	103,518	97,027
Convertible notes payable	10,815	10,134	11,895
Accumulated deficit	(43,011)	(60,419)	(67,648)
Total stockholders (deficit) equity	(41,494)	62,093	55,867

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OVERVIEW

Our business

We are a biopharmaceutical company focused on discovering and developing first-in-class drugs that target *microRNAs* to treat a broad range of diseases. *microRNAs* are recently discovered, naturally occurring ribonucleic acid, or RNA, molecules that play a critical role in regulating key biological pathways. Scientific research has shown that the improper balance, or dysregulation, of *microRNAs* is directly linked to many diseases. We believe we have assembled the leading position in the *microRNA* field, including expertise in *microRNA* biology and oligonucleotide chemistry, a broad intellectual property estate, key opinion leaders and disciplined drug discovery and development processes. We refer to these assets as our *microRNA* product platform. We are using our *microRNA* product platform to develop chemically modified, single-stranded oligonucleotides that we call anti-miRs. We use these anti-miRs to modulate *microRNAs* and by doing so return diseased cells to their healthy state. We believe *microRNAs* may be transformative in the field of drug discovery and that anti-miRs may become a new and major class of drugs with broad therapeutic application much like small molecules, biologics and monoclonal antibodies. We are currently optimizing anti-miRs in several distinct programs, both independently and with our strategic alliance partners, AstraZeneca AB, or AstraZeneca, GlaxoSmithKline plc, or GSK, and Sanofi. We also have a collaboration agreement with Biogen Idec MA Inc. to evaluate the potential use of *microRNA* signatures as a biomarker for human patients with multiple sclerosis.

We are currently executing on our "Road to the Clinic" strategy which sets forth certain corporate goals that seek to advance our *microRNA* therapeutic pipeline toward the clinic. Specifically, we set the goal of nominating two *microRNA* candidates for clinical development in 2013. In May 2013, we announced our first clinical candidate as RG-101, for which we have full ownership and commercial rights. RG-101 is a GalNAc-conjugated *microRNA* anti-miR, which targets *microRNA*-122 for the treatment of patients with chronic hepatitis C virus infection, or HCV. We expect to submit our first investigation new drug application, or IND, to the U.S. Food and Drug Administration, or FDA, or equivalent foreign regulatory filing with foreign regulatory authorities, as applicable, for RG-101 in the first half of 2014. We anticipate that we will nominate a second clinical candidate by the end of 2013.

RNA plays an essential role in the process used by cells to encode and translate genetic information from DNA to proteins. RNA is comprised of subunits called nucleotides and is synthesized from a DNA template by a process known as transcription. Transcription generates different types of RNA, including messenger RNAs that carry the information for proteins in the sequence of their nucleotides. In contrast, *microRNAs* are small RNAs that do not code for proteins, but rather are responsible for regulating gene expression by affecting the translation of target messenger RNAs. By interacting with many messenger RNAs, a single *microRNA* can regulate several genes that are instrumental for the normal function of a biological pathway. More than 500 *microRNAs* have been identified to date in humans, each of which is believed to interact with a specific set of genes that control key aspects of cell biology. Since most diseases are multi-factorial and involve multiple targets in a pathway, the ability to modulate gene networks by targeting a single *microRNA* provides a new therapeutic approach for treating complex diseases.

We were formed in 2007 when Alnylam Pharmaceuticals, Inc., or Alnylam, and Isis Pharmaceuticals, Inc., or Isis, contributed significant intellectual property, know-how and financial and human capital to pursue the development of drugs targeting *microRNAs*. This provided the foundation for our leadership position in the *microRNA* field and, since then, we have leveraged their RNA-based discovery and development expertise, established over more than 20 years, to build our own proprietary *microRNA* product platform that combines a deep understanding of biology with innovative chemistries and disciplined processes.

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We are developing single-stranded oligonucleotides, which are chemically synthesized chains of nucleotides, that are mirror images of specific target *microRNAs*. We incorporate proprietary chemical modifications to enhance drug properties such as potency, stability and tissue distribution. We refer to these chemically modified oligonucleotides as anti-miRs. Each anti-miR is designed to bind with and inhibit a specific *microRNA* target that is up-regulated, or overproduced, in a cell and that is involved in the disease state. In binding to the *microRNA*, anti-miRs correct the dysregulation and return diseased cells to their healthy state. We have demonstrated therapeutic benefits of our anti-miRs in at least 20 different preclinical models of human diseases.

We have identified and validated several *microRNA* targets across a number of disease categories and are working independently and with our strategic alliance partners to optimize anti-miR development candidates. We expect that anti-miR development candidates will be easily formulated in saline solution and administered systemically or locally depending on the therapeutic indication. Our therapeutic development programs are shown in the table below:

<i>microRNA</i> target	anti-miR program	Commercial rights
miR-122	RG-101 for HCV	Regulus*
miR-221	Hepatocellular carcinoma	Regulus
miR-10b	Glioblastoma	Regulus
miR-21	Hepatocellular carcinoma	Sanofi
miR-21	Kidney fibrosis	Sanofi
miR-33	Atherosclerosis	AstraZeneca

* With the exception of RG-101, commercial rights for miR-122 target licensed to GSK.

One aspect of our strategy is to pursue a balanced approach between product candidates that we develop ourselves and those that we develop with partners. We intend to focus our own resources on proprietary product opportunities in therapeutic areas where development and commercialization are appropriate for our size and financial resources, which we anticipate will include niche indications and orphan diseases. In therapeutic areas where costs are more significant, development timelines are longer or markets are too large for our capabilities, we will seek to secure partners with requisite expertise and resources.

Our approach has been validated to date by the following strategic alliances and collaborations with large pharmaceutical companies:

Ø In April 2008, we formed a strategic alliance with GSK to discover and develop *microRNA* therapeutics for immuno-inflammatory diseases. In February 2010, we and GSK expanded the alliance to include potential *microRNA* therapeutics for the treatment of HCV. In June 2013, we amended our agreement with GSK and agreed that RG-101 is fully-owned by us and that miR-122 remains a collaboration target under the agreement.

Ø In June 2010, we formed a strategic alliance with Sanofi to discover and develop *microRNA* therapeutics for fibrotic diseases. In July 2012, we expanded the alliance to include potential *microRNA* therapeutics in oncology. The original research term for this strategic alliance expired in June 2013, upon which we and Sanofi entered into a letter agreement pursuant to which we granted Sanofi an exclusive right to negotiate for the co-development and commercialization of certain of our unencumbered *microRNA* programs through December 2013, for which Sanofi has agreed to pay us an upfront option fee of \$2.5 million, \$1.25 million of which is creditable against future amounts payable by Sanofi to us. In addition, Sanofi granted us an exclusive option, which also expires in December 2013, to negotiate the co-development and commercialization of miR-21.

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- Ø In August 2012, we formed a strategic alliance with AstraZeneca to discover and develop *microRNA* therapeutics for cardiovascular diseases, metabolic diseases and oncology.

- Ø In August 2012, we entered into a collaboration agreement with Biogen Idec to evaluate the potential use of *microRNA* signatures as a biomarker for human patients with multiple sclerosis. In June 2013, we and Biogen Idec amended the collaboration agreement to update the research plan and criteria for success.

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Under our existing strategic alliances with AstraZeneca, GSK and Sanofi, we are eligible to receive up to approximately \$1.3 billion in milestone payments upon successful commercialization of *micro*RNA therapeutics for the eight programs contemplated by our agreements. These payments include up to \$42.0 million upon achievement of preclinical and IND milestones, up to \$272.0 million upon achievement of clinical development milestones, up to \$305.0 million upon achievement of regulatory milestones and up to \$670.0 million upon achievement of commercialization milestones.

Our leadership

Our management has more than 50 years of collective experience leading the discovery and development of innovative therapeutics, including significant operational and financial experience with emerging biotechnology companies, which we believe is the ideal combination of talent to execute our strategy. In addition, our experienced board of directors, which includes representatives of our founding companies, Alnylam and Isis, provides significant support and guidance in all aspects of our business.

Our executive officers are:

- Ø Kleanthis G. Xanthopoulos, Ph.D., our President and Chief Executive Officer, is an entrepreneur who has been involved in founding several companies, including Anadys Pharmaceuticals, Inc. (acquired by F. Hoffman-La Roche Inc. in 2011), which he started as President and Chief Executive Officer.
- Ø Neil W. Gibson, Ph.D., our Chief Scientific Officer, is a leading scientist focused on cancer research and drug development who previously served as Chief Scientific Officer of the Oncology Research Unit at Pfizer Inc. and as Chief Scientific Officer of OSI Pharmaceuticals, Inc. He was involved in the development of several commercial cancer drugs including Xalkori[®] (crizotinib), Nexavar[®] (sorafenib) and Tarceva[®] (erlotinib).

Our executive team is supported by the following key personnel:

- Ø Mary Glanville, our Senior Vice President of Human Capital, is an accomplished human resources executive in the life sciences industry who previously served in management roles at Anadys Pharmaceuticals, Inc. (acquired by F. Hoffman-La Roche Inc. in 2011), Inflazyme Inc. and Inex Pharmaceuticals Corp.
- Ø Victor Knopov, Ph.D., our Vice President, Pharmaceutical Development, is a leader in oligonucleotide drug delivery and pharmaceutical development who has held positions at Nitto Denko Technical Corporation, Bio-Medics, Inc., EnGene, Inc., Marina Biotech, Inc. and Inex Pharmaceuticals Corporation. Dr. Knopov has extensive knowledge of Chemistry, Manufacturing and Control, or CMC, development for various technology platforms including commercial production of enzymes, anticancer liposomal products as well as advanced delivery systems for antisense, plasmids and siRNA based on lipids, polymer nanoparticles and conjugated systems.
- Ø Daniel R. Chevallard, CPA, our Vice President, Finance and Accounting, is a corporate finance leader with public accounting expertise who previously held senior roles in corporate finance, accounting and financial reporting as a corporate controller and Senior Director, Finance at Prometheus Laboratories Inc. and who was a senior financial auditor at Ernst & Young LLP.

Our executive team, key personnel and board of directors are supported by our scientific advisory board members, who are renowned pioneers in the *micro*RNA field:

- Ø David Baltimore, Ph.D., Chairman of our scientific advisory board and Professor of Biology at the California Institute of Technology, received the Nobel Prize in 1975 and is highly regarded as a pioneer in virology and immunology, with his current research investigating the role of *microRNAs* in immunity. Dr. Baltimore is also a member of our board of directors.

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- Ø David Bartel, Ph.D., Professor of Biology at the Massachusetts Institute of Technology and the Whitehead Institute for Biomedical Research and an investigator at the Howard Hughes Medical Institute, studies *microRNA* genomics, target recognition and regulatory functions.

- Ø Gregory Hannon, Ph.D., Professor at the Cold Spring Harbor Laboratory and an investigator at the Howard Hughes Medical Institute, has identified and characterized many of the major biogenesis and effector complexes for *microRNA* biology.

- Ø Markus Stoffel, M.D., Ph.D., Professor of Metabolic Diseases at the Swiss Federal Institute of Technology, is focused on *microRNA* research and the regulation of glucose and lipid metabolism.

- Ø Thomas Tuschl, Ph.D., Professor and Head of the Laboratory for RNA Molecular Biology at the Rockefeller University and an investigator at the Howard Hughes Medical Institute, discovered many of the mammalian *microRNA* genes and has developed methods for characterization of small RNAs.

THE POTENTIAL OF *microRNA* BIOLOGY

RNA plays an essential role in the process used by cells to encode and translate genetic information from DNA to proteins. RNA is comprised of subunits called nucleotides and is synthesized from a DNA template by a process known as transcription. Transcription generates different types of RNA, including messenger RNAs that carry the information for proteins in the sequence of their nucleotides. In contrast, *microRNAs* are small RNAs that do not code for proteins, but rather are responsible for regulating gene expression by affecting the translation of target messenger RNAs. This is achieved when the *microRNA* binds with its messenger RNA targets and blocks cell machinery, called ribosomes, from translating them into proteins, as shown below.

Step 1. *microRNAs* are transcribed from DNA in the nucleus and exported to the cytoplasm.

Step 2. In the cytoplasm, *microRNAs* associate with the RNA-induced silencing complex, or RISC.

Step 3. The *microRNA* in RISC targets specific messenger RNAs.

Step 4. The *microRNA* interaction with its target messenger RNAs blocks translation into proteins.

RNA therapeutics are drugs designed to specifically target RNA. The field of RNA therapeutics consists of various technologies including antisense therapeutics, RNAi therapeutics and *microRNA* therapeutics:

Antisense therapeutics Antisense therapeutics are small oligonucleotides that target RNA through hybridization, a specific type of binding, and modulate the function of the targeted RNA. There are at least 12 known antisense mechanisms that can be exploited once an antisense drug binds to its target RNA. One of our founding companies, Isis, is leading the discovery and development of antisense therapeutics with over 25 drugs currently in development. Isis' most advanced drug, KYNAMRO ,

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which is partnered with Genzyme Corporation, a subsidiary of Sanofi, was approved by the FDA in January 2013 for the treatment of homozygous familial hypercholesterolemia. The majority of Isis' antisense drugs in development bind to the specific RNAs of a particular gene, and ultimately inhibit or alter the expression of the protein encoded in the target gene.

RNAi therapeutics RNAi therapeutics are RNA-like oligonucleotides that harness RNAi, a powerful and natural biologic mechanism that was awarded the 2006 Nobel Prize for Physiology or Medicine. RNAi therapeutics are rationally designed to silence disease causing genes. The molecule that mediates RNAi, small interfering RNA, or siRNA, binds with a cellular complex known as the RNA-induced silencing complex, or RISC. The siRNA within RISC is processed into single-stranded RNA that targets a specific messenger RNA and promotes its degradation through cleavage. In this way, RNAi therapeutics can be used to target specific disease causing genes. One of our founding companies, Alnylam, has shown human proof-of-concept in clinical trials with multiple RNAi drug candidates.

microRNA therapeutics microRNA therapeutics are single- or double-stranded RNA-like oligonucleotides that are chemically modified and target specific microRNAs. Single-stranded microRNA therapeutics, or anti-miRs, are designed to bind and inhibit specific microRNAs that have been up-regulated in diseases as shown in the figure below. Double-stranded microRNA therapeutics, or miR-mimics, are designed to replace the activity of specific microRNAs that have been down-regulated in disease. In this way, microRNA therapeutics can be used to modulate specific microRNA targets and regulate entire biological pathways.

Step 1. microRNA expression is up-regulated in disease such that a specific microRNA is produced in excess amounts.

Step 2. The up-regulated microRNA targets messenger RNAs, resulting in lower levels of key proteins.

Step 3. The anti-miR therapeutic is delivered to the diseased cell and binds to the up-regulated microRNA, resulting in the elimination of excess microRNA.

Step 4. Use of the anti-miR therapeutic therefore restores the normal function of microRNA biology in the cell and corrects the disease.

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microRNA THERAPEUTICS AS A NEW CLASS OF DRUGS

We believe that *microRNA* therapeutics have the potential to become a new and major class of drugs with broad therapeutic application. There are several reasons why *microRNA* therapeutics have transformative potential, some of which are listed below.

microRNAs represent a new drug target space *microRNAs* are a recent discovery in biology and, up until now, have not been a focus of pharmaceutical research. Traditional drug classes cannot be used to target *microRNAs* because they are typically designed to bind and inhibit proteins, not RNA molecules. *microRNA* therapeutics provide the capability to very specifically modulate *microRNAs* and allow access to this new target space.

microRNAs are dysregulated in a broad range of diseases *microRNAs* play a critical role in regulating biological pathways by controlling the translation of many target genes. More than 500 *microRNAs* have been identified to date in humans, each of which are believed to interact with a specific set of genes that control key aspects of cell biology. Thus the improper balance, or dysregulation, of *microRNAs* has been directly linked to numerous diseases, including cancer, diabetes, congestive heart failure, viral infections and macular degeneration.

microRNA therapeutics target entire disease pathways *microRNAs* are naturally occurring molecules that have evolved to regulate gene networks responsible for entire biological pathways. Because of this unique attribute, the use of *microRNA* therapeutics may allow for more effective treatment of complex multi-factorial diseases in which the entire disease pathway can be addressed.

microRNA therapeutics can be produced with efficient rational design Traditional drug classes, like small molecules, usually require screening of thousands of potential compounds to identify prospective leads. Given that *microRNAs* are a short sequence of nucleotides and that the corresponding sequence of the mirror image anti-miR is also known, *microRNA* therapeutics allow for a more efficient rational drug design process.

microRNA therapeutics may be synergistic with other therapies Because of their completely different mechanisms of action, *microRNA* therapeutics and traditional drugs can be synergistic. In certain fields, such as cancer and infectious diseases, physicians typically treat patients with combinations of drugs that have different mechanisms in the hope that there will be complementary activity.

OUR *microRNA* PRODUCT PLATFORM

We are the leading company in the field of *microRNA* therapeutics dedicated to pioneering a new paradigm in treating serious diseases. We believe we have assembled the leading position in the *microRNA* field, including expertise in *microRNA* biology and oligonucleotide chemistry, broad intellectual property estate, key opinion leaders and disciplined drug discovery and development processes. We refer to these assets as our *microRNA* product platform. Backed by our founding companies, Alnylam and Isis, we are uniquely positioned to leverage oligonucleotide technologies that have been proven in clinical trials. Central to achieving our goals is the know-how that we have accumulated in oligonucleotide design and how the specific chemistries behave in the clinical setting.

We view the following as providing a competitive advantage for our *microRNA* product platform:

Ø a mature platform selectively producing multiple development candidates advancing to the clinic;

Ø scientific advisors who are pioneers in the *microRNA* field, including the first researcher to discover *microRNAs* in humans;

Ø

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access to proven RNA therapeutic technologies through our founding companies, as well as approximately 900 patents and patent applications relating to oligonucleotide technologies;

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Ø a leading *microRNA* intellectual property estate with access to over 170 *microRNA* patents and patent applications covering compositions and therapeutic uses;

Ø development expertise and financial resources provided by our three major strategic alliances with AstraZeneca, GSK and Sanofi; and

Ø over 30 academic collaborations that help us identify new *microRNA* targets and support our early stage discovery efforts.

The disciplined approach we take to the discovery and development of *microRNA* therapeutics is as important as the assets assembled to execute on our plans. Beginning with how we evaluate a therapeutic opportunity and followed by the identification of a specific *microRNA* target, its validation and optimization of the development candidates that will go into clinical trials, each is the subject of proprietary standards and rules that increase our probability of technical success. Our disciplined approach is based on the following four steps:

Step 1 - Evaluation of microRNA therapeutic opportunities

The initiation of our *microRNA* discovery and development efforts is based on rigorous scientific and business criteria, including:

Ø existence of significant scientific evidence to support the role of a specific *microRNA* in a disease;

Ø availability of predictive preclinical disease models to test our *microRNA* development candidates;

Ø ability to effectively deliver anti-miRs to the diseased cells or tissues; and

Ø existence of a reasonable unmet medical need and commercial opportunity.

The advantage of our evaluation criteria is that they can be applied to a broad range of *microRNA* targets, allowing us to generate a focused portfolio of discovery programs that we believe have a high probability of clinical and commercial success.

Once we have decided to initiate a new program, we use a disciplined approach to identify novel *microRNA* targets, validate such novel *microRNA* targets and use our proprietary methodologies to optimize lead *microRNA* development candidates for IND-enabling studies and subsequent clinical development.

Step 2 - Identification of microRNA targets

We have developed a significant understanding and know-how of human *microRNA* biology and the biological pathways that are regulated by *microRNAs*. We identify *microRNA* targets through bioinformatic analysis of public and proprietary *microRNA* expression profiling data sets from samples of diseased human tissues. The analysis of such data sets can immediately highlight a potential role for specific *microRNAs* in the diseases being studied. Further investigation of animal models that are predictive of human diseases in which those same *microRNAs* are also dysregulated provides additional data to support a new program. We have applied this strategy successfully in our existing programs and we believe that this approach will continue to help us identify clinically relevant *microRNA* targets.

Step 3 - Validation of microRNA targets

Our validation strategy is based on two distinct steps. First, using genetic tools, we determine whether up-regulation of the *microRNA* in healthy animals can create the specific disease state and inhibition of the *microRNA* can lead to a therapeutic benefit. Second, using animal models predictive of human diseases, we determine whether pharmacological modulation of the up-regulated *microRNA* target with our anti-miRs can also lead to a therapeutic benefit. This validation process enables us to prioritize the best *microRNA* targets that appear to be key drivers of diseases and not simply correlating markers.

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Step 4 - Optimization of microRNA development candidates

We have developed a proprietary process that allows us to rapidly generate an optimized development candidate following the identification and validation of a *microRNA* target. Unlike traditional drug classes, such as small molecules, in which thousands of compounds must be screened to identify prospective leads, the fact that anti-miRs are mirror images of their target *microRNAs* allows for a more efficient rational design process. The optimization process incorporates our extensive knowledge base around oligonucleotide chemistry and anti-miR design to efficiently synthesize a starting pool of rationally designed anti-miRs to be evaluated in a series of proven assays and models that quickly allow us to:

- ∅ identify our most effective anti-miRs in mechanistic cell-based assays;

- ∅ evaluate the activity of our anti-miRs in preclinical animal models that are predictive of human diseases; and

- ∅ eliminate anti-miRs that may trigger undesirable effects.

We also enhance our anti-miRs for distribution to the tissues where the specific *microRNA* target is causing disease. For example, we employ a conjugate approach to successfully deliver anti-miRs to target tissues and achieve optimized cellular uptake. Our conjugate platform includes several receptor-mediated chemistries such as triantennary N-acetylgalactosamine, or GalNAc, conjugates. We have demonstrated the ability to achieve optimized delivery to cells in the liver with both intravenous and subcutaneous administration of GalNAc conjugates in multiple species and with multiple targets.

We believe that our optimization process provides us with a competitive advantage in the discovery and development of *microRNA* therapeutics. The lessons we learn from one program can be applied to other programs at an earlier stage in our portfolio, leading to potential acceleration of the advancement of those programs towards IND-enabling activities and future clinical development.

***microRNA* BIOMARKERS**

Through our *microRNA* target identification and validation efforts we have developed proprietary technologies for *microRNA* profiling and analysis of human clinical samples such as tissue biopsies. More recently, *microRNAs* have been detected in bodily fluids such as blood, and emerging data generated by us and others have demonstrated that *microRNA* signatures in blood can mimic the expression profile observed in disease tissues.

The identification of dysregulated *microRNAs* from various human tissues and blood helps us identify and validate potential *microRNA* targets for therapeutic development. Equally important, such *microRNAs* may become biomarkers that can be used to select optimal patient segments for our clinical trials. We expect this personalized approach to clinical development to result in a significantly improved risk-benefit ratio in the appropriate patient populations and plan to implement the strategy in our programs.

We believe that *microRNA* biomarkers in the blood are of significant value and provide opportunities to develop companion diagnostics for any drugs that we may successfully develop and drugs developed by other companies. In August 2012, we entered into an agreement with Biogen Idec MA Inc. to collaborate on *microRNA* biomarkers for multiple sclerosis.

OUR INITIAL DEVELOPMENT CANDIDATES

We have demonstrated in at least 20 preclinical animal models that are predictive of human diseases that the inhibition of up-regulated *microRNA* targets using anti-miRs can modulate entire biological pathways, returning diseased cells to their healthy state. Based on the

extensive preclinical data we have

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generated to date, we believe that our *microRNA* product platform has the potential to provide significant therapeutic benefit in a broad range of human diseases. We have chosen to focus our initial efforts on select therapeutic areas with unmet medical needs including HCV, oncology and metabolic diseases. We have identified and validated several *microRNA* targets that play a role in these areas.

Our *microRNA* development candidates target miR-122 in HCV, miR-21 and miR-221 in hepatocellular carcinoma, miR-21 in kidney fibrosis, miR-33 in atherosclerosis and miR-10b in GBM.

RG-101 targeting miR-122 in hepatitis C virus infection

Market opportunity:

Hepatitis C is a result of a hepatocyte specific infection induced by the virus known as HCV. Chronic HCV may lead to significant liver disease, including chronic active hepatitis, cirrhosis, and hepatocellular carcinoma. According to the World Health Organization, up to 170 million people are chronically infected with HCV worldwide, and more than 350,000 people die from HCV annually. The CDC estimates that there are currently approximately 3.2 million persons infected with HCV in the United States.

Current treatments:

The current standard of care for HCV is a combination of injectable pegylated interferon-alfa, oral ribavirin and an oral protease inhibitor. Two protease inhibitors were approved for such combination treatment in 2011: telaprevir (marketed as Incivek® in North America by Vertex Pharmaceuticals Incorporated, as Incivo® in Europe by Johnson & Johnson and as TELAVIC® in Japan by Mitsubishi Tanabe Pharma Corporation) and boceprevir (marketed as Victrelis® by Merck & Co, Inc.). All-oral combination therapies that include new direct-acting antivirals are being developed and in clinical trials appear to achieve significant improvements in efficacy, tolerability and treatment duration. However, unmet needs will likely remain for certain segments of the HCV patient population, including those who have not responded at all to previous therapies and those who have relapsed following previous therapies.

Our program:

We have nominated RG-101 as our first *microRNA* clinical candidate for the treatment of HCV. RG-101, which is wholly-owned by us, is a hepatocyte-targeted GalNAc-conjugated anti-miR targeting *microRNA*-122, or miR-122. miR-122 is the most abundant *microRNA* in liver hepatocytes and HCV has evolved to utilize it as a viral replication factor such that the stability and propagation of HCV is dependent on the interaction of miR-122 and the HCV genome. Clinical trials have shown that inhibiting the miR-122 target with an oligonucleotide administered weekly can result in a three-fold logarithmic viral load reduction observed after five weekly doses in HCV patients.

We believe that RG-101 has several attractive properties that make our approach to treating HCV unique and differentiated among the current therapies:

- Ø RG-101 employs a unique mechanism of action by targeting a host factor. We believe by targeting a host factor there is a lower likelihood for the virus to develop resistance, which has been observed with direct-acting antivirals. In addition, because of its unique mechanism of action, we believe that RG-101 will have minimal to potentially no negative drug-drug interactions with current and future direct-acting antiviral treatment regimens.
- Ø RG-101 has the potential to be a pan-genotypic agent. The miR-122 binding site of the HCV genome is one of the most highly conserved regions across all HCV genotypes. Therefore, RG-101 is expected to be active against all viral genotypes. In preclinical studies, RG-101 has demonstrated activity across a broad spectrum of HCV genotypes and against the most commonly identified HCV mutations detected in patients being treated with direct-acting antiviral therapy.

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Ø RG-101 has a convenient dosing regimen. The pharmacological activity of RG-101 has been shown in animal models to be sustained for more than 28 days after a single dose administration. These data suggest the feasibility of a convenient subcutaneous dosing regimen, to be administered during a patient's regularly scheduled physician visit.

Ø RG-101 is potent and has a favorable safety profile to date. In pharmacology studies using a human liver chimeric mouse model to assess potency against HCV, RG-101 demonstrated significant lowering of viral titer load. These experiments are helping us refine the initial starting dose for clinical trials in humans and assess the therapeutic index. Further, we did not identify any adverse effects that would preclude the development of RG-101 for the treatment of HCV.

Given its attractive properties and preclinical data demonstrated to date, we believe that RG-101 may be an attractive agent to add to existing therapeutic regimens. We currently plan to develop RG-101 as a key component of an HCV combination regimen for patients who have failed, or are intolerant of, the current standard of care and specific patient populations such as HCV/HIV co-infection. In the near term, we plan to study RG-101 as monotherapy in healthy subjects and in HCV patients in Phase 1 clinical trials. We anticipate being able to evaluate the ability of a single dose of RG-101 to reduce viral load in HCV patients within the first year of the development program. If these clinical trials are successful, we expect to study RG-101 in Phase 2 clinical trials, in which we will focus primarily on demonstrating the efficacy of RG-101 in combination with other HCV therapeutics in patients who have failed other HCV treatments and in specific patient populations.

miR-21 and miR-221 for hepatocellular carcinoma

Market opportunity:

Hepatocellular carcinoma, or HCC, is the most prevalent form of liver cancer and is the most common cancer in some parts of the world, with more than 1 million new cases diagnosed each year worldwide according to the National Cancer Institute. According to the World Health Organization, liver cancer is the third leading cause of cancer deaths worldwide. According to recent reports from the Centers for Disease Control, or the CDC, HCC rates in the United States are increasing with common risk factors including alcohol consumption, metabolic syndrome and type 2 diabetes.

Current treatments:

Patients diagnosed with HCC have poor prognosis with a relatively low five-year survival rate of approximately 10%. Treatment options include surgical resection, transplantation and chemoembolization (delivery of drug directly to the tumor through a catheter). The only systemic drug therapy approved for the treatment of unresectable HCC is the multi-kinase inhibitor sorafenib (co-marketed by Bayer AG and Onyx Pharmaceuticals, Inc. as Nexavar®), which has been shown to be poorly tolerated and provides a 2.8-month overall survival benefit.

Our programs:

miR-21 is one of the most validated *microRNA* targets in oncology, with numerous scientific publications suggesting that miR-21 plays an important role in the initiation and progression of cancers including liver, kidney, breast, prostate, lung and brain. Similarly, miR-221 has been identified to be upregulated in multiple cancers including liver, kidney, prostate, brain, thyroid, ovarian, and breast cancer. In addition there is genetic evidence that links miR-21 and miR-221 to HCC. We are developing oncology anti-miRs targeting miR-21 and miR-221, which we refer to as anti-miR-21 and anti-miR-221, for HCC because our analysis of liver biopsies from HCC patients has shown that miR-21 and miR-221 are up-regulated relative to surrounding normal liver tissues. We have also shown that miR-21 and miR-221 levels are increased in a

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genetically engineered mouse that develops HCC, thereby enabling us to test anti-miR-21 and anti-miR-221 in a preclinical model that mimics the human disease. Testing anti-miR-21 in this mouse model of HCC showed delayed tumor progression resulting in a survival rate of 80% at the study endpoint (compared to a 0% survival rate for the control group).

As part of our strategic alliance with Sanofi, we anticipate entering into an additional agreement under which we plan to nominate an anti-miR-21 development candidate for the treatment of HCC and file an IND and to pursue clinical development of such candidate together with Sanofi. We intend to independently file an IND, develop and commercialize an anti-miR-221 development candidate for the treatment of HCC.

miR-21 in kidney fibrosis

Market opportunity:

Fibrosis is the harmful build-up of excessive fibrous tissue leading to scarring and ultimately the loss of organ function. Fibrosis can affect any tissue and organ system, and is most common in the heart, liver, lung, peritoneum, and kidney. The fibrotic scar tissue is made up of extracellular matrix proteins. Fibrosis is widespread in industrialized nations and regularly leads to organ failure, contributing significantly to morbidity and mortality. Kidney fibrosis is the principal process underlying the progression of chronic kidney disease, or CKD, and ultimately leads to end-stage renal disease, a devastating disorder that requires dialysis or kidney transplantation. According to the CDC, more than 20 million people in the United States have CKD with over 100,000 patients starting treatment for end-stage renal disease annually. The National Kidney Foundation estimates that the annual cost of treating kidney failure in the U.S. is approximately \$23.0 billion.

Current treatments:

Currently there are no approved drugs for fibrosis in the United States. In Europe, Asia and Japan there is only one approved therapy, pirfenidone (marketed as Esbriet® in Europe by InterMune, Inc. and as Pirespa in Japan by Shionogi & Co.), for lung fibrosis termed idiopathic pulmonary fibrosis, or IPF (scarring of the lung). The clinical results for pirfenidone concluded that it was able to improve progression-free survival and, to a lesser extent, improve pulmonary function allowing the approval for the treatment of mild-to-moderate IPF.

Our program:

Our lead program for fibrosis targets miR-21, which has been found in human tissue and animal models to be up-regulated in multiple fibrotic conditions. We and our academic collaborators have shown that either the absence of miR-21 or the inhibition of miR-21 reduces fibrosis in multiple preclinical models of organ fibrosis, including kidney and heart. We have also shown that anti-miR-21 treatment administered to preclinical animal models that are predictive of human kidney fibrosis can reduce fibrosis by up to 50%. In addition, the effects of our anti-miR-21 have been associated with improved kidney function and decreased mortality associated with injury to the kidney. Based on these data, we believe that anti-miR-21 could have therapeutic benefit in patients with CKD and kidney fibrosis.

As part of our strategic alliance with Sanofi, we anticipate entering into an additional agreement under which we will nominate an anti-miR-21 clinical candidate and file an IND initially for the treatment of Alport's syndrome, an orphan genetic disorder caused by mutations in collagen synthesizing genes, that leads to kidney fibrosis.

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miR-10b in glioblastoma

Market opportunity:

GBM, also known as glioblastoma or grade IV astrocytoma, is an aggressive tumor that forms from abnormal growth of glial (supportive) tissue of the brain. According to the New England Journal of Medicine, GBM is the most prevalent form of primary brain tumor and accounts for approximately 50% of the 22,500 new cases of brain cancer diagnosed in the United States each year. Treatment options are limited and expected survival is little over one year. GBM is considered a rare, or orphan, disease by the FDA and EMA.

Current treatments:

The standard of care for GBM involves surgical removal of the tumor followed by radiotherapy and chemotherapy with temozolomide (marketed as Temodar[®] and Temodal[®] by Merck & Co., Inc.), a non-specific cytotoxic agent approved for newly diagnosed GBM. Temozolomide has been shown to be poorly tolerated and provides a 2.5-month overall survival benefit. In addition, bevacizumab (marketed as Avastin[®] by Genentech Inc. and F. Hoffman-La Roche Ltd.) was granted accelerated approval in 2009 for the treatment of GBM with progressive disease in adult patients following prior therapy.

Our program:

Through proprietary bioinformatic analysis of academic laboratory profiling studies of GBM tumors, we have identified specific dysregulated *microRNAs* in distinct subtypes of the disease. Our analysis found that miR-10b is highly overexpressed, up to eight-fold, in a particular GBM patient population called the proneural subtype. Our findings show that treatment of GBM cell lines with anti-miRs targeting miR-10b, which we refer to as anti-miR-10b, reduces proliferation by blocking cell cycle progression and triggering cell death. In addition, we have shown in preclinical animal models of GBM, that direct injection into the tumor and spinal fluid achieves appropriate tissue delivery of anti-miRs for potential therapeutic effects.

We have a research collaboration with the Samsung Biomedical Research Institute to assist us in testing our anti-miR-10b development candidates in specialized preclinical models that mimic human brain cancer. In addition, we have funding support from Accelerate Brain Cancer Cure, or ABC², a non-profit organization dedicated to accelerating therapies for brain cancer patients.

We intend to independently file an IND, develop and commercialize our anti-miR-10b development candidate for the treatment of GBM. Following the initiation of a Phase 1 clinical trial in patients with recurrent GBM to assess the safety and tolerability of our anti-miR-10b development candidate under the IND, we anticipate filing for orphan drug status for this development candidate. Upon identification of the maximum tolerated dose, we plan to enroll an expanded cohort using our *microRNA* biomarker strategy to identify patients with up-regulated miR-10b to further assess safety and evaluate efficacy on a preliminary basis in accordance with Response Criteria in Solid Tumors, or RECIST, measurement guidelines.

miR-33 in atherosclerosis

Market opportunity:

Atherosclerosis is the build up of plaque that occurs when cholesterol and inflammatory cells accumulate in blood vessels. These plaques can rupture, leading to slowing or blockage of blood flow and ultimately resulting in a heart attack or stroke. Scientific research has shown a strong correlation between high cholesterol levels and cardiovascular disease which, according to the CDC, is the leading cause of death in the United States.

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Current treatments:

Most patients with atherosclerosis have high levels of a particular type of cholesterol particle known as LDL-C. The current standard of care is treatment with a class of drugs called statins that inhibit the production of cholesterol in the liver and therefore reduce the amount of LDL-C in circulation that might end up in plaques. However, such an approach has been shown to reduce the risk of a future heart attack or stroke by only approximately 30-40%. Recently, the scientific community has focused on another cholesterol particle known as HDL-C because it has been shown to remove cholesterol from plaques and transport it to the liver for excretion from the body.

Our program:

Our lead program for atherosclerosis targets miR-33, which has a unique mechanism of action for the management of cholesterol levels. The inhibition of miR-33 with our anti-miRs promotes reverse cholesterol transport, or RCT, which is the efflux of cholesterol from specific cholesterol-laden inflammatory cells called macrophages in atherosclerotic plaques. A natural consequence of enhancing RCT is an increase in the number of HDL-C particles that can remove cholesterol to the liver for excretion from the body. We are developing anti-miRs targeting miR-33, which we refer to as anti-miR-33. Treatment with anti-miR-33 in an atherosclerotic mouse model led to reduction in arterial plaque size by 35% and treatment in non-human primates increased circulating levels of HDL-C by 50%. By enhancing RCT, anti-miR-33 differs from other emerging therapeutic strategies that focus only on raising HDL-C in circulation.

In addition to direct benefits on atherosclerosis, treatment with anti-miR-33 in a preclinical study increased the breakdown of lipids, such as fatty acids, and enhanced signaling through the insulin receptor. These findings suggest that the inhibition of miR-33 could have additional benefits in other aspects of the metabolic syndrome, such as non-alcoholic steatohepatitis (fatty liver disease) and type-2 diabetes. We expect anti-miR-33 to be developed as a treatment for atherosclerosis, initially for patients at high-risk of recurrent cardiovascular events, such as heart attack.

As part of our strategic alliance with AstraZeneca, we, in consultation with AstraZeneca, plan to nominate an anti-miR-33 development candidate for the treatment of atherosclerosis and file an IND. We expect that AstraZeneca will initiate and fund Phase 1 clinical trials under the IND, according to a clinical development plan designed in consultation with us.

OUR STRATEGY

We are building the leading biopharmaceutical company focused on the discovery and development of first-in-class, targeted drugs based on our proprietary *microRNA* product platform. The key elements of our strategy are:

- Ø *Rapidly advance our initial programs into clinical development.* We are currently optimizing our proprietary and partnered anti-miRs for development candidate selection. Under our Road to the Clinic strategy, we have nominated our proprietary compound, RG-101, in HCV as our first clinical candidate and expect to submit our first IND, or equivalent foreign regulatory filing, for RG-101 in the first half of 2014. We anticipate that we will nominate a second clinical candidate by the end of 2013.
- Ø *Focus our resources on developing drugs for niche indications or orphan diseases.* We believe that *microRNA* therapeutics have utility in almost every disease state as they regulate pathways, not single targets. We intend to focus on proprietary product opportunities in niche therapeutic areas where the development and commercialization activities are appropriate for our size and financial resources.

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- Ø *Selectively form strategic alliances to augment our expertise and accelerate development and commercialization.* We have established strategic alliances with AstraZeneca, GSK and Sanofi and we will continue to seek partners who can bring therapeutic expertise, development and commercialization capabilities and funding to allow us to maximize the potential of our *microRNA* product platform.

- Ø *Selectively use our microRNA product platform to develop additional targets.* We have identified several other *microRNA* targets with potential for therapeutic modulation and will apply our rigorous scientific and business criteria to develop them.

- Ø *Develop microRNA biomarkers to support therapeutic product candidates.* We believe that *microRNA* biomarkers may be used to select optimal patient segments in clinical trials, to develop companion diagnostics, and to monitor disease progression or relapse. We believe these *microRNA* biomarkers can be applied toward drugs that we develop and drugs developed by other companies, including small molecules and monoclonal antibodies.

- Ø *Maintain scientific and intellectual leadership in the microRNA field.* We will continue to conduct research in the *microRNA* field to better understand this new biology and characterize the specific mechanism of action for our future drugs. This includes building on our strong network of key opinion leaders and securing additional intellectual property rights to broaden our existing proprietary asset estate.

OUR STRATEGIC ALLIANCES AND COLLABORATIONS

Our goal is to discover and develop *microRNA* therapeutics. To access the substantial funding and expertise required to develop and commercialize *microRNA* therapeutics, we have formed and intend to seek other opportunities to form strategic alliances with pharmaceutical companies who can augment our industry leading *microRNA* expertise. To date, we have focused on forging a limited number of significant strategic alliances with leading pharmaceutical partners and academic laboratories where both parties contribute expertise to enable the discovery and development of potential *microRNA* therapeutics.

Under our existing strategic alliances with AstraZeneca, GSK and Sanofi, we are eligible to receive up to approximately \$1.3 billion in milestone payments upon successful commercialization of *microRNA* therapeutics for the eleven programs contemplated by our agreements. These payments include up to \$42.0 million upon achievement of preclinical and IND milestones, up to \$272.0 million upon achievement of clinical development milestones, up to \$305.0 million upon achievement of regulatory milestones and up to \$670.0 million upon achievement of commercialization milestones.

Our strategic alliance with GlaxoSmithKline

In April 2008, we entered into a product development and commercialization agreement with Glaxo Group Limited, an affiliate of GlaxoSmithKline plc, or GSK. Under the terms of the agreement, we agreed to develop four programs of interest to GSK in the areas of inflammation and immunology and granted to GSK an option to obtain an exclusive worldwide license to develop, manufacture and commercialize products in each program. We are responsible for the discovery, optimization and development of anti-miR product candidates in each program through proof-of-concept, defined as the achievement of relevant efficacy and safety endpoints in the first clinical trial designed to show efficacy, safety and tolerability, unless GSK chooses to exercise its option at an earlier stage. Upon GSK exercising its option with respect to a particular program and paying an option exercise fee, we will grant GSK an exclusive worldwide license to develop drugs under the selected program, and GSK will thereafter be responsible for all development, manufacturing and commercialization activities and costs. As of the date of the agreement, GSK had pre-selected two *microRNA* alliance targets. In February 2010, we and GSK

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expanded the alliance to include miR-122 for the treatment of HCV. In June 2013, we amended our agreement with GSK to specify that RG-101 is fully owned by us and that miR-122 will remain a collaboration target under the agreement. We will be solely responsible for the development, manufacture and commercialization of RG-101 and GSK has no rights to this compound.

Upon entering into the agreement, we received an upfront payment of \$15.0 million as an option fee, and GSK loaned \$5.0 million to us under a convertible note. In connection with the expansion of the alliance to include miR-122 for the treatment of HCV, in February 2010, GSK made an upfront payment to us of \$3.0 million and loaned an additional \$5.0 million to us pursuant to a second convertible note. The notes were amended and restated in July 2012 and upon closing of our initial public offering, the principal and accrued interest of one note was converted to 1,447,037 shares of our common stock. The note that did not automatically convert upon the initial public offering was restated in October 2012 and accrues interest at 3.297% with an adjusted face amount equal to the principal and accrued interest as of the completion of our initial public offering, which totaled approximately \$5.4 million, and will mature in October 2015. At GSK's option, this note is convertible into shares of our common stock at any time prior to the maturity date with a conversion equal to the quotient of all outstanding principal and interest divided by the initial public offering price of \$4.00 per share. Under our strategic alliance with GSK, we earned a \$500,000 milestone payment in each of May 2009 and July 2011. We are eligible to receive up to \$144.5 million in preclinical, clinical, regulatory and commercialization milestone payments for each of the four *microRNA* programs under our alliance with GSK. We are also eligible to receive tiered royalties as a percentage of annual sales which can increase up to the low end of the 10 to 20% range. These royalties are subject to reduction upon the expiration of certain patents or introduction of generic competition into the market, or if GSK is required to obtain licenses from third parties to develop, manufacture or commercialize products under the alliance.

For each *microRNA* alliance target selected by GSK under the agreement, we commence a research program directed against such target under a research plan adopted by a joint committee to discover and optimize compounds that meet candidate selection criteria. On a program-by-program basis, GSK may exercise its option at any time on or before completion of the proof-of-concept trial. To exercise its option, GSK must pay us an option exercise fee, which varies depending on the stage of the program at which the option is exercised. Milestone payments payable by GSK are higher if GSK exercises its option upon completion of the proof-of-concept trial. Once a *microRNA* alliance target has been selected by GSK, neither party may work independently or with a third party on a *microRNA* compound designed to modulate an alliance target. In addition, during the research term, neither we nor our affiliates may work independently or with a third party on any compound that is designed to modulate an alliance target.

If GSK does not exercise its option, or ceases development after exercising its option with respect to a particular program, we will have all rights to develop or commercialize product candidates under the program (including the right to sublicense these rights to a third party) at our sole expense. In the event the product is eventually commercialized, GSK will be entitled to reverse royalties as a percentage of net sales, subject to certain caps.

Either party may terminate the agreement upon written notice in the event of the other party's material breach, including the failure to comply with such party's diligence obligations, that remains uncured for 90 days. GSK has the unilateral right to terminate the agreement in its entirety or on an alliance target basis upon 90 days' prior written notice to us.

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Our strategic alliance with Sanofi

Sanofi collaboration and license agreement

In June 2010, we entered into a collaboration and license agreement with Sanofi, which we subsequently amended, restated and superseded in July 2012. Under the terms of the agreement, we have agreed to collaborate with Sanofi to develop and commercialize licensed compounds targeting four *microRNA* alliance targets initially focused in the field of fibrosis. The agreement specified that miR-21 would be the first alliance target in the field of fibrosis and we granted Sanofi an exclusive worldwide license to develop and commercialize products under the alliance. The July 2012 amended and restated agreement expanded the alliance to include potential *microRNA* therapeutics in oncology.

Under the terms of the agreement, we have agreed to use commercially reasonable efforts to provide Sanofi with validated *microRNA* targets and are responsible for conducting all research and compound manufacturing activities until acceptance of an IND. After acceptance of the IND, Sanofi will assume all costs, responsibilities and obligations for further development and commercialization.

Under the terms of the agreement, we received an upfront payment of \$25.0 million which was allocated to the research programs. In addition, Sanofi made a \$10.0 million equity investment in the company. We also received \$5.0 million for one year of research and development funding. Subsequently, we received \$5.0 million for research and development funding following each of the first and second anniversaries of our entry into the agreement in June 2010. The research term ended in June 2013 per the terms of the agreement and therefore we have no further research obligations under the agreement. Under the terms of the agreement, Sanofi may continue development of any licensed compounds. We are also entitled to receive preclinical, clinical, regulatory and commercialization milestone payments of up to \$213.0 million in the aggregate for all alliance product candidates. In addition, we are entitled to receive royalties based on a percentage of net sales which will range from the mid-single digits to the low end of the 10 to 20% range, depending upon the target and the volume of sales.

Sanofi may terminate the agreement in full or on a product-by-product basis by giving 30 days prior written notice to us. Either party may also terminate the agreement for a material breach by the other party which remains uncured after 120 days notice of such breach, except that we may not exercise this termination right until after the expiration of the research term if Sanofi is in breach of its obligations to use commercially reasonable efforts. In the event a program or the agreement is terminated by Sanofi, the rights to develop and commercialize product candidates in the terminated programs (including the right to sublicense these rights to a third party) returns to us. If we sublicense the rights to a third party, we will be required to pay a percentage of sublicense revenues to Sanofi in the low end of the 10 to 20% range, and if we commercialize a product on our own, we will be required to pay royalties in the low single digits to Sanofi as a percentage of net sales.

In April 2013, we entered into a letter agreement with Sanofi to extend the time period available to Sanofi to extend its option to extend the research term under the agreement. The original research term for our strategic alliance with Sanofi expired in June 2013, upon which we and Sanofi entered into an option agreement pursuant to which we have the exclusive right to negotiate with Sanofi to enter into a co-development and commercialization agreement for an anti-miR-21 for the treatment of oncology indications and Alport's disease through December 2013 and pursuant to which we granted Sanofi an exclusive right to negotiate with us to enter into a development and license agreement for the co-development and commercialization of certain of our unencumbered *microRNA* programs through December 2013. In connection with the option agreement, Sanofi has agreed to pay us an upfront option fee of \$2.5 million, \$1.25 million of which is creditable against future payments payable by Sanofi to us.

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Sanofi non-exclusive technology alliance and option agreement

Concurrently with the collaboration and license agreement, we also entered into a non-exclusive technology alliance and option agreement with Sanofi. Under this agreement, Sanofi received an option for a broader *microRNA* technology license. Sanofi may exercise the option at any time until the date 30 days after the third anniversary of the agreement, subject to a one-time extension and payment of an extension fee.

If Sanofi exercises its option under this agreement, we will receive a payment of up to \$50.0 million, payable in installments. In return, Sanofi will receive a license to our *microRNA* product platform technology for research of *microRNA* compounds. The option also provides us with certain rights to participate in the development and commercialization of products. We are also entitled to receive a product-by-product milestone payment and royalties as a percentage of net sales in the low single digits for products commercialized by Sanofi.

Our strategic alliance with AstraZeneca

In August 2012, we entered into a collaboration and license agreement with AstraZeneca. Under the terms of the agreement, we have agreed to collaborate with AstraZeneca to identify, research and develop compounds targeting three *microRNA* alliance targets primarily in the fields of cardiovascular diseases, metabolic diseases and oncology and granted to AstraZeneca an exclusive, worldwide license to thereafter develop, manufacture and commercialize lead compounds designated by AstraZeneca in the course of the collaboration activities against the alliance targets for all human therapeutic uses. Under the terms of the agreement we are required to use commercially reasonable efforts to perform all research, development and manufacturing activities described in the research plan, at our cost, until the acceptance of an IND or the end of the research term, which extends until the fourth anniversary of the date of the agreement, and may be extended only by mutual written agreement of us and AstraZeneca. Following the earlier to occur of the acceptance of an IND in a major market or the end of the research term, AstraZeneca will assume all costs, responsibilities and obligations for further development, manufacture and commercialization of alliance product candidates. In April 2013, we and AstraZeneca amended the collaboration and license agreement to provide that we would undertake *microRNA* analysis of certain samples controlled by AstraZeneca in connection with miR-33 and another *microRNA* target. All results and inventions relating to the *microRNA* analysis of such clinical samples will be owned solely by AstraZeneca, but AstraZeneca granted us a perpetual, non-exclusive license to such results and inventions for our internal research and development purposes.

Under the terms of the agreement, we are entitled to receive an upfront payment of \$3.0 million. If all three targets are successfully developed and commercialized through pre-agreed sales targets we could receive milestone payments up to \$498.0 million, including up to \$5.0 million for preclinical milestones, up to \$123.0 million for clinical milestones, and up to \$370.0 million for commercialization milestones. In addition, we are entitled to receive royalties based on a percentage of net sales which will range from the mid-single digits to the low end of the 10 to 20% range, depending upon the product and the volume of sales, which royalties may be reduced in certain, limited circumstances.

Either party may terminate the agreement upon written notice to the other party provided within 20 business days after the end of the research term if no lead compound has been designated at that time. Either party may also terminate the agreement in the event of the other party's material breach which remains uncured for 40 business days following notice thereof (or 30 business days in the case of nonpayment). During the research term, AstraZeneca may terminate the agreement in its entirety or on a collaboration target-by-collaboration target basis at any time within 20 business days of our notice to AstraZeneca of the closing of a transaction that would result in a change of control. During the research term, AstraZeneca may also terminate the agreement in its entirety or on a collaboration target-by-

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collaboration target basis for any reason upon 60 business days prior written notice to us. Following the research term, AstraZeneca may terminate the agreement in its entirety or on a collaboration target-by-collaboration target basis for any reason upon 12 months prior written notice to us.

Concurrently with the collaboration and license agreement, we entered into a Common Stock Purchase Agreement, or CSPA, with AstraZeneca, pursuant to which we agreed to sell to AstraZeneca an aggregate of \$25.0 million of our common stock in a private placement concurrently with our initial public offering, at a price per share equal to the price at which we sold our common stock to the public in such initial public offering. In October 2012, in accordance with the CSPA, we sold AstraZeneca 6,250,000 shares of our common stock at a price per share of \$4.00. Further, the CSPA stipulated that AstraZeneca could not sell, transfer, make any short sale of, or grant any option for the sale of any common stock for a 365-day period following the effective date of our initial public offering.

Our collaboration with Biogen Idec

In August 2012, we entered into a collaboration and license agreement with Biogen Idec pursuant to which we and Biogen Idec have agreed to collaborate on *microRNA* biomarkers for multiple sclerosis, or MS. Under the terms of the agreement, we granted Biogen Idec an exclusive, royalty free, worldwide license to our interest in the collaboration intellectual property for the purpose of commercializing non-*microRNA* products for the treatment, diagnosis and prevention of MS and non-MS diseases and disorders. We also granted Biogen Idec an exclusive, royalty-free, worldwide license, with the right to sublicense, to our interest in the collaboration intellectual property (and a non-exclusive license to our background intellectual property) for the purpose of commercializing products for the diagnosis of MS. We also granted Biogen Idec a right of first negotiation on certain commercial transactions relating to *microRNA* products which utilize intellectual property developed during the collaboration. Pursuant to the terms of the agreement, in August 2012 we received an upfront payment of \$0.8 million. We can earn the following research milestones: \$0.25 million for identification of a *microRNA* biomarker; \$0.5 million for validation of the *microRNA* biomarker in a second independent sample set; and \$0.5 million upon the refinement of the *microRNA* biomarker signature from a longitudinal study of patient samples on MS therapy. In June 2013, we and Biogen amended the agreement to update the research plan and criteria for success. In June 2013 we and Biogen Idec entered into an amendment agreement which revised the terms with respect to the Phase 1 research plan and Phase 1 development milestones under the collaboration and license agreement.

Concurrently with the collaboration and license agreement, we entered into a note purchase agreement with Biogen Idec, pursuant to which we issued Biogen Idec a convertible promissory note in the principal amount of \$5.0 million. The \$5.0 million note plus accrued interest converted into 1,256,232 shares of our common stock upon the closing of our initial public offering in October 2012 at a conversion price of \$4.00 per share.

Either party may terminate the agreement upon the other party's material breach which remains uncured for 60 days following notice thereof. If the agreement is terminated in connection with a party's material breach, the non-breaching party will retain the license rights granted by the breaching party under the agreement, but all license rights granted by the non-breaching party to the breaching party will terminate. Each party may also terminate the agreement for convenience upon 30 days prior written notice to the other party, but in such case the terminating party will forfeit the license rights granted to it by the non-terminating party pursuant to the agreement, and the non-terminating party will retain the license rights granted by the terminating party.

Our strategic alliance with Alnylam and Isis

In September 2007, we entered into a license and collaboration agreement with Alnylam and Isis, which we subsequently amended, restated and superseded in January 2009, and further amended in June 2010 and

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October 2011. Under the agreement, we acquired an exclusive, royalty-bearing, worldwide license, with rights to sublicense, to patent rights owned or licensed by Alnylam and Isis to develop, manufacture and commercialize products covered by the licensed patent rights for use in *microRNA* compounds which are *microRNA* antagonists and *microRNA* therapeutics containing these compounds. In addition, we have certain rights to miR-mimics. Under the agreement, we granted to both Alnylam and Isis a license to practice our intellectual property developed by us to the extent that it is useful specifically to Alnylam's RNAi programs or Isis' single-stranded oligonucleotide programs, but not including *microRNA* compounds or therapeutics that are the subject of our exclusive licenses from Alnylam and Isis.

We are required to use commercially reasonable efforts to develop and commercialize licensed products under the agreement. We are required to notify Alnylam and Isis when a program reaches development stage (defined as initiation of good laboratory practices, or GLP, toxicology studies) and whether or not we intend to pursue the program. Under the agreement, both Alnylam and Isis have an option to assume the development and commercialization of product candidates in a program that we do not pursue. If neither Alnylam nor Isis exercises this option, we are required to use our best efforts to finalize a term sheet with a third party with respect to such program. In the event we are unable to complete a transaction with a third party, both Alnylam and Isis have a second opt-in option.

If an election is made by either Alnylam or Isis (but not both) to opt-in, such party will pay us a one-time fixed payment, the amount of which will depend on whether the first or the second opt-in option was exercised, with a higher amount due if the first opt-in option was exercised. Clinical and regulatory milestones are also payable to us in the event the opt-in election is exercised. Such milestones total \$64.0 million in the aggregate if the election is made during the first opt-in period or \$15.7 million in the aggregate if the election is made at the second opt-in period. Tiered royalties are payable to us as a percentage of net sales on all products commercialized by the opt-in party. These royalties range from the low to middle single digits depending upon the volume of sales. The opt-in party is also entitled to sublicense the development program to a third party. In such a case, we are also entitled to receive a percentage of the sublicense income received by the opt-in party. The percentage payable depends upon the point at which the opt-in party sublicenses the program and ranges from the low end of the 10 to 20% range to the high end of the 40 to 50% range. The opt-in party is only required to pay the higher of the clinical and regulatory milestones or the sublicense income received in any calendar quarter. The opt-in party is also responsible for all third party payments due under other agreements as a result of the development. In the event both Alnylam and Isis elect to opt-in during either opt-in period, the parties have agreed to work together to amend the development plan to continue development of the project, including funding of such project and assignment of roles and responsibilities.

In the event we or one of our strategic alliance partners continues with the development of a program, each of Alnylam and Isis are entitled to royalties as a percentage of net sales. For products that we independently commercialize, these royalties will be in the low single digits. For products commercialized by a third-party collaborator, the royalties will be either the same percentage of net sales as described above or, if the sublicense does not provide a specified level of royalties to us or upon our election, a percentage of the sublicense income received by us from the strategic alliance partner and a modified royalty. The modified royalty would be based upon the lower of the single digit percentage discussed above or one third of the royalty received by us after payments made by us to third parties for development, manufacture and commercialization activities under other agreements. In addition, if we sublicense rights to a collaborator, we will be required to pay to each of Alnylam and Isis a percentage of our sublicense income in the mid-single digits. We are also responsible for payments due to third parties under other agreements as a result of our development activities, including payments owed by Alnylam and/or Isis under their agreements.

Under the October 2011 amendment, Alnylam and Isis granted us the right to research *microRNA* mimics under the licensed intellectual property of Alnylam and Isis. In the event we develop a miR-mimic, we must

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first obtain approval from Alnylam and/or Isis, as applicable, and such approval is subject to the consent of applicable third parties, if any. No additional consideration will be owed by us to Alnylam or Isis for granting approval. We have the right to sublicense our research rights. We granted to both Alnylam and Isis a fully paid up, worldwide and exclusive license to any intellectual property developed by us and useful to their research programs and which are not *microRNA* antagonists or approved miR-mimics.

The agreement expires on the earlier of the cessation of development of the potential royalty-bearing products prior to the commercial sale of any such products anywhere in the world or following the first commercial sale of such products, the expiration of royalty obligations determined on a country-by-country and product-by-product basis.

OUR INTELLECTUAL PROPERTY AND TECHNOLOGY LICENSES

Intellectual property

We strive to protect and enhance the proprietary technologies that we believe are important to our business, including seeking and maintaining patents intended to cover our products and compositions, their methods of use and any other inventions that are important to the development of our business. We also rely on trade secrets to protect aspects of our business that are not amenable to, or that we do not consider appropriate for, patent protection.

Our success will depend significantly on our ability to obtain and maintain patent and other proprietary protection for commercially important technology, inventions and know-how related to our business, defend and enforce our patents, preserve the confidentiality of our trade secrets and operate without infringing the valid and enforceable patents and proprietary rights of third parties. We also rely on know-how, continuing technological innovation and in-licensing opportunities to develop, strengthen and maintain our proprietary position in the field of *microRNA* therapeutics.

We believe that we have a strong intellectual property position and substantial know-how relating to the development and commercialization of *microRNA* therapeutics, consisting of:

- Ø over 170 patents or patent applications that we own or have in-licensed from academic institutions and third parties including our founding companies, Alnylam and Isis, related to *microRNA* and *microRNA* drug products; and
- Ø approximately 900 patents or patent applications exclusively licensed from our founding companies, Alnylam and Isis, related to RNA technologies, including patent and patent applications relating to chemical modification of oligonucleotides that are useful for *microRNA* therapeutics.

Our objective is to continue to expand our intellectual property estate through our multiple layer approach in order to protect our *microRNA* therapeutics and to maintain our leading position in the *microRNA* therapeutics field. Examples of the technologies covered by our patent portfolio are described below.

We have exclusively licensed patent rights from Julius-Maximilians-Universität Würzburg and Bayerische Patent Allianz GmbH, which we collectively refer to herein as the University of Würzburg, which rights encompass the use of anti-miR therapeutics targeting miR-21 for the treatment of fibrosis, including kidney, liver, lung and cardiac fibrosis. In collaboration with us, investigators at the University of Würzburg demonstrated that targeting miR-21 in a disease model resulted in beneficial phenotypic effects, including the inhibition of the development of fibrosis. The Würzburg-licensed patent portfolio includes more than 20 U.S. and foreign patents and patent applications. Any patents within this portfolio that have issued or may yet issue would have a statutory expiration date in 2029.

We and Alnylam have a co-exclusive license from Stanford University, or Stanford, to patent rights concerning the use of anti-miR therapeutics targeting miR-122 for the treatment of HCV. This patent

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portfolio is based upon research conducted by Peter Sarnow, Ph.D. and colleagues at Stanford, demonstrating that miR-122 is required for HCV replication in mammalian cells. The Stanford-licensed portfolio includes more than 12 U.S and foreign patents and patent applications. Any patents within this portfolio that have issued or may yet issue would have a statutory expiration date in 2025.

In support of our program targeting miR-33, we have exclusively licensed from New York University, or NYU, patent rights encompassing the use of an anti-miR therapeutic targeting miR-33 for the treatment of atherosclerosis, metabolic syndrome and elevated triglycerides. In collaboration with us, Kathryn Moore, Ph.D. and colleagues at NYU demonstrated that inhibiting miR-33 has several therapeutic benefits, including reduction of atherosclerotic plaque size in an experimental model of atherosclerosis, in addition to reduction of serum triglycerides in non-human primates. The NYU-licensed patent rights include five US and foreign patent applications. Any patents that may issue from these applications would have a statutory expiration date in 2031.

Our portfolio of exclusively and jointly owned patent and patent applications is currently composed of over 55 U.S. and foreign patents and patent applications. We are the sole owner of over 50 of the patents and pending applications. We jointly own at least five of the patents and pending applications including those claiming methods for treating liver cancer, including HCC, using anti-miRs targeting miR-21. The patents have statutory expiration dates in through 2029. Any patents that may issue from the pending applications would have statutory expiration dates through 2034.

Our founding companies, Alnylam and Isis, each own or otherwise have rights to numerous patents and patent applications concerning oligonucleotide technologies and a substantial number of these patents and applications have been exclusively licensed to us for use in the *microRNA* field. The technologies covered in these patents and applications include various chemical modifications that are applicable to *microRNA* therapeutics. Among the licensed patents or patent applications, those covering key chemical modifications for use in *microRNA* drug products have statutory expiration dates through 2028.

We have a co-exclusive license to the patent portfolio owned by Max-Planck-Gesellschaft, or MPG, which has been granted to us by Max-Planck-Innovation GmbH, or MI, a wholly-owned subsidiary of MPG acting as MPG's technology transfer agency. MPG and MI are collectively referred to herein as Max-Planck. This patent portfolio is based on the pioneering *microRNA* research conducted by Thomas Tuschl, Ph.D. and colleagues at the Max-Planck Institute of Biophysical Chemistry, which led to the discovery of over 100 human *microRNA* sequences, including *microRNAs* that are the focus of several of our programs. The patent rights encompass both *microRNA* mimic and anti-miR products. Our license is co-exclusive with our founding companies, Alnylam and Isis, for the exploitation of the Max-Planck patent rights for therapeutic uses. In addition, we also have a co-exclusive license to develop and commercialize diagnostics based upon the Max-Planck patent rights contained in these applications. The Max-Planck licensed patent portfolio, referred to herein as the Tuschl 3 patents, includes at least 25 U.S. and foreign patents and patent applications. Any patents within this portfolio that have issued or may yet issue would have a statutory expiration date in 2022.

The term of individual patents depends upon the legal term of the patents in the countries in which they are obtained. In most countries in which we file, the patent term is 20 years from the date of filing the non-provisional application. In the United States, a patent's term may be lengthened by patent term adjustment, which compensates a patentee for administrative delays by the U.S. Patent and Trademark Office in granting a patent, or may be shortened if a patent is terminally disclaimed over an earlier-filed patent.

The term of a patent that covers an FDA-approved drug may also be eligible for patent term extension, which permits patent term restoration of a U.S. patent as compensation for the patent term lost during the FDA regulatory review process. The Hatch-Waxman Act permits a patent term extension of up to five years beyond the expiration of the patent. The length of the patent term extension is related to the

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length of time the drug is under regulatory review. A patent term extension cannot extend the remaining term of a patent beyond a total of 14 years from the date of product approval and only one patent applicable to an approved drug may be extended. Similar provisions are available in Europe and other foreign jurisdictions to extend the term of a patent that covers an approved drug. When possible, depending upon the length of clinical trials and other factors involved in the filing of a new drug application, or NDA, we expect to apply for patent term extensions for patents covering our *microRNA* product candidates and their methods of use.

We may rely, in some circumstances, on trade secrets to protect our technology. However, trade secrets can be difficult to protect. We seek to protect our proprietary technology and processes, in part, by entering into confidentiality agreements with our employees, consultants, scientific advisors and contractors. We also seek to preserve the integrity and confidentiality of our data and trade secrets by maintaining physical security of our premises and physical and electronic security of our information technology systems. While we have confidence in these individuals, organizations and systems, agreements or security measures may be breached, and we may not have adequate remedies for any breach. In addition, our trade secrets may otherwise become known or be independently discovered by competitors. To the extent that our consultants, contractors or collaborators use intellectual property owned by others in their work for us, disputes may arise as to the rights in related or resulting know-how and inventions.

OUR TECHNOLOGY LICENSES

Max-Planck

Therapeutic license

Prior to 2011, our access to the Tuschl 3 patents was derived from agreements between Max-Planck and our founding companies, Alnylam and Isis, for exclusive use in *microRNA* therapeutics. In April 2011, we entered into a direct, co-exclusive license with Max-Planck. The license provides to us, Alnylam and Isis, co-exclusively, access to the Tuschl 3 patents for therapeutic use. Max-Planck retains the right to practice the intellectual property licensed under the agreement for non-commercial purposes.

Under the terms of the license, we are permitted to sublicense our rights outright or as part of an alliance. The license requires that we use commercially reasonable diligence in developing and commercializing a product. In order to secure the license, we made an upfront payment of \$400,000 to Max-Planck. We will be required to make payments based upon the initiation of clinical trials and/or product approval milestones totaling up to \$1.6 million for each licensed product reaching such clinical stage. In addition to milestone payments, we will be required to pay royalties of a percentage of cumulative annual net sales of a licensed product commercialized by us or one of our strategic alliance partners. The percentage is in the low single digits, with the exact percentage depending upon whether the licensed product incorporates intellectual property covered by a Tuschl 3 patent that is still a pending application or, alternatively, an issued patent, and also upon the volume of annual sales. The royalties payable to Max-Planck are subject to reduction for any third party payments required to be made, with a minimum floor in the low single digits.

We may unilaterally terminate the license agreement upon three months' notice and payment of all accrued amounts owing to Max-Planck. Max-Planck may terminate the agreement upon 30 days' prior written notice if we challenge the validity of its patents, or in the event of our material breach which remains uncured after 60 days of receiving written notice of such breach (30 days in the case of nonpayment). Absent early termination, the agreement will automatically terminate upon the expiration or abandonment of all issued patents and filed patent applications with the patent rights covered by the agreement. The longest lived patent rights licensed to us under the agreement are currently expected to expire in September 2022.

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Diagnostic license

In addition, in June 2009, we entered into a co-exclusive license with Max-Planck for use of the Tuschl 3 patents for diagnostic purposes. Under the terms of the license, we made an aggregate initial payment to Max-Planck of 175,000 in three installments, with 75,000 paid in June 2009 and 50,000 paid in each of June 2010 and June 2011. In addition, we made annual maintenance payments of 10,000 in 2011 and 20,000 in 2012 and will make an increased annual maintenance payment commencing in 2013 and thereafter during the term of the agreement. In addition to maintenance payments, we will be required to pay royalties of a percentage of net sales of licensed products. The percentage is in the mid-single digits in the event we market the product and low end of the 10 to 20% range in the event we sell the product through a distributor. The royalties payable to Max-Planck are reduced by the royalties payable to third parties but only if aggregate royalties payable to Max-Planck and third parties exceed a percentage in the mid-10 to 20% range.

We are required to use commercially reasonable efforts to develop and commercialize products under the agreement. Under the terms of the agreement, Max-Planck is permitted to provide up to three additional co-exclusive licenses to its diagnostic patent rights. We may unilaterally terminate the license agreement upon three months' notice and payment of all accrued amounts owing to Max-Planck. Max-Planck may terminate the agreement upon 30 days' prior written notice if we challenge the validity of its patent rights, or in the event of our material breach which remains uncured after 60 days of receiving written notice of such breach (30 days in the case of nonpayment). Absent early termination, the agreement will automatically terminate upon the expiration or abandonment of all issued patents and filed patent applications with the patent rights covered by the agreement. The longest lived patent rights licensed to us under the agreement are currently expected to expire in September 2022.

Max-Planck retains the right to practice the intellectual property licensed under the agreement for non-commercial purposes.

University of Würzburg

In May 2010, we exclusively licensed patent rights from the University of Würzburg which encompass the use of anti-miR therapeutics targeting miR-21 for the treatment of fibrosis, including kidney, liver, lung and cardiac fibrosis.

The University of Würzburg has reserved the right to use the licensed intellectual property for academic and non-commercial purposes. We have the right to grant sublicenses to third parties under the agreement provided such sublicense is for the purpose of developing or commercializing a product. We must obtain the University of Würzburg's written consent to any such sublicense, which may not be unreasonably withheld. We must use commercially reasonable diligence in our efforts to develop, manufacture and commercialize a licensed product. We have assumed certain development milestone obligations and must report on our progress in achieving these milestones on an annual basis.

As a license issuance fee, we paid the University of Würzburg 300,000. In addition, upon commercialization of a product, we will pay to the University of Würzburg a percentage of net sales as a royalty. This royalty is in the low single digits and is reduced upon expiration of all patent claims covering the product. We also paid the University of Würzburg a partnership bonus of 200,000 upon entering into our strategic alliance agreement with Sanofi. Under the agreement, beginning January 1, 2020 and ending on the date we receive NDA approval for a licensed product, we will accrue a minimum royalty obligation of 150,000 per year, which will become payable upon approval of an NDA for a licensed product. After approval of an NDA for a licensed product, we will be required to pay the University of Würzburg an annual minimum royalty, which increases in the five years following approval up to a maximum of 3.0 million per year. The minimum royalties are creditable against actual royalties due and payable for the same calendar year.

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In addition, we will be required to pay the University of Würzburg milestone payments of up to an aggregate of 1.75 million, based upon achievement of specified clinical and regulatory events. In the event we initiate a Phase 2 clinical trial for another indication with the same licensed product, we will be required to pay 50% of the milestone payments applicable to such milestone events. These milestone events are also tied to the due dates set forth in the commercialization plan but may be extended by delays caused by scientific challenges, regulatory requirements or other circumstances outside of our control. We must request an extension in writing explaining the cause for the delay and proposing new due dates. The University of Würzburg may accept the revised dates or reject them, in which case an arbitrator will set the revised dates.

We may terminate the agreement upon 30 days' notice to the University of Würzburg. The University of Würzburg may terminate the agreement if we challenge the validity of its patent rights, or in the event of our nonpayment which remains uncured after 60 days of receiving written notice of such nonpayment. Absent early termination, the agreement will terminate upon the later of the expiration of the last to expire patent licensed to us under the agreement (which is currently expected to be in February 2029) or 10 years following the date of the most recent first commercial sale in a new country of a licensed product.

Stanford University

In August 2005, Alnylam and Isis entered into a co-exclusive license agreement with Stanford, relating to its patent applications claiming the use of miR-122 to reduce the replication of HCV. Upon our formation, we received access to the Stanford technology as an affiliate of Alnylam and Isis. In July 2009, Isis assigned its rights and obligations under the license agreement to us.

Under the license agreement, we are permitted to research, develop, manufacture and commercialize therapeutics for the treatment and prevention of HCV and related conditions. Diagnostics and reagents are specifically excluded from the license. In addition, the license provides a non-exclusive right to research, develop, manufacture and commercialize therapeutics for all conditions or diseases other than HCV. Stanford retained the right, on behalf of itself and all other non-profit academic institutions, to practice the licensed patents for non-profit purposes.

We are permitted to sublicense our rights under the agreement in connection with a bona fide partnership seeking to research and/or develop products under a jointly prepared research plan and which also includes a license to our intellectual property or in association with providing services to a sublicensee. In the event we receive an upfront payment in connection with a sublicense, we are obligated to pay to Stanford a one-time fixed payment amount, which amount will vary depending upon the size of upfront payment we receive. We must also make an annual license maintenance payment during the term of the agreement. The maintenance payments are creditable against royalty payments made in the same year. We will be required to pay milestones for an exclusively licensed product which will be payable upon achievement of specified regulatory and clinical milestones in an aggregate amount of up to \$400,000. Milestones for a non-exclusively licensed product will be payable upon achievement of the same milestones in an aggregate amount of up to \$300,000 for the first such product and up to \$200,000 for the second such product. Upon commercialization of a product, we will be required to pay to Stanford a percentage of net sales as a royalty. This percentage is in the low single digits. The payment will be reduced by other payments we are required to make to third parties until a minimum royalty has been reached.

The agreement requires that we use commercially reasonable efforts to develop, manufacture and commercialize a licensed product and we have agreed to meet certain development and commercialization milestones.

We may terminate the agreement upon 30 days' notice. Stanford may terminate the agreement in the event of our nonpayment or material breach which remains uncured after 60 days of receiving written

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notice of such nonpayment or breach. Absent early termination, the agreement will automatically terminate upon the expiration of the last to expire patent licensed to us under the agreement, which is currently expected to be in May 2025.

New York University

In March 2011, we entered into an exclusive license with NYU related to our miR-33 program. The license provides us the right to develop, manufacture and commercialize therapeutics for the treatment or prevention of atherosclerotic plaque and/or other metabolic disorders under NYU's patents. We are entitled to grant sublicenses under the agreement. NYU retains the right to practice the intellectual property licensed under the agreement for non-commercial purposes.

Under the terms of the agreement, we paid to NYU an upfront payment of \$25,000. An equal additional payment will be required upon issuance of a patent containing a claim of treating or preventing disease. We will be required to make payments to NYU upon achievement of specified clinical and regulatory milestones of up to an aggregate of \$925,000. These milestone payments will only be made after issuance of a therapeutic claim under the NYU patent applications. We are also required to pay royalties of a percentage of net sales for any product sold by us or a strategic alliance partner. The royalty rate is in the low single digits and is subject to reduction to a minimum amount in the event we are required to pay royalties to a third party. In the event we sublicense the NYU patents, NYU is also entitled to receive a percentage of the sublicense income received by us. The percentage payable depends upon the development stage of the program when the sublicense is completed with the highest percentage paid with submission of the first IND. The percentage thereafter declines until completion of the first Phase 2 clinical trial.

We are required, under the terms of the agreement, to use reasonable diligence to develop and commercialize a product and are required to provide NYU with annual reports detailing our progress in this regard. In particular, we are required to fulfill specific development and regulatory milestones by particular dates. The agreement may be terminated by either party upon written notice to the other party of its material breach of the agreement which has remained uncured for 60 days following written notice thereof (30 days in the case of nonpayment). We may also terminate the license upon 60 days' notice in the event development of a product is not scientifically or commercially feasible. Absent early termination, the agreement will automatically terminate upon the expiration of the longest-lived patent rights covered by the agreement, which is currently expected to be in August 2031.

COMPETITION

The biotechnology and pharmaceutical industries are characterized by intense and rapidly changing competition to develop new technologies and proprietary products. While we believe that our proprietary asset estate and scientific expertise in the *microRNA* field provide us with competitive advantages, we face potential competition from many different sources, including larger and better-funded pharmaceutical companies. Not only must we compete with other companies that are focused on *microRNA* therapeutics but any products that we may commercialize will have to compete with existing therapies and new therapies that may become available in the future.

We are aware of several companies that are working specifically to develop *microRNA* therapeutics. These include the biotechnology companies Groove Biopharma, Inc., miRagen Therapeutics, Inc., Mirna Therapeutics, Inc., and Santaris Pharma A/S. These competitors also compete with us in recruiting human capital and securing licenses to complementary technologies or specific *microRNAs* that may be critical to the success of our business. They also compete with us for potential funding from the pharmaceutical industry.

In addition, we expect that for each disease category for which we determine to develop and apply our *microRNA* therapeutics there are other biotechnology companies that will compete against us by

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applying marketed products and development programs using technology other than *microRNA* therapeutics. The key competitive factors that will affect the success of any of our development candidates, if commercialized, are likely to be their efficacy relative to such competing technologies, safety, convenience, price and the availability of reimbursement from government and other third-party payors. Our commercial opportunity could be reduced or eliminated if our competitors have products which are better in one or more of these categories.

MANUFACTURING

We contract with third parties to manufacture our compounds and intend to do so in the future. We do not own or operate and we do not expect to own or operate, facilities for product manufacturing, storage and distribution, or testing. We have personnel with extensive technical, manufacturing, analytical and quality experience and strong project management discipline to oversee contract manufacturing and testing activities, and to compile manufacturing and quality information for our regulatory submissions.

Manufacturing is subject to extensive regulations that impose various procedural and documentation requirements, which govern record keeping, manufacturing processes and controls, personnel, quality control and quality assurance, among others. Our systems and contractors are required to be in compliance with these regulations, and this is assessed regularly through monitoring of performance and a formal audit program.

Drug substance

Our current drug substance supply chain involves various contractors that supply the raw materials and others that manufacture the anti-miR drug substance. We believe our current drug substance contractors have the scale, the systems and the experience to supply all planned IND-enabling studies, early clinical supplies and may be considered for later clinical trials and commercial manufacturing. To ensure continuity in our supply chain, we plan to establish supply arrangements with alternative suppliers for certain portions of our supply chain, as appropriate.

Our process uses common synthetic chemistry and readily available materials. We have established an ongoing program to identify possible process changes to improve purity, yield, manufacturability, and process changes will be implemented as warranted and appropriate. Based upon our knowledge of anti-sense compounds and conjugate chemistry, we do not anticipate any stability issues with our anti-miR product candidates.

Drug product

Our drug product is expected to consist of the anti-miR drug substance in a powdered form formulated in water or a saline solution for injection. Drug product manufacturing uses common processes and readily available materials. When a potential product is ready to commence IND-enabling studies, we will be required to commence drug product stability studies.

GOVERNMENT REGULATION AND PRODUCT APPROVAL

Government authorities in the United States, at the federal, state and local level, and other countries extensively regulate, among other things, the research, development, testing, manufacture, quality control, approval, labeling, packaging, storage, record-keeping, promotion, advertising, distribution, post-approval monitoring and reporting, marketing and export and import of products such as those we are developing. Any product candidate that we develop must be approved by the FDA before it may be legally marketed in the United States and by the appropriate foreign regulatory agency before it may be legally marketed in foreign countries.

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U.S. drug development process

In the United States, the FDA regulates drugs under the Federal Food, Drug and Cosmetic Act, or FDCA, and implementing regulations. Drugs are also subject to other federal, state and local statutes and regulations. The process of obtaining regulatory approvals and the subsequent compliance with appropriate federal, state, local and foreign statutes and regulations require the expenditure of substantial time and financial resources. Failure to comply with the applicable U.S. requirements at any time during the product development process, approval process or after approval, may subject an applicant to administrative or judicial civil or criminal sanctions. FDA sanctions could include refusal to approve pending applications, withdrawal of an approval, clinical hold, warning letters, product recalls, product seizures, total or partial suspension of production or distribution, injunctions, fines, refusals of government contracts, debarment, restitution, disgorgement or civil or criminal penalties. Any agency or judicial enforcement action could have a material adverse effect on us. The process required by the FDA before a drug may be marketed in the United States generally involves the following:

- Ø completion of nonclinical laboratory tests, animal studies and formulation studies according to good laboratory practices, or GLP, or other applicable regulations;
- Ø submission to the FDA of an application for an investigational new drug application, or IND, which must become effective before human clinical trials may begin;
- Ø performance of adequate and well-controlled human clinical trials according to the FDA's regulations commonly referred to as current good clinical practices, or GCPs, which are ethical and scientific quality standards and FDA requirements for conducting, recording and reporting clinical trials to assure that the rights, safety and well-being of trial participants are protected and to establish the safety and efficacy of the proposed drug for its intended use;
- Ø submission to the FDA of an NDA for a new drug;
- Ø satisfactory completion of an FDA inspection of the manufacturing facility or facilities where the drug is produced to assess compliance with the FDA's current good manufacturing practice standards, or cGMP, to assure that the facilities, methods and controls are adequate to preserve the drug's identity, strength, quality and purity;
- Ø potential FDA audit of the nonclinical and clinical trial sites that generated the data in support of the NDA; and
- Ø FDA review and approval of the NDA.

The lengthy process of seeking required approvals and the continuing need for compliance with applicable statutes and regulations require the expenditure of substantial resources and approvals are inherently uncertain.

Before testing any compounds with potential therapeutic value in humans, the drug candidate enters the preclinical testing stage. Preclinical tests, also referred to as nonclinical studies, include laboratory evaluations of product chemistry, toxicity and formulation, as well as animal studies to assess the potential safety and activity of the drug candidate. The conduct of the preclinical tests must comply with federal regulations and requirements including GLP. The sponsor must submit the results of the preclinical tests, together with manufacturing information, analytical data, any available clinical data or literature and a proposed clinical protocol, to the FDA as part of the IND. The IND automatically

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becomes effective 30 days after receipt by the FDA, unless the FDA places the clinical trial on a clinical hold within that 30-day time period. In such a case, the IND sponsor and the FDA must resolve any outstanding concerns before the clinical trial can begin. The FDA may also impose clinical holds on a drug candidate at any time before or during clinical trials due to safety concerns or non-compliance.

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Accordingly, we cannot be sure that submission of an IND will result in the FDA allowing clinical trials to begin, or that, once begun, issues will not arise that suspend or terminate such trial.

During the development of a new drug, sponsors are given opportunities to meet with the FDA at certain points. These points may be prior to submission of an IND, at the end of Phase 2, and before an NDA is submitted. Meetings at other times may be requested. These meetings can provide an opportunity for the sponsor to share information about the data gathered to date, for the FDA to provide advice, and for the sponsor and FDA to reach agreement on the next phase of development. Sponsors typically use the end of Phase 2 meeting to discuss their Phase 2 clinical results and present their plans for the pivotal Phase 3 clinical trial that they believe will support approval of the new drug. If this type of discussion occurred, a sponsor may be able to request a Special Protocol Assessment, or SPA, the purpose of which is to reach agreement with the FDA on the design of the Phase 3 clinical trial protocol design and analysis that will form the primary basis of an efficacy claim.

According to a FDA guidance for industry on the SPA process, a sponsor which meets the prerequisites may make a specific request for a special protocol assessment and provide information regarding the design and size of the proposed clinical trial. The FDA is supposed to evaluate the protocol within 45 days of the request to assess whether the proposed trial is adequate, and that evaluation may result in discussions and a request for additional information. A SPA request must be made before the proposed trial begins, and all open issues must be resolved before the trial begins. If a written agreement is reached, it will be documented and made part of the record. The agreement will be binding on the FDA and may not be changed by the sponsor or the FDA after the trial begins except with the written agreement of the sponsor and the FDA or if the FDA determines that a substantial scientific issue essential to determining the safety or efficacy of the drug was identified after the testing began.

Clinical trials involve the administration of the drug candidate to healthy volunteers or patients under the supervision of qualified investigators, generally physicians not employed by or under the trial sponsor's control. Clinical trials are conducted under protocols detailing, among other things, the objectives of the clinical trial, dosing procedures, subject selection and exclusion criteria, and the parameters to be used to monitor subject safety. Each protocol must be submitted to the FDA as part of the IND. Clinical trials must be conducted in accordance with the FDA's regulations comprising the good clinical practices requirements. Further, each clinical trial must be reviewed and approved by an independent institutional review board, or IRB, at or servicing each institution at which the clinical trial will be conducted. An IRB is charged with protecting the welfare and rights of trial participants and considers such items as whether the risks to individuals participating in the clinical trials are minimized and are reasonable in relation to anticipated benefits. The IRB also approves the form and content of the informed consent that must be signed by each clinical trial subject or his or her legal representative and must monitor the clinical trial until completed.

Human clinical trials are typically conducted in three sequential phases that may overlap or be combined:

- Ø *Phase 1.* The drug is initially introduced into healthy human subjects and tested for safety, dosage tolerance, absorption, metabolism, distribution and excretion. In the case of some products for severe or life-threatening diseases, especially when the product may be too inherently toxic to ethically administer to healthy volunteers, the initial human testing is often conducted in patients.
- Ø *Phase 2.* The drug is evaluated in a limited patient population to identify possible adverse effects and safety risks, to preliminarily evaluate the efficacy of the product for specific targeted diseases and to determine dosage tolerance, optimal dosage and dosing schedule.
- Ø *Phase 3.* Clinical trials are undertaken to further evaluate dosage, clinical efficacy and safety in an expanded patient population at geographically dispersed clinical trial sites. These clinical trials are intended to establish the overall risk/benefit ratio of the product and provide an adequate basis for product labeling. Generally, two adequate and well-controlled Phase 3 clinical trials are required by the FDA for approval of an NDA.

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Post-approval clinical trials, sometimes referred to as Phase 4 clinical trials, may be conducted after initial marketing approval. These clinical trials are used to gain additional experience from the treatment of patients in the intended therapeutic indication.

Annual progress reports detailing the results of the clinical trials must be submitted to the FDA and written IND safety reports must be promptly submitted to the FDA and the investigators for serious and unexpected adverse events or any finding from tests in laboratory animals that suggests a significant risk for human subjects. Phase 1, Phase 2 and Phase 3 clinical trials may not be completed successfully within any specified period, if at all. The FDA or the sponsor or its data safety monitoring board may suspend a clinical trial at any time on various grounds, including a finding that the research subjects or patients are being exposed to an unacceptable health risk. Similarly, an IRB can suspend or terminate approval of a clinical trial at its institution if the clinical trial is not being conducted in accordance with the IRB's requirements or if the drug has been associated with unexpected serious harm to patients. Concurrent with clinical trials, companies usually complete additional animal studies and must also develop additional information about the chemistry and physical characteristics of the drug as well as finalize a process for manufacturing the product in commercial quantities in accordance with cGMP requirements. The manufacturing process must be capable of consistently producing quality batches of the drug candidate and, among other things, must develop methods for testing the identity, strength, quality and purity of the final drug. Additionally, appropriate packaging must be selected and tested and stability studies must be conducted to demonstrate that the drug candidate does not undergo unacceptable deterioration over its shelf life.

U.S. review and approval processes

The results of product development, nonclinical studies and clinical trials, along with descriptions of the manufacturing process, analytical tests conducted on the chemistry of the drug, proposed labeling and other relevant information are submitted to the FDA as part of an NDA requesting approval to market the product. The submission of an NDA is subject to the payment of substantial user fees; a waiver of such fees may be obtained under certain limited circumstances.

In addition, under the Pediatric Research Equity Act, or PREA, an NDA or supplement to an NDA must contain data to assess the safety and effectiveness of the drug for the claimed indications in all relevant pediatric subpopulations and to support dosing and administration for each pediatric subpopulation for which the product is safe and effective. The FDA may grant deferrals for submission of data or full or partial waivers. Unless otherwise required by regulation, PREA does not apply to any drug for an indication for which orphan designation has been granted.

The FDA reviews all NDAs submitted to determine if they are substantially complete before it accepts them for filing. Once the submission is accepted for filing, the FDA begins an in-depth review of the NDA. Under the goals and policies agreed to by the FDA under the Prescription Drug User Fee Act, or PDUFA, the FDA has 10 months in which to complete its initial review of a standard NDA and respond to the applicant, and six months for a priority NDA. The FDA does not always meet its PDUFA goal dates for standard and priority NDAs. The review process and the PDUFA goal date may be extended by three months if the FDA requests or the NDA sponsor otherwise provides additional information or clarification regarding information already provided in the submission within the last three months before the PDUFA goal date.

After the NDA submission is accepted for filing, the FDA reviews the NDA to determine, among other things, whether the proposed product is safe and effective for its intended use, and whether the product is being manufactured in accordance with cGMP to assure and preserve the product's identity, strength, quality and purity. The FDA may refer applications for novel drug or biological products or drug or biological products which present difficult questions of safety or efficacy to an advisory committee,

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typically a panel that includes clinicians and other experts, for review, evaluation and a recommendation as to whether the application should be approved and under what conditions. The FDA is not bound by the recommendations of an advisory committee, but it considers such recommendations carefully when making decisions. During the drug approval process, the FDA also will determine whether a risk evaluation and mitigation strategy, or REMS, is necessary to assure the safe use of the drug. If the FDA concludes a REMS is needed, the sponsor of the NDA must submit a proposed REMS; the FDA will not approve the NDA without a REMS, if required.

Before approving an NDA, the FDA will inspect the facilities at which the product is manufactured. The FDA will not approve the product unless it determines that the manufacturing processes and facilities are in compliance with cGMP requirements and adequate to assure consistent production of the product within required specifications. Additionally, before approving an NDA, the FDA will typically inspect one or more clinical sites to assure that the clinical trials were conducted in compliance with IND study requirements. If the FDA determines that the application, manufacturing process or manufacturing facilities are not acceptable it will outline the deficiencies in the submission and often will request additional testing or information.

The NDA review and approval process is lengthy and difficult and the FDA may refuse to approve an NDA if the applicable regulatory criteria are not satisfied or may require additional clinical data or other data and information. Even if such data and information is submitted, the FDA may ultimately decide that the NDA does not satisfy the criteria for approval. Data obtained from clinical trials are not always conclusive and the FDA may interpret data differently than we interpret the same data. The FDA will issue a complete response letter if the agency decides not to approve the NDA. The complete response letter usually describes all of the specific deficiencies in the NDA identified by the FDA. The deficiencies identified may be minor, for example, requiring labeling changes, or major, for example, requiring additional clinical trials. Additionally, the complete response letter may include recommended actions that the applicant might take to place the application in a condition for approval. If a complete response letter is issued, the applicant may either resubmit the NDA, addressing all of the deficiencies identified in the letter, or withdraw the application.

If a product receives regulatory approval, the approval may be significantly limited to specific diseases and dosages or the indications for use may otherwise be limited, which could restrict the commercial value of the product. Further, the FDA may require that certain contraindications, warnings or precautions be included in the product labeling. In addition, the FDA may require post marketing clinical trials, sometimes referred to as Phase 4 clinical trials testing, which involves clinical trials designed to further assess a drug safety and effectiveness and may require testing and surveillance programs to monitor the safety of approved products that have been commercialized.

Orphan drug designation

Under the Orphan Drug Act, the FDA may grant orphan designation to a drug or biological product intended to treat a rare disease or condition, which is generally a disease or condition that affects fewer than 200,000 individuals in the United States, or more than 200,000 individuals in the United States and for which there is no reasonable expectation that the cost of developing and making a drug or biological product available in the United States for this type of disease or condition will be recovered from sales of the product. Orphan product designation must be requested before submitting an NDA. After the FDA grants orphan product designation, the identity of the therapeutic agent and its potential orphan use are disclosed publicly by the FDA. Orphan product designation does not convey any advantage in or shorten the duration of the regulatory review and approval process.

If a product that has orphan designation subsequently receives the first FDA approval for the disease or condition for which it has such designation, the product is entitled to orphan product exclusivity, which

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means that the FDA may not approve any other applications to market the same drug or biological product for the same indication for seven years, except in limited circumstances, such as a showing of clinical superiority to the product with orphan exclusivity. Competitors, however, may receive approval of different products for the indication for which the orphan product has exclusivity or obtain approval for the same product but for a different indication for which the orphan product has exclusivity. Orphan product exclusivity also could block the approval of one of our products for seven years if a competitor obtains approval of the same drug or biological product as defined by the FDA or if our drug candidate is determined to be contained within the competitor's product for the same indication or disease. If a drug or biological product designated as an orphan product receives marketing approval for an indication broader than what is designated, it may not be entitled to orphan product exclusivity. Orphan drug status in the European Union has similar but not identical benefits in the European Union.

Expedited development and review programs

The FDA has a Fast Track program that is intended to expedite or facilitate the process for reviewing new drugs and biological products that meet certain criteria. Specifically, new drugs and biological products are eligible for Fast Track designation if they are intended to treat a serious or life-threatening condition and demonstrate the potential to address unmet medical needs for the condition. Fast Track designation applies to the combination of the product and the specific indication for which it is being studied. Unique to a Fast Track product, the FDA may consider for review sections of the NDA on a rolling basis before the complete application is submitted, if the sponsor provides a schedule for the submission of the sections of the NDA, the FDA agrees to accept sections of the NDA and determines that the schedule is acceptable, and the sponsor pays any required user fees upon submission of the first section of the NDA.

Any product submitted to the FDA for marketing, including a Fast Track program, may also be eligible for other types of FDA programs intended to expedite development and review, such as priority review and accelerated approval. Any product is eligible for priority review if it has the potential to provide safe and effective therapy where no satisfactory alternative therapy exists or a significant improvement in the treatment, diagnosis or prevention of a disease compared to marketed products. The FDA will attempt to direct additional resources to the evaluation of an application for a new drug or biological product designated for priority review in an effort to facilitate the review. Additionally, a product may be eligible for accelerated approval. Drug or biological products studied for their safety and effectiveness in treating serious or life-threatening illnesses and that provide meaningful therapeutic benefit over existing treatments may receive accelerated approval, which means that they may be approved on the basis of adequate and well-controlled clinical trials establishing that the product has an effect on a surrogate endpoint that is reasonably likely to predict a clinical benefit, or on the basis of an effect on a clinical endpoint other than survival or irreversible morbidity. As a condition of approval, the FDA may require that a sponsor of a drug or biological product receiving accelerated approval perform adequate and well-controlled post-marketing clinical trials. In addition, the FDA currently requires as a condition for accelerated approval pre-approval of promotional materials, which could adversely impact the timing of the commercial launch of the product. Fast Track designation, priority review and accelerated approval do not change the standards for approval but may expedite the development or approval process.

Post-approval requirements

Any drug products for which we or our strategic alliance partners receive FDA approvals are subject to continuing regulation by the FDA, including, among other things, record-keeping requirements, reporting of adverse experiences with the product, providing the FDA with updated safety and efficacy information, product sampling and distribution requirements, complying with certain electronic records and signature requirements and complying with FDA promotion and advertising requirements, which

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include, among others, standards for direct-to-consumer advertising, promoting drugs for uses or in patient populations that are not described in the drug's approved labeling (known as off-label use), industry-sponsored scientific and educational activities, and promotional activities involving the internet. Failure to comply with FDA requirements can have negative consequences, including adverse publicity, enforcement letters from the FDA, mandated corrective advertising or communications with doctors, and civil or criminal penalties. Although physicians may prescribe legally available drugs for off-label uses, manufacturers may not market or promote such off-label uses.

We will rely, and expect to continue to rely, on third parties for the production of clinical and commercial quantities of any products that we may commercialize. Our strategic alliance partners may also utilize third parties for some or all of a product we are developing with such strategic alliance partner. Manufacturers of our products are required to comply with applicable FDA manufacturing requirements contained in the FDA's cGMP regulations. cGMP regulations require among other things, quality control and quality assurance as well as the corresponding maintenance of records and documentation. Drug manufacturers and other entities involved in the manufacture and distribution of approved drugs are required to register their establishments with the FDA and certain state agencies, and are subject to periodic unannounced inspections by the FDA and certain state agencies for compliance with cGMP and other laws. Accordingly, manufacturers must continue to expend time, money, and effort in the area of production and quality control to maintain cGMP compliance. Discovery of problems with a product after approval may result in restrictions on a product, manufacturer, or holder of an approved NDA, including withdrawal of the product from the market. In addition, changes to the manufacturing process generally require prior FDA approval before being implemented and other types of changes to the approved product, such as adding new indications and additional labeling claims, are also subject to further FDA review and approval.

The FDA also may require post-marketing testing, known as Phase 4 testing, risk minimization action plans and surveillance to monitor the effects of an approved product or place conditions on an approval that could restrict the distribution or use of the product.

U.S. patent term restoration and marketing exclusivity

Depending upon the timing, duration and specifics of the FDA approval of the use of our drug candidates, some of our United States patents may be eligible for limited patent term extension under the Drug Price Competition and Patent Term Restoration Act of 1984, commonly referred to as the Hatch-Waxman Amendments. The Hatch-Waxman Amendments permit a patent restoration term of up to five years as compensation for patent term lost during product development and the FDA regulatory review process. However, patent term restoration cannot extend the remaining term of a patent beyond a total of 14 years from the product's approval date. The patent term restoration period is generally one-half the time between the effective date of an IND and the submission date of an NDA plus the time between the submission date of an NDA and the approval of that application. Only one patent applicable to an approved drug is eligible for the extension and the application for the extension must be submitted prior to the expiration of the patent. The United States Patent and Trademark Office, or U.S. PTO, in consultation with the FDA, reviews and approves the application for any patent term extension or restoration. In the future, we may intend to apply for restoration of patent term for one of our currently owned or licensed patents to add patent life beyond its current expiration date, depending on the expected length of the clinical trials and other factors involved in the filing of the relevant NDA. We cannot be certain that the U.S. PTO and FDA would grant any patent term extension.

Market exclusivity provisions under the FDCA can also delay the submission or the approval of certain applications of other companies seeking to reference another company's NDA. The FDCA provides a five-year period of non-patent marketing exclusivity within the United States to the first applicant to obtain approval of an NDA for a new chemical entity. A drug is a new chemical entity if the FDA has

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not previously approved any other new drug containing the same active moiety, which is the molecule or ion responsible for the action of the drug substance. During the exclusivity period, the FDA may not accept for review an abbreviated new drug application, or ANDA, or a 505(b)(2) NDA submitted by another company for another version of such drug where the applicant does not own or have a legal right of reference to all the data required for approval. However, an application may be submitted after four years if it contains a certification of patent invalidity or non-infringement to one of the patents listed with the FDA by the innovator NDA holder. The FDCA also provides three years of marketing exclusivity for an NDA, or supplement to an existing NDA if new clinical investigations, other than bioavailability studies, that were conducted or sponsored by the applicant are deemed by the FDA to be essential to the approval of the application, for example new indications, dosages or strengths of an existing drug. This three-year exclusivity covers only the conditions associated with the new clinical investigations and does not prohibit the FDA from approving ANDAs for drugs containing the original active agent. Five-year and three-year exclusivity will not delay the submission or approval of a full NDA. However, an applicant submitting a full NDA would be required to conduct or obtain a right of reference to all of the preclinical studies and adequate and well-controlled clinical trials necessary to demonstrate safety and effectiveness. Pediatric exclusivity is another type of regulatory market exclusivity in the United States. Pediatric exclusivity, if granted, adds six months to existing exclusivity periods and patent terms. This six-month exclusivity, which runs from the end of other exclusivity protection or patent term, may be granted based on the voluntary completion of a pediatric trial in accordance with an FDA-issued Written Request for such a trial.

U.S. Foreign Corrupt Practices Act

The U.S. Foreign Corrupt Practices Act, or FCPA, prohibits certain individuals and entities, including us, from promising, paying, offering to pay, or authorizing the payment of anything of value to any foreign government official, directly or indirectly, to obtain or retain business or an improper advantage. The U.S. Department of Justice and the U.S. Securities and Exchange Commission, or SEC, have increased their enforcement efforts with respect to the FCPA. Violations of the FCPA may result in large civil and criminal penalties and could result in an adverse effect on a company's reputation, operations, and financial condition. A company may also face collateral consequences such as debarment and the loss of export privileges.

Federal and state fraud and abuse laws

In addition to FDA restrictions on marketing of pharmaceutical products, several other types of state and federal laws have been applied to restrict certain business practices in the biopharmaceutical industry in recent years. These laws include anti-kickback statutes and false claims statutes.

The federal Anti-Kickback Statute prohibits, among other things, knowingly and willfully offering, paying, soliciting, or receiving remuneration to induce or in return for purchasing, leasing, ordering, or arranging for the purchase, lease, or order of any healthcare item or service reimbursable under Medicare, Medicaid, or other federally financed healthcare programs. The term remuneration has been broadly interpreted to include anything of value, including for example, gifts, discounts, the furnishing of supplies or equipment, credit arrangements, payments of cash, waivers of payment, ownership interests and providing anything at less than its fair market value. The Anti-Kickback Statute has been interpreted to apply to arrangements between pharmaceutical manufacturers on one hand and prescribers, purchasers, and formulary managers on the other. Although there are a number of statutory exemptions and regulatory safe harbors protecting certain common activities from prosecution, the exemptions and safe harbors are drawn narrowly, and our practices may not in all cases meet all of the criteria for statutory exemptions or safe harbor protection. Practices that involve remuneration that may be alleged to be intended to induce prescribing, purchases, or recommendations may be subject to scrutiny if they

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do not qualify for an exemption or safe harbor. . Several courts have interpreted the statute's intent requirement to mean that if any one purpose of an arrangement involving remuneration is to induce referrals of federal healthcare covered business, the statute has been violated. The reach of the Anti-Kickback Statute was also broadened by the Patient Protection and Affordable Health Care Act, as amended by the Health Care and Education Affordability Reconciliation Act, or collectively the PPACA, which, among other things, amends the intent requirement of the federal Anti-Kickback Statute. Pursuant to the statutory amendment, a person or entity no longer needs to have actual knowledge of this statute or specific intent to violate it in order to have committed a violation. In addition, the PPACA provides that the government may assert that a claim including items or services resulting from a violation of the federal Anti-Kickback Statute constitutes a false or fraudulent claim for purposes of the civil False Claims Act (discussed below) or the civil monetary penalties statute, which imposes penalties against any person who is determined to have presented or caused to be presented a claim to a federal health program that the person knows or should know is for an item or service that was not provided as claimed or is false or fraudulent.

The federal False Claims Act prohibits any person from knowingly presenting, or causing to be presented, a false claim for payment to the federal government. Recently, several pharmaceutical and other healthcare companies have been prosecuted under these laws for allegedly providing free product to customers with the expectation that the customers would bill federal programs for the product. Other companies have been prosecuted for causing false claims to be submitted because of the companies' marketing of the product for unapproved, and thus non-reimbursable, uses. Many states also have statutes or regulations similar to the federal Anti-Kickback Statute and False Claims Act, which state laws apply to items and services reimbursed under Medicaid and other state programs, or, in several states, apply regardless of the payer. Also, the federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, created new federal criminal statutes that prohibit knowingly and willfully executing a scheme to defraud any healthcare benefit program, including private third-party payers and knowingly and willfully falsifying, concealing or covering up a material fact or making any materially false, fictitious or fraudulent statement in connection with the delivery of or payment for healthcare benefits, items or services.

Because of the breadth of these laws and the narrowness of the federal Anti-Kickback Statute's safe harbors, it is possible that some of our business activities could be subject to challenge under one or more of such laws. Such a challenge could have a material adverse effect on our business, financial condition and results of operations. If we obtain FDA approval for any of our product candidates and begin commercializing those products in the United States, our operations may be directly, or indirectly through our customers, distributors, or other business partners, subject to various federal and state fraud and abuse laws, including, without limitation, anti-kickback statutes and false claims statutes. These laws may impact, among other things, our proposed sales, marketing and education programs.

In addition, we may be subject to data privacy and security regulation by both the federal government and the states in which we conduct our business. HIPAA, as amended by the Health Information Technology and Clinical Health Act, or HITECH, and its implementing regulations, imposes certain requirements relating to the privacy, security and transmission of individually identifiable health information. Among other things, HITECH makes HIPAA's privacy and security standards directly applicable to business associates, independent contractors or agents of covered entities that receive or obtain protected health information in connection with providing a service on behalf of a covered entity. HITECH also increased the civil and criminal penalties that may be imposed against covered entities, business associates and possibly other persons, and gave state attorneys general new authority to file civil actions for damages or injunctions in federal courts to enforce the federal HIPAA laws and seek attorney's fees and costs associated with pursuing federal civil actions. In addition, state laws govern the privacy and security of health information in certain circumstances, many of which differ from each other in significant ways and may not have the same effect, thus complicating compliance efforts.

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If our operations are found to be in violation of any of the federal and state laws described above or any other governmental regulations that apply to us, we may be subject to penalties, including criminal and significant civil monetary penalties, damages, fines, imprisonment, exclusion from participation in government healthcare programs, and the curtailment or restructuring of our operations, any of which could adversely affect our ability to operate our business and our results of operations. To the extent that any of our product candidates are ultimately sold in a foreign country, we may be subject to similar foreign laws and regulations, which may include, for instance, applicable post-marketing requirements, including safety surveillance, anti-fraud and abuse laws, and implementation of corporate compliance programs and reporting of payments or transfers of value to healthcare professionals.

In the United States and foreign jurisdictions, there have been a number of legislative and regulatory changes to the healthcare system that could affect our future results of operations. In particular, there have been and continue to be a number of initiatives at the United States federal and state levels that seek to reduce healthcare costs. The Medicare Prescription Drug, Improvement, and Modernization Act of 2003, or the MMA, imposed new requirements for the distribution and pricing of prescription drugs for Medicare beneficiaries. Under Part D, Medicare beneficiaries may enroll in prescription drug plans offered by private entities which will provide coverage of outpatient prescription drugs. Part D plans include both stand-alone prescription drug benefit plans and prescription drug coverage as a supplement to Medicare Advantage plans. Unlike Medicare Part A and B, Part D coverage is not standardized. Part D prescription drug plan sponsors are not required to pay for all covered Part D drugs, and each drug plan can develop its own drug formulary that identifies which drugs it will cover and at what tier or level. However, Part D prescription drug formularies must include drugs within each therapeutic category and class of covered Part D drugs, though not necessarily all the drugs in each category or class. Any formulary used by a Part D prescription drug plan must be developed and reviewed by a pharmacy and therapeutic committee. Government payment for some of the costs of prescription drugs may increase demand for our products for which we receive marketing approval. However, any negotiated prices for our products covered by a Part D prescription drug plan will likely be lower than the prices we might otherwise obtain. Moreover, while the MMA applies only to drug benefits for Medicare beneficiaries, private payors often follow Medicare coverage policy and payment limitations in setting their own payment rates. Any reduction in payment that results from Medicare Part D may result in a similar reduction in payments from non-governmental payors.

The American Recovery and Reinvestment Act of 2009 provides funding for the federal government to compare the effectiveness of different treatments for the same illness. A plan for the research will be developed by the Department of Health and Human Services, the Agency for Healthcare Research and Quality and the National Institutes for Health, and periodic reports on the status of the research and related expenditures will be made to Congress. Although the results of the comparative effectiveness studies are not intended to mandate coverage policies for public or private payors, it is not clear what effect, if any, the research will have on the sales of any product, if any such product or the condition that it is intended to treat is the subject of a study. It is also possible that comparative effectiveness research demonstrating benefits in a competitor's product could adversely affect the sales of our product candidates. If third-party payors do not consider our products to be cost-effective compared to other available therapies, they may not cover our products as a benefit under their plans or, if they do, the level of payment may not be sufficient to allow us to sell our products on a profitable basis.

In March 2010 the PPACA was enacted, which includes measures to significantly change the way healthcare is financed by both governmental and private insurers. Among the provisions of the PPACA of importance to the pharmaceutical and biotechnology industry are the following:

- Ø an annual, nondeductible fee on any entity that manufactures or imports certain branded prescription drugs and biologic agents, apportioned among these entities according to their market share in certain government healthcare programs, that began in 2011;

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- Ø an increase in the rebates a manufacturer must pay under the Medicaid Drug Rebate Program to 23.1% and 13% of the average manufacturer price for branded and generic drugs, respectively;
- Ø a new Medicare Part D coverage gap discount program, in which manufacturers must agree to offer 50% point-of-sale discounts to negotiated prices of applicable brand drugs to eligible beneficiaries during their coverage gap period, as a condition for the manufacturer's outpatient drugs to be covered under Medicare Part D;
- Ø extension of manufacturers' Medicaid rebate liability to covered drugs dispensed to individuals who are enrolled in Medicaid managed care organizations;
- Ø expansion of eligibility criteria for Medicaid programs by, among other things, allowing states to offer Medicaid coverage to additional individuals and by adding new mandatory eligibility categories for certain individuals with income at or below 133% of the Federal Poverty Level beginning in 2014, thereby potentially increasing manufacturers' Medicaid rebate liability;
- Ø expansion of the entities eligible for discounts under the Public Health Service pharmaceutical pricing program;
- Ø new requirements under the federal Open Payments program, created under Section 6002 of the PPACA and its implementing regulations, that manufacturers of drugs, devices, biologics and medical supplies for which payment is available under Medicare, Medicaid or the Children's Health Insurance Program (with certain exceptions) report annually to the U.S. Department of Health and Human Services, or HHS, information related to payments or other transfers of value made or distributed to physicians (defined to include doctors, dentists, optometrists, podiatrists and chiropractors) and teaching hospitals, and that applicable manufacturers and applicable group purchasing organizations report annually to HHS ownership and investment interests held by physicians (as defined above) and their immediate family members, with data collection required beginning August 1, 2013 and reporting to the Centers for Medicare & Medicaid Services, or CMS, required by March 31, 2014 and by the 90th day of each subsequent calendar year;
- Ø a new requirement to annually report drug samples that manufacturers and distributors provide to physicians, effective April 1, 2012;
- Ø expansion of health care fraud and abuse laws, including the False Claims Act and the Anti-Kickback Statute, new government investigative powers, and enhanced penalties for noncompliance;
- Ø a licensure framework for follow-on biologic products;
- Ø a new Patient-Centered Outcomes Research Institute to oversee, identify priorities in, and conduct comparative clinical effectiveness research, along with funding for such research;

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Ø creation of the Independent Payment Advisory Board which, beginning in 2014, will have authority to recommend certain changes to the Medicare program that could result in reduced payments for prescription drugs and those recommendations could have the effect of law even if Congress does not act on the recommendations; and

Ø establishment of a Center for Medicare Innovation at CMS to test innovative payment and service delivery models to lower Medicare and Medicaid spending, potentially including prescription drug spending that began on January 1, 2011.

In addition, other legislative changes have been proposed and adopted since the PPACA was enacted. In August 2011, the president signed into law the Budget Control Act of 2011, which, among other things, created the Joint Select Committee on Deficit Reduction, or joint committee, to recommend proposals in spending reductions to Congress. The joint committee did not achieve its targeted deficit reduction of at least \$1.2 trillion for the years 2013 through 2021, triggering automatic reductions to several

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government programs. These reductions include aggregate reductions to Medicare payments to providers of up to 2% per fiscal year, starting in 2013. In January 2013, the president signed into law the American Taxpayer Relief Act of 2012, which, among other things, reduced Medicare payments to several providers and increased the statute of limitations period for the government to recover overpayments to providers from three to five years. These new laws may result in additional reductions in Medicare and other healthcare funding, which could have a material adverse effect on our financial operations.

Europe / rest of world government regulation

In addition to regulations in the United States, we and our strategic alliance partners will be subject to a variety of regulations in other jurisdictions governing, among other things, clinical trials and any commercial sales and distribution of our products.

Whether or not we or our collaborators obtain FDA approval for a product, we must obtain the requisite approvals from regulatory authorities in foreign countries prior to the commencement of clinical trials or marketing of the product in those countries. Certain countries outside of the United States have a similar process that requires the submission of a clinical trial application much like the IND prior to the commencement of human clinical trials. In the European Union, for example, a clinical trial application, or CTA, must be submitted to each country's national health authority and an independent ethics committee, much like the FDA and IRB, respectively. Once the CTA is approved in accordance with a country's requirements, clinical trial development may proceed.

The requirements and process governing the conduct of clinical trials, product licensing, pricing and reimbursement vary from country to country. In all cases, the clinical trials are conducted in accordance with GCP and the applicable regulatory requirements and the ethical principles that have their origin in the Declaration of Helsinki.

To obtain regulatory approval of an investigational drug or biological product under European Union regulatory systems, we or our strategic alliance partners must submit a marketing authorization application. The application used to file the NDA or BLA in the United States is similar to that required in the European Union, with the exception of, among other things, country-specific document requirements. In the European Economic Area, or EEA (which is comprised of the 27 Member States of the European Union plus Norway, Iceland and Liechtenstein), medicinal products can only be commercialized after obtaining a Marketing Authorization, or MA. There are two types of marketing authorizations: the Community MA, which is issued by the European Commission through the Centralized Procedure based on the opinion of the Committee for Medicinal Products for Human Use, or CHMP, a body of the EMA, and which is valid throughout the entire territory of the EEA; and the National MA, which is issued by the competent authorities of the Member States of the EEA and only authorized marketing in that Member State's national territory and not the EEA as a whole.

The Centralized Procedure is mandatory for certain types of products, such as biotechnology medicinal products, orphan medicinal products, and medicinal products containing a new active substance indicated for the treatment of AIDS, cancer, neurodegenerative disorders, diabetes, auto-immune and viral diseases. The Centralized Procedure is optional for products containing a new active substance not yet authorized in the EEA, or for products that constitute a significant therapeutic, scientific or technical innovation or which are in the interest of public health in the European Union. The National MA is for products not falling within the mandatory scope of the Centralized Procedure. Where a product has already been authorized for marketing in a Member State of the EEA, this National MA can be recognized in another Member States through the Mutual Recognition Procedure. If the product has not received a National MA in any Member State at the time of application, it can be approved simultaneously in various Member States through the Decentralized Procedure. Under the Decentralized

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Business

Procedure an identical dossier is submitted to the competent authorities of each of the Member States in which the MA is sought, one of which is selected by the applicant as the Reference Member state, or RMS. If the RMS proposes to authorize the product, and the other Member States do not raise objections, the product is granted a national MA in all the Member States where the authorization was sought. Before granting the MA, the EMA or the competent authorities of the Member States of the EEA make an assessment of the risk-benefit balance of the product on the basis of scientific criteria concerning its quality, safety and efficacy.

For other countries outside of the European Union, such as countries in Eastern Europe, Latin America or Asia, the requirements governing the conduct of clinical trials, product licensing, pricing and reimbursement vary from country to country. In all cases, again, the clinical trials are conducted in accordance with GCP and the applicable regulatory requirements and the ethical principles that have their origin in the Declaration of Helsinki.

If we or our strategic alliance partners fail to comply with applicable foreign regulatory requirements, we may be subject to, among other things, fines, suspension or withdrawal of regulatory approvals, product recalls, seizure of products, operating restrictions and criminal prosecution.

EMPLOYEES

As of March 31, 2013, we had 71 full-time employees, 31 of whom have Ph.D. degrees. Of these full-time employees, 57 employees are engaged in research and development activities and 14 employees are engaged in finance, legal, human resources, facilities and general management. We have no collective bargaining agreements with our employees and we have not experienced any work stoppages. We consider our relations with our employees to be good.

FACILITIES

Our corporate headquarters are located in La Jolla, California. The facility we lease encompasses approximately 28,881 square feet of office and laboratory space. The lease for this facility expires in June 2017, subject to our option to renew for up to two additional three-year terms. We believe that our facility is sufficient to meet our needs and that suitable additional space will be available as and when needed.

LEGAL PROCEEDINGS

From time to time, we are subject to various legal proceedings and claims that arise in the ordinary course of our business activities. Although the results of litigation and claims cannot be predicted with certainty, as of the date of this prospectus, we do not believe we are party to any claim or litigation the outcome of which, if determined adversely to us, would individually or in the aggregate be reasonably expected to have a material adverse effect on our business. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources and other factors.

Table of Contents**Certain relationships and related party transactions**

The following includes a summary of transactions since January 1, 2010 to which we have been a party, in which the amount involved in the transaction exceeded \$120,000, and in which any of our directors, executive officers or, to our knowledge, beneficial owners of more than 5% of our capital stock or any member of the immediate family of any of the foregoing persons had or will have a direct or indirect material interest, other than equity and other compensation, termination, change in control and other arrangements, which are described under Executive and director compensation.

DIRECTOR AFFILIATIONS WITH OUR PRINCIPAL STOCKHOLDERS & STRATEGIC PARTNERS

Some of our directors or former directors, are affiliated with our principal stockholders and strategic partners as indicated in the table below:

Director	Affiliation
John M. Maraganore, Ph.D.	Alnylam Pharmaceuticals, Inc.
Stelios Papadopoulos, Ph.D.	Biogen Idec
B. Lynne Parshall	Isis Pharmaceuticals, Inc.
Douglas E. Williams, Ph.D.	Biogen Idec
Barry E. Greene (former director)	Alnylam Pharmaceuticals, Inc.
Stanley T. Crooke, M.D., Ph.D. (former director)	Isis Pharmaceuticals, Inc.

PREFERRED STOCK FINANCINGS

Series B Convertible Preferred Stock Financing. In October 2010, we issued and sold to Aventis Holdings, Inc. an aggregate of 2,499,999 shares of series B convertible preferred stock, at a purchase price of \$4.00 per share, for aggregate consideration of \$10.0 million. In connection with the October 2010 financing, we entered into an investor rights agreement with Aventis Holdings, Inc., containing information rights, rights of first refusal and registration rights, among other things. This investor rights agreement will terminate in October 2015, except for certain of the registration rights granted thereunder, as more fully described below in Description of capital stock Registration Rights.

STRATEGIC ALLIANCES AND COLLABORATIONS

In April 2008, we entered into a product development and commercialization agreement with GSK, which was amended in February 2010, June 2010, July 2011, June 2012 and June 2013. Upon entering into the agreement, GSK loaned \$5.0 million to us under a convertible promissory note, which was amended in January 2011, amended and restated in July 2012 and amended and restated in October 2012. This agreement and the associated convertible promissory note are described under Business Our Strategic Alliances.

In January 2009, we entered into an amended and restated license and collaboration agreement with Alnylam Pharmaceuticals, Inc. and Isis Pharmaceuticals, Inc., which the parties amended in June 2010, October 2011. This agreement is described under Business Our Strategic Alliances.

In February 2010, we entered into an exclusive license and nonexclusive option agreement with GSK. Upon entering into the agreement, GSK loaned \$5.0 million to us under a convertible promissory note, which was amended and restated in July 2012. This agreement and the associated convertible promissory note are described under Business Our Strategic Alliances.

In June 2010, we entered into a collaboration and license agreement and a non-exclusive technology alliance and option agreement with Sanofi, an affiliate of Aventis Holdings, Inc. In July 2012, we

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Certain relationships and related party transactions

amended and restated the 2010 license and collaboration agreement and further amended it by letter agreement in April 2013. In June 2013, we and Sanofi entered into an option agreement pursuant to which we granted Sanofi an exclusive right to negotiate with us to enter into a development and license agreement for the co-development and commercialization of certain of our unencumbered *microRNA* programs through December 2013, for which Sanofi has agreed to pay us an upfront option fee of \$2.5 million, \$1.25 million of which is creditable against future payments payable by Sanofi to us. In addition, Sanofi granted us an exclusive option, which also expires December 2013, to negotiate the co-development and commercialization of miR-21. These agreements are described under **Business Our Strategic Alliances**.

In August 2012, we entered into a collaboration and license agreement with AstraZeneca, which the parties amended in April 2013. Upon entering into the agreement, AstraZeneca entered into a common stock purchase agreement pursuant to which we agreed to sell to AstraZeneca an aggregate of \$25.0 million of our common stock in a separate private placement concurrent with the completion of this offering. These agreements are described under **Business Our Strategic Alliances**.

In August 2012, we entered into a collaboration and license agreement with Biogen Idec, which the parties amended in June 2013. Upon entering into the agreement, Biogen Idec loaned \$5.0 million to us under a convertible promissory note. These agreements are described under **Business Our Strategic Alliances**.

In December 2012, we entered into a material transfer agreement with Alnylam Pharmaceuticals, Inc. for the purchase of GalNAc conjugate, a component of our drug product. We paid to Alnylam \$150,000 for time and materials. In March 2013, we agreed to purchase additional GalNAc conjugate for our GLP studies and for Alnylam's time to support the transfer of the GalNAc technologies to us and to our contract manufacturers. We expect to pay approximately \$500,000 during 2013 for these activities consisting of pass through costs for the manufacture of the GalNAc conjugate and the time of Alnylam's employees required in the manufacture of the conjugate and the technology transfer.

EMPLOYMENT ARRANGEMENTS

We have entered into written employment agreements with our executive officers, including our President and Chief Executive Officer, Kleanthis G. Xanthopoulos, Ph.D., our former Chief Operating Officer and Executive Vice President, Finance, Garry E. Menzel, Ph.D., and our Chief Scientific Officer, Neil W. Gibson, Ph.D. These agreements are described under **Executive and director compensation** in our Proxy Statement on Schedule 14A incorporated by reference herein.

STOCK OPTIONS GRANTED TO EXECUTIVE OFFICERS AND DIRECTORS

We have granted stock options to our executive officers and directors, as more fully described under **Executive and director compensation** in our Proxy Statement on Schedule 14A incorporated by reference herein.

INDEMNIFICATION AGREEMENTS

We have entered into separate indemnification agreements with our directors and executive officers, in addition to the indemnification provided for in our amended and restated bylaws. These agreements, among other things, require us to indemnify our directors and executive officers for certain expenses, including attorneys' fees, judgments, fines and settlement amounts incurred by a director or executive officer in any action or proceeding arising out of his or her services as one of our directors or executive officers or any other company or enterprise to which the person provides services at our request. We believe that these indemnification agreements, together with the provisions in our bylaws, are necessary to attract and retain qualified persons as directors and officers.

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Certain relationships and related party transactions

POLICIES AND PROCEDURES FOR TRANSACTIONS WITH RELATED PERSONS

We have adopted a written related-person transactions policy that sets forth our policies and procedures regarding the identification, review, consideration, approval and oversight of related-person transactions. For purposes of our policy only, a related-person transaction is a past, present or future transaction, arrangement or relationship (or any series of similar transactions, arrangements or relationships) in which we and any related person are participants involving an amount that exceeds \$120,000.

Transactions involving compensation for services provided to us by an employee, consultant or director will not be considered related-person transactions under this policy. A related person, as determined since the beginning of our last fiscal year, is any executive officer, director or a holder of more than five percent of our common stock, including any of their immediate family members and any entity owned or controlled by such persons.

The policy imposes an affirmative duty upon each director and executive officer to identify, and we will request that significant stockholders identify, any transaction involving them, their affiliates or immediate family members that may be considered a related party transaction before such person engages in the transaction. Under the policy, where a transaction has been identified as a related-person transaction, management must present information regarding the proposed related-person transaction to our audit committee (or, where review by our audit committee would be inappropriate, to another independent body of our board of directors) for review. The presentation must include a description of, among other things, the material facts, the direct and indirect interests of the related persons, the benefits of the transaction to us and whether any alternative transactions are available. In considering related-person transactions, our audit committee or other independent body of our board of directors takes into account the relevant available facts and circumstances including, but not limited to:

- ∅ the risks, costs and benefits to us of the transaction;
- ∅ the impact on a director's independence in the event the related person is a director, immediate family member of a director or an entity with which a director is affiliated;
- ∅ the terms of the transaction;
- ∅ the availability of other sources for comparable services or products; and
- ∅ the terms available to or from, as the case may be, unrelated third parties or to or from our employees generally.

In the event a director has an interest in the proposed transaction, the director must recuse himself or herself from the deliberations and approval. Our policy requires that, in reviewing a related party transaction, our audit committee must consider, in light of known circumstances, and determine in the good faith exercise of its discretion whether the transaction is in, or is not inconsistent with, the best interests of us and our stockholders.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

None of our current or former executive officers serves as a member of the compensation committee. None of our officers serves, or has served during the last completed fiscal year on the board of directors or compensation committee, or other committee serving an equivalent function, of any other entity that has one or more of its executive officers serving as a member of our board of directors or our compensation committee. Prior to establishing the compensation committee, our full board of directors made decisions relating to compensation of our officers.

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Principal stockholders

The following table sets forth information regarding beneficial ownership of our capital stock as of May 31, 2013 by:

Ø each person, or group of affiliated persons, known by us to beneficially own more than 5% of our common stock;

Ø each of our directors;

Ø each of our named executive officers; and

Ø all of our directors and current executive officers as a group.

The numbers of shares and percentage ownership information before the offering is based on 36,052,587 shares of common stock outstanding as of May 31, 2013. The numbers of shares and percentage ownership information after the offering is based on the sale of shares of common stock in this offering.

Information with respect to beneficial ownership has been furnished by each director, officer or beneficial owner of more than 5% of our common stock. We have determined beneficial ownership in accordance with the rules of the SEC. These rules generally attribute beneficial ownership of securities to persons who possess sole or shared voting power or investment power with respect to those securities. In addition, the rules include shares of common stock issuable pursuant to the exercise of stock options that are either immediately exercisable or exercisable on or before July 30, 2013 which is 60 days after May 31, 2013. These shares are deemed to be outstanding and beneficially owned by the person holding those options for the purpose of computing the percentage ownership of that person, but they are not treated as outstanding for the purpose of computing the percentage ownership of any other person. Unless otherwise indicated, the persons or entities identified in this table have sole voting and investment power with respect to all shares shown as beneficially owned by them, subject to applicable community property laws.

Table of Contents**Principal stockholders**

Except as otherwise noted below, the address for each person or entity listed in the table is c/o Regulus Therapeutics Inc., 3545 John Hopkins Court, Suite 210, San Diego, California 92121.

Name and address of beneficial owner	Number of shares		Percentage of shares		
	beneficially owned		beneficially owned		
	before offering ⁽¹⁾	after offering	before offering	after offering	
5% or greater stockholders					
Isis Pharmaceuticals, Inc. ⁽²⁾ 2855 Gazelle Court Carlsbad, CA 92010	7,074,500	7,074,500	19.6%		
AstraZeneca AB SE-431 83 Molndal Sweden	6,250,000	6,250,000	17.3%		
Alnylam Pharmaceuticals, Inc. 300 Third Street, 3 rd Floor Cambridge, MA 02142	6,150,500	6,150,500	17.1%		
Aventis Holdings, Inc. c/o Sanofi 54, rue La Boétie 75414 Paris France	3,749,999	3,749,999	10.4%		
Glaxo Group Limited ⁽³⁾	3,340,182	3,340,182	8.9%		
	\$ 12,516	\$ 3,839	\$ —	\$ 129,758	
Income/(loss) from operations	\$ 26,487	\$ 4,130	\$ (260)	\$ 599	
Interest income, net				\$(3,841)	
Other income, net				\$ 27,115	
Income before income taxes				53	
				536	
				\$ 26,526	
Six Months Ended October 26, 2013					
	Automotive	Interconnect	Power Products	Other	Eliminations/Corporate
Net sales	\$ 230,396	\$ 88,609	\$ 36,205	\$ 5,040	\$ (2,070)
Transfers between segments	(845)	(1,271)	(117)	(71)	2,304
Net sales to unaffiliated customers	\$ 229,551	\$ 87,338	\$ 36,088	\$ 4,969	\$ 234
					\$ 358,180
					\$ 358,180

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Income (loss) from operations	\$30,420	\$14,323	\$6,038	\$(149)) \$ (13,770))	\$36,862
Interest expense, net							177
Other expense, net							493
Income before income taxes							\$36,192

Six Months Ended October 27, 2012

	Automotive	Interconnect	Power Products	Other	Eliminations/Corporate	Consolidated	
Net sales	\$151,606	\$66,270	\$24,740	\$7,745	\$ (1,865)) \$248,496	
Transfers between segments	(408)) (1,305)) (105)) (39)) 1,857) —	
Net sales to unaffiliated customers	\$151,198	\$64,965	\$24,635	\$7,706	\$ (8)) \$248,496	
Income (loss) from operations	\$29,147	\$9,004	\$51	\$1,548	\$ (8,465)) \$31,285	
Interest expense, net							7
Other expense, net							495
Income before income taxes							\$30,783

METHODE ELECTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
(Dollar amounts in thousands, except per share data)

8. CONTINGENCIES

Delphi Settlement

In September 2012, the Company and various Delphi parties settled all Delphi related litigation matters. In addition to resolving all claims between the parties, the Company assigned certain patents to Delphi and entered into a non-compete with respect to the related technology. In exchange, the Company received a payment of \$20,000, half of which was paid in October 2012 and half of which was paid in January 2013. The Company recorded the entire gain in the second quarter of fiscal 2013, in the income from settlement section of our consolidated statement of operations.

Certain litigation arising in the normal course of business is pending against us. We are from time to time subject to various legal actions and claims incidental to our business, including those arising out of alleged defects, breach of contracts, employment-related matters and environmental matters. We consider insurance coverage and third-party indemnification when determining required accruals for pending litigation and claims. Although the outcome of potential legal actions and claims cannot be determined, it is our opinion, based on the information available, that we have adequate reserves for these liabilities.

9. PRE-PRODUCTION COSTS RELATED TO LONG-TERM SUPPLY ARRANGEMENTS

We incur pre-production tooling costs related to certain products produced for our customers under long-term supply agreements. We had \$16,138 and \$11,511 as of October 26, 2013 and April 27, 2013, respectively, of pre-production tooling costs related to customer-owned tools for which reimbursement is contractually guaranteed by the customer or for which the customer has provided a non-cancelable right to use the tooling. Engineering, testing and other costs incurred in the design and development of production parts are expensed as incurred, unless the costs are reimbursable, as specified in a customer contract.

10. DEBT AND CREDIT AGREEMENT

We are party to an Amended and Restated Credit Agreement with Bank of America, N.A., as administrative agent, and certain other financial institutions, which has a maturity of September 21, 2017. The credit facility is in the aggregate principal amount of \$100,000, with an option to increase the principal amount by an additional \$50,000, subject to customary conditions and approval of the lender(s) providing new commitment(s). The credit facility provides for variable rates of interest based on the type of borrowing and the Company's debt to EBITDA financial ratio. The Amended and Restated Credit Agreement is guaranteed by certain of our U.S. subsidiaries. At October 26, 2013, the interest rate on the credit facility was 1.5% plus LIBOR. At October 26, 2013, we were in compliance with the covenants of the agreement. During the first half of fiscal 2014, we had borrowings of \$21,500 and payments of \$13,986, which includes interest of \$486 under this credit facility. As of October 26, 2013, there were outstanding balances against the credit facility of \$51,500. There was \$48,500 available to borrow under the credit facility as of October 26, 2013, which does not include the option to increase the principal amount. We believe the fair value approximates the carrying amount as of October 26, 2013.

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

Cautionary Statement

Certain statements in this report are forward-looking statements that are subject to certain risks and uncertainties. We undertake no duty to update any such forward-looking statements to conform to actual results or changes in our expectations. Our business is highly dependent upon two large automotive customers and specific makes and models of automobiles. Our results will be subject to many of the same risks that apply to the automotive, appliance, computer and communications industries, such as general economic conditions, interest rate fluctuations, consumer spending patterns and technological changes. Other factors which may result in materially different results for future periods include the following risk factors. Additional risks and uncertainties not presently known or that our management currently believe to be insignificant may also adversely affect our financial condition or results of operations. These risk factors should be considered in connection with evaluating the forward-looking statements contained in this report because these factors could cause our actual results and condition to differ materially from those projected in forward-looking statements. The forward-looking statements in this report are subject to the safe harbor protection provided under the securities laws and are made as of the date of this report.

Our business is highly dependent on two large automotive customers. If we were to lose either of these customers or experienced a significant decline in the volume or price of products purchased by these customers, or if either of the customers declare bankruptcy, our future results could be adversely affected.

Because we derive a substantial portion of our revenues from customers in the automotive, appliance, computer and communications industries, we are susceptible to trends and factors affecting those industries.

We face risks relating to our international operations, including political and economic instability, expropriation, or the imposition of government controls.

Our inability to effectively manage the timing, quality and cost of new program launches could adversely affect our financial performance.

Products we manufacture may contain design or manufacturing defects that could result in reduced demand for our products or services and liability claims against us.

Our technology-based business and the markets in which we operate are highly competitive. If we are unable to compete effectively, our sales could decline.

We are dependent on the availability and price of materials.

Disruption of our supply chain could have an adverse effect on our business, financial condition and results of operations.

Downturns in the automotive industry or the bankruptcy of certain automotive customers could reduce the sales and profitability of our business.

We may be unable to keep pace with rapid technological changes, which could adversely affect our business.

If we are unable to protect our intellectual property or we infringe, or are alleged to infringe, on another person's intellectual property, our business, financial condition and operating results could be materially adversely affected.

• We are subject to continuing pressure to lower our prices.

- We currently have a significant amount of our cash located outside the U.S.

• We may be required to recognize impairment charges for our goodwill and indefinite-lived intangible assets.

• A significant fluctuation between the U.S. dollar and other currencies could adversely impact our operating results.

• We may acquire businesses or divest business operations. These transactions may pose significant risks and may materially adversely affect our business, financial condition and operating results.

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• We could suffer significant business interruptions.

• Unfavorable tax law changes may adversely affect our financial results.

• Our information technology (“IT”) systems could be breached.

• The SEC's annual disclosure and reporting requirements for those companies who use conflict minerals mined from the Democratic Republic of Congo (DRC) and adjoining countries may be difficult and costly to implement.

Any such forward-looking statements are not guarantees of future performance and actual results, developments and business decisions may differ materially from those foreseen in such forward-looking statements. These forward-looking statements speak only as of the date of the report, press release, statement, document, webcast or oral discussion in which they are made. We do not intend to update any forward-looking statements, all of which are expressly qualified by the foregoing. See Part I — Item 1A, Risk Factors of our Form 10-K for the fiscal year ended April 27, 2013, for a further discussion regarding some of the reasons that actual results may be materially different from those we anticipate.

Overview

We are a global manufacturer of component and subsystem devices with manufacturing, design and testing facilities in China, Egypt, Germany, India, Italy, Lebanon, Malta, Mexico, the Philippines, Singapore, Switzerland, the United Kingdom and the United States. We are a global designer and manufacturer of electronic and electro-mechanical devices. We design, manufacture and market devices employing electrical, radio remote control, electronic, wireless, sensing and optical technologies. Our business is managed on a segment basis, with those segments being Automotive, Interconnect, Power Products and Other. For more information regarding the business and products of these segments, see “Item 1. Business.” of our Form 10-K for the fiscal year ended April 27, 2013.

Our components are found in the primary end markets of the aerospace, appliance, automotive, construction, consumer and industrial equipment markets, communications (including information processing and storage, networking equipment, wireless and terrestrial voice/data systems), rail and other transportation industries.

Delphi Settlement

In September 2012, the Company and various Delphi parties settled all Delphi related litigation matters. In addition to resolving all claims between the parties, the Company assigned certain patents to Delphi and entered into a non-compete with respect to the related technology. In exchange, the Company received a payment of \$20.0 million, half of which was paid in October 2012 and half of which was paid in January 2013. The Company recorded the entire gain in the second quarter of fiscal 2013, in the income from settlement section of our consolidated statement of operations.

Hetronic Italy Transaction

In September 2012, we acquired certain assets of Hetronic South Europe S.R.L. for \$1.4 million in cash, as well as the forgiveness of debt owed to the Company of \$1.3 million, for total consideration of \$2.7 million. We operate this business under the name Hetronic Italy. The business, located in Milan, Italy, is a market leader in industrial safety radio remote controls, primarily serving the Italian market. The accounts and transactions of Hetronic Italy have been included in the Hetronic Group in the Interconnect segment in the consolidated financial statements from the effective date of the acquisition.

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Results of Operations for the Three Months Ended October 26, 2013 as Compared to the Three Months Ended October 27, 2012

Consolidated Results

Below is a table summarizing results for the three months ended:

(\$ in millions)

("N/M" equals not meaningful)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$190.9	\$129.8	\$61.1	47.1	%
Cost of products sold	149.5	107.5	42.0	39.1	%
Gross profit	41.4	22.3	19.1	85.7	%
Selling and administrative expenses	19.7	15.2	4.5	29.6	%
Income from settlement	—	(20.0)	20.0	N/M	
Interest expense, net	0.1	0.1	—	—	%
Other expense, net	0.4	0.5	(0.1)	(20.0))%
Income tax expense	1.4	3.2	(1.8)	(56.3))%
Net loss attributable to noncontrolling interest	—	(0.1)	0.1	N/M	
Net income attributable to Methode Electronics, Inc.	\$19.8	\$23.4	\$(3.6)	(15.4))%
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	78.3	% 82.8	%		
Gross margins	21.7	% 17.2	%		
Selling and administrative expenses	10.3	% 11.7	%		
Income from settlement	—	% (15.4))%		
Interest expense, net	0.1	% 0.1	%		
Other expense, net	0.2	% 0.4	%		
Income tax expense	0.7	% 2.5	%		
Net loss attributable to noncontrolling interest	—	% (0.1))%		
Net income attributable to Methode Electronics, Inc.	10.4	% 18.0	%		

Net Sales. Consolidated net sales increased \$61.1 million, or 47.1%, to \$190.9 million for the three months ended October 26, 2013, from \$129.8 million for the three months ended October 27, 2012. The Automotive segment net sales increased \$45.9 million, or 57.2%, to \$126.1 million for the second quarter of fiscal 2014, from \$80.2 million for the second quarter of fiscal 2013 primarily related to the GM Center Console program, which launched in the first quarter of fiscal 2014, and increased sales volumes for steering-angle sensors, and visible and hidden switch product lines. The Interconnect segment net sales increased \$10.3 million, or 30.9%, to \$43.6 million for the second quarter of fiscal 2014, compared to \$33.3 million for the second quarter of fiscal 2013, primarily due to higher sales volumes in appliance and data products. The Power Products segment net sales increased \$6.2 million, or 49.6%, to \$18.7 million for the second quarter of fiscal 2014, compared to \$12.5 million for the second quarter of fiscal 2013, primarily due to higher sales volumes for cabling and busbar products. The Other segment net sales decreased \$1.5 million, or 39.5%, to \$2.3 million for the second quarter of fiscal 2014, as compared to \$3.8 million for the second quarter of fiscal 2013, primarily due to lower sales volumes for our torque-sensing products. Translation of foreign operations net sales for

the three months ended October 26, 2013 increased reported net sales by \$1.9 million or 1.0% due to average currency rate fluctuations in the second quarter of fiscal 2014, compared to the second quarter of fiscal 2013, primarily due to the strengthening of the Euro compared to the U.S. dollar.

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Cost of Products Sold. Consolidated cost of products sold increased \$42.0 million, or 39.1%, to \$149.5 million for the three months ended October 26, 2013, compared to \$107.5 million for the three months ended October 27, 2012. Consolidated cost of products sold as a percentage of sales was 78.3% for the second quarter of fiscal 2014, compared to 82.8% for the second quarter of fiscal 2013. The Automotive segment experienced a decrease in cost of goods sold as a percentage of sales due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding operation into our manufacturing processes. The Interconnect segment experienced a slight decrease in cost of products sold as a percentage of sales primarily due to manufacturing efficiencies related to higher sales volumes for our appliance products. The Power Products segment experienced a decrease in cost of products sold as a percentage of sales primarily due to lower development costs, favorable commodity pricing for raw materials and favorable product sales mix.

Gross Profit. Consolidated gross profit increased \$19.1 million, or 85.7%, to \$41.4 million for the three months ended October 26, 2013, as compared to \$22.3 million for the three months ended October 27, 2012. Gross margins as a percentage of net sales increased to 21.7% for the three months ended October 26, 2013, compared to 17.2% for the three months ended October 27, 2012. The increase is primarily due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding facility in our manufacturing process in the Automotive segment. The Interconnect segment experienced a slight increase in gross margins as a percentage of sales primarily due to higher sales volumes for our appliance products. The Power Products segment experienced an increase in gross margins as a percentage of sales primarily due to favorable commodity pricing for raw materials and favorable product sales mix.

Selling and Administrative Expenses. Selling and administrative expenses increased by \$4.5 million, or 29.6%, to \$19.7 million for the three months ended October 26, 2013, compared to \$15.2 million for the three months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales decreased to 10.3% for the three months ended October 26, 2013 from 11.7% for the three months ended October 27, 2012. The decrease is primarily due to higher sales volumes. The selling and administrative expenses in the second quarter of fiscal 2013 benefitted from a \$1.1 million reversal of various accruals related to a customer bankruptcy. In the second quarter of fiscal 2014, performance-based compensation expense increased \$2.7 million, primarily related to increased sales and net income levels, excluding the income from settlement from the fiscal 2013 results. In addition, expenses for marketing, travel and legal expenses increased \$0.7 million.

Income From Settlement. In September 2012, the Company and various Delphi parties settled all Delphi related litigation matters. In addition to resolving all claims between the parties, the Company assigned certain patents to Delphi and entered into a non-compete agreement with respect to the related technology. In exchange, the Company received a payment of \$20.0 million, half of which was paid in October 2012 and the other half was paid in January 2013. The Company recorded the entire gain in the second quarter of fiscal 2013, in the income from settlement section of our consolidated statement of operations.

Interest Expense, Net. Interest expense, net was flat at \$0.1 million for both the three months ended October 26, 2013 and October 27, 2012.

Other Expense, Net. Other expense, net decreased \$0.1 million, to \$0.4 million for the three months ended October 26, 2013, compared to \$0.5 million for the three months ended October 27, 2012. All amounts for both the second quarter of fiscal 2014 and fiscal 2013, relate to currency rate fluctuations. The functional currencies of these operations are the British pound, Chinese yuan, Euro, Indian Rupee, Mexican peso, Singapore dollar and Swiss Franc. Some foreign operations have transactions denominated in currencies other than their functional currencies, primarily sales in U.S. dollars and Euros, creating exchange rate sensitivities.

Income Tax Expense. Income tax expense decreased \$1.8 million, or 56.3%, to \$1.4 million for the three months ended October 26, 2013, compared to \$3.2 million for the three months ended October 27, 2012. The income tax expense for both the second quarter of fiscal 2014 and fiscal 2013 relates to income taxes on foreign profits.

Net Income Attributable to Methode Electronics, Inc. Net income attributable to Methode Electronics, Inc. decreased \$3.6 million, or 15.4%, to \$19.8 million for the three months ended October 26, 2013, compared to \$23.4 million for the three months ended October 27, 2012. The fiscal 2014 second quarter benefitted from the GM Center Console Program, higher sales volumes and manufacturing efficiencies. The fiscal 2013 second quarter benefitted from the \$20.0 million settlement and the \$1.1 million reversal of various accruals related to a customer bankruptcy.

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Operating Segments

Automotive Segment Results

Below is a table summarizing results for the three months ended:

(\$ in millions)

("N/M" equals not meaningful)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$126.1	\$80.2	\$45.9	57.2	%
Cost of products sold	101.3	68.3	33.0	48.3	%
Gross profit	24.8	11.9	12.9	108.4	%
Selling and administrative expenses	6.8	5.4	1.4	25.9	%
Income from settlement	—	(20.0)	20.0	N/M	
Income from operations	\$18.0	\$26.5	\$(8.5)	(32.1)	%
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	80.3	% 85.2	%		
Gross margins	19.7	% 14.8	%		
Selling and administrative expenses	5.4	% 6.7	%		
Income from settlement	—	% (24.9)	%		
Income from operations	14.3	% 33.0	%		

Net Sales. Automotive segment net sales increased \$45.9 million, or 57.2%, to \$126.1 million for the three months ended October 26, 2013, from \$80.2 million for the three months ended October 27, 2012. Net sales increased in North America \$38.5 million, or 147.5%, to \$64.6 million in the second quarter of fiscal 2014, compared to \$26.1 million in the second quarter of fiscal 2013 primarily due to the GM Center Console Program, which launched in the first quarter of fiscal 2014, partially offset with decreased sales volumes for our Ford Center Console Program and our transmission lead-frame assembly. Net sales increased in Europe by \$6.1 million, or 16.8%, to \$42.5 million in the second quarter of fiscal 2014, compared to \$36.4 million in the second quarter of fiscal 2013, primarily due to hidden and visible switch products as well as currency rate fluctuations. Net sales in Asia increased \$1.3 million, or 7.3%, to \$19.0 million in the second quarter of fiscal 2014, compared to \$17.7 million in the second quarter of fiscal 2013, primarily due to increased sales volumes for our steering-angle sensor products. Translation of foreign operations net sales for the three months ended October 26, 2013 increased reported net sales by \$1.9 million, or 1.5%, due to average currency rates in the second quarter of fiscal 2014, compared to the average currency rates in the second quarter of fiscal 2013, primarily due to the strengthening of the Euro as compared to the U.S. dollar.

Cost of Products Sold. Automotive segment cost of products sold increased \$33.0 million, or 48.3%, to \$101.3 million for the three months ended October 26, 2013, from \$68.3 million for the three months ended October 27, 2012. The Automotive segment cost of products sold as a percentage of sales decreased to 80.3% in the second quarter of fiscal 2014, compared to 85.2% in the second quarter of fiscal 2013. The decrease is primarily due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding operation into our manufacturing processes.

Gross Profit. Automotive segment gross profit increased \$12.9 million, or 108.4%, to \$24.8 million for the three months ended October 26, 2013, as compared to \$11.9 million for the three months ended October 27, 2012. The Automotive segment gross margins as a percentage of net sales were 19.7% for the three months ended October 26, 2013, as compared to 14.8% for the three months ended October 27, 2012. The increase is primarily due to increased manufacturing efficiencies

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related to the increased sales volumes and the vertical integration of our paint and decorative molding facility in our manufacturing process.

Selling and Administrative Expenses. Selling and administrative expenses increased \$1.4 million, or 25.9%, to \$6.8 million for the three months ended October 26, 2013, compared to \$5.4 million for the three months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales were 5.4% for the three months ended October 26, 2013 and 6.7% for the three months ended October 27, 2012. The selling and administrative expenses in the second quarter of fiscal 2013 benefitted from a \$1.1 million reversal of various accruals related to a customer bankruptcy. Legal expenses decreased \$0.3 million in the second quarter of fiscal 2014, primarily due to the settlement of the Delphi litigation in the second quarter of fiscal 2013, more than offset with higher selling and administrative expenses at our Chinese and European operations of \$0.2 million and \$0.3 million, respectively.

Income From Settlement. In September 2012, the Company and various Delphi parties settled all Delphi related litigation matters. In addition to resolving all claims between the parties, the Company assigned certain patents to Delphi and entered into a non-compete agreement with respect to the related technology. In exchange, the Company received a payment of \$20.0 million, half of which was paid in October 2012 and the other half was paid in January 2013. The Company recorded the entire gain in the second quarter of fiscal 2013, in the income from settlement section of our consolidated statement of operations.

Income from Operations. Automotive segment income from operations decreased \$8.5 million, or 32.1%, to \$18.0 million for the three months ended October 26, 2013, compared to \$26.5 million for the three months ended October 27, 2012. The fiscal 2014 second quarter benefitted from the GM Center Console Program, higher sales volumes and manufacturing efficiencies. The fiscal 2013 second quarter benefitted from the \$20.0 million settlement and the \$1.1 million reversal of various accruals related to a customer bankruptcy.

Interconnect Segment Results

Below is a table summarizing results for the three months ended:
(\$ in millions)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$43.6	\$33.3	\$10.3	30.9	%
Cost of products sold	32.4	24.8	7.6	30.6	%
Gross profit	11.2	8.5	2.7	31.8	%
Selling and administrative expenses	4.3	4.4	(0.1)	(2.3))%
Income from operations	\$6.9	\$4.1	\$2.8	68.3	%
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	74.3	% 74.5	%		
Gross margins	25.7	% 25.5	%		
Selling and administrative expenses	9.9	% 13.2	%		
Income from operations	15.8	% 12.3	%		

Net Sales. Interconnect segment net sales increased \$10.3 million, or 30.9%, to \$43.6 million for the three months ended October 26, 2013, from \$33.3 million for the three months ended October 27, 2012. Net sales increased in North America by \$10.9 million, or 45.0%, to \$35.1 million in the second quarter of fiscal 2014, compared to \$24.2 million in the second quarter of fiscal 2013, primarily due to stronger sales volumes for our appliance, data solutions and radio remote control

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products. Net sales in Europe decreased \$0.8 million, or 13.6%, to \$5.1 million in the second quarter of fiscal 2014, compared to \$5.9 million in the second quarter of fiscal 2013, primarily due to lower radio remote control and sensor sales volumes. Net sales in Asia increased \$0.2 million, or 6.2%, to \$3.4 million in the second quarter of fiscal 2014, compared to \$3.2 million in the second quarter of fiscal 2013, primarily due to higher radio remote control sales, partially offset with lower sales volumes from certain legacy products resulting from the planned exit of a product line.

Cost of Products Sold. Interconnect segment cost of products sold increased \$7.6 million, or 30.6%, to \$32.4 million for the three months ended October 26, 2013, compared to \$24.8 million for the three months ended October 27, 2012. Interconnect segment cost of products sold as a percentage of net sales decreased slightly to 74.3% for the three months ended October 26, 2013, compared to 74.5% for the three months ended October 27, 2012. The decrease in cost of products sold as a percentage of sales is primarily due to manufacturing efficiencies related to higher sales volumes for our appliance products.

Gross Profit. Interconnect segment gross profit increased \$2.7 million, or 31.8%, to \$11.2 million for the three months ended October 26, 2013, compared to \$8.5 million for the three months ended October 27, 2012. Gross margins as a percentage of net sales increased slightly to 25.7% for the three months ended October 26, 2013, from 25.5% for the three months ended October 27, 2012. The increase in gross margins as a percentage of sales is primarily due to manufacturing efficiencies related to higher sales volumes for our appliance products.

Selling and Administrative Expenses. Selling and administrative expenses decreased slightly by \$0.1 million, or 2.3%, to \$4.3 million for the three months ended October 26, 2013, compared to \$4.4 million for the three months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales decreased to 9.9% for the three months ended October 26, 2013, from 13.2% for the three months ended October 27, 2012. The decrease is primarily due to higher sales volumes.

Income from Operations. Interconnect segment income from operations increased \$2.8 million, or 68.3%, to \$6.9 million for the three months ended October 26, 2013, compared to \$4.1 million for the three months ended October 27, 2012, primarily due to higher sales volumes and slightly lower selling and administrative expenses.

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Power Products Segment Results

Below is a table summarizing results for the three months ended:

(\$ in millions)

("N/M" equals not meaningful)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$ 18.7	\$ 12.5	\$ 6.2	49.6	%
Cost of products sold	13.8	11.0	2.8	25.5	%
Gross profit	4.9	1.5	3.4	226.7	%
Selling and administrative expenses	1.3	1.8	(0.5)	(27.8))%
Income/(loss) from operations	\$ 3.6	\$ (0.3)	\$ 3.9	N/M	
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	73.8	% 88.0	%		
Gross margins	26.2	% 12.0	%		
Selling and administrative expenses	7.0	% 14.4	%		
Income/(loss) from operations	19.3	% (2.4))%		

Net Sales. Power Products segment net sales increased \$6.2 million, or 49.6%, to \$18.7 million for the three months ended October 26, 2013, compared to \$12.5 million for the three months ended October 27, 2012. Net sales increased in North America by \$2.4 million, or 28.6%, to \$10.8 million in the second quarter of fiscal 2014, compared to \$8.4 million in the second quarter of fiscal 2013, primarily due to higher sales volumes for our cabling and busbar products, partially offset by lower sales volumes for our heat sink products. Net sales in Europe increased \$2.8 million, or 560.0%, to \$3.3 million in the second quarter of fiscal 2014, compared to \$0.5 million in the second quarter of fiscal 2012, due to sales of a by-pass switch for a substation and busbars for electric vehicles. Net sales in Asia increased \$1.0 million, or 27.8%, to \$4.6 million in the second quarter of fiscal 2014, compared to \$3.6 million in the second quarter of fiscal 2013, primarily due to increased sales volumes of busbar and cabling assemblies.

Cost of Products Sold. Power Products segment cost of products sold increased \$2.8 million, or 25.5%, to \$13.8 million for the three months ended October 26, 2013, compared to \$11.0 million for the three months ended October 27, 2012. The Power Products segment cost of products sold as a percentage of sales decreased to 73.8% for the three months ended October 26, 2013, from 88.0% for the three months ended October 27, 2012. The decrease in cost of products sold as a percentage of sales is primarily due to higher sales volumes, lower product development costs, favorable commodity pricing for raw materials and favorable product sales mix.

Gross Profit. Power Products segment gross profit increased \$3.4 million, or 226.7%, to \$4.9 million in the second quarter of fiscal 2014, compared to \$1.5 million in the second quarter of fiscal 2013. Gross margins as a percentage of net sales increased to 26.2% for the three months ended October 26, 2013 from 12.0% for the three months ended October 27, 2012. The increase in gross margins is primarily due to higher sales volumes, lower product development costs, favorable commodity pricing for raw materials and favorable product sales mix.

Selling and Administrative Expenses. Selling and administrative expenses decreased \$0.5 million, or 27.8%, to \$1.3 million for the three months ended October 26, 2013, compared to \$1.8 million for the three months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales decreased to 7.0% for the three months ended October 26, 2013 from 14.4% for the three months ended October 27, 2012. Selling and administrative expenses decreased due to lower commission and bonus expense in North America.

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Income/(Loss) From Operations. Power Products segment income/(loss) from operations increased \$3.9 million, to income of \$3.6 million for the three months ended October 26, 2013, compared to a loss of \$0.3 million for the three months ended October 27, 2012, due to higher sales, favorable commodity pricing for raw materials, favorable product mix and lower selling and administrative expenses.

Other Segment Results

Below is a table summarizing results for the three months ended:
(\$ in millions)

	October 26, 2013	October 27, 2012	Net Change	Net Change
Net sales	\$2.3	\$3.8	\$(1.5)	(39.5)%
Cost of products sold	2.0	2.6	(0.6)	(23.1)%
Gross profit	0.3	1.2	(0.9)	(75.0)%
Selling and administrative expenses	0.6	0.6	—	— %
Income/(loss) from operations	\$(0.3)	\$0.6	\$(0.9)	N/M
Percent of sales:	October 26, 2013	October 27, 2012		
Net sales	100.0	% 100.0	%	
Cost of products sold	87.0	% 68.4	%	
Gross margins	13.0	% 31.6	%	
Selling and administrative expenses	26.1	% 15.8	%	
Income/(loss) from operations	(13.0)%	15.8	%	

Net Sales. The Other segment net sales decreased \$1.5 million, or 39.5%, to \$2.3 million for the three months ended October 26, 2013, compared to \$3.8 million for the three months ended October 27, 2012. Net sales from our torque-sensing business decreased 65.3% in the second quarter of fiscal 2014, compared to the second quarter of fiscal 2013, primarily due to the planned exit of certain product lines and lower demand in the e-bike and motorcycle markets. Net sales from our testing facilities decreased 6.6%, primarily due to lower vibration shock testing sales in the second quarter of fiscal 2014, compared to the second quarter of fiscal 2013.

Cost of Products Sold. Other segment cost of products sold decreased \$0.6 million to \$2.0 million for the three months ended October 26, 2013, compared to \$2.6 million for the three months ended October 27, 2012. Cost of products sold as a percentage of sales increased to 87.0% in the second quarter of fiscal 2014, compared to 68.4% in the second quarter of fiscal 2013. The increase in cost of products sold as a percentage of sales is primarily due to manufacturing inefficiencies as a result of lower sales volumes in our torque-sensing business. In addition, our torque sensing business experienced additional manufacturing inefficiencies due to a move of production from our North American facility to our Malta facility, which occurred during the second quarter of fiscal 2014.

Gross Profit. The Other segment gross profit decreased \$0.9 million, or 75.0%, to \$0.3 million for the three months ended October 26, 2013, compared to \$1.2 million for the three months ended October 27, 2012. The gross margins as a percentage of sales decreased to 13.0% for the three months ended October 26, 2013, compared to 31.6% for the three months ended October 27, 2012. The decrease in gross margins as a percentage of sales is primarily due to efficiencies caused by significantly lower sales volumes and the move of production from North America to Malta.

Selling and Administrative Expenses. Selling and administrative expenses were flat at \$0.6 million for both the three months ended October 26, 2013 and three months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales increased to 26.1% for the three months ended October 26, 2013, from 15.8% for the three months ended October 27, 2012.

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Income/(Loss) From Operations The Other segment income/(loss) from operations decreased \$0.9 million, to a loss of \$0.3 million for the three months ended October 26, 2013, compared to income of \$0.6 million for the three months ended October 27, 2012. The decrease was primarily due to significantly lower sales volumes and production inefficiencies as a result of the planned move of production from North America to Malta.

Results of Operations for the Six Months Ended October 26, 2013 as Compared to the Six Months Ended October 27, 2012

Consolidated Results

Below is a table summarizing results for the six months ended:

(\$ in millions)

("N/M" equals not meaningful)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$358.2	\$248.5	\$109.7	44.1	%
Cost of products sold	282.8	204.7	78.1	38.2	%
Gross profit	75.4	43.8	31.6	72.1	%
Selling and administrative expenses	38.6	32.5	6.1	18.8	%
Income from settlement	—	(20.0)	20.0	N/M	
Interest expense, net	0.2	—	0.2	N/M	
Other expense, net	0.5	0.5	—	—	%
Income tax expense	2.7	3.7	(1.0)	(27.0))%
Net loss attributable to noncontrolling interest	—	(0.1)	0.1	N/M	
Net income attributable to Methode Electronics, Inc.	\$33.4	\$27.2	\$6.2	22.8	%
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	79.0	% 82.4	%		
Gross margins	21.0	% 17.6	%		
Selling and administrative expenses	10.8	% 13.1	%		
Income from settlement	—	% (8.0))%		
Interest expense, net	0.1	% —	%		
Other expense, net	0.1	% 0.2	%		
Income tax expense	0.8	% 1.5	%		
Net loss attributable to noncontrolling interest	—	% —	%		
Net income attributable to Methode Electronics, Inc.	9.3	% 10.9	%		

Net Sales. Consolidated net sales increased \$109.7 million, or 44.1%, to \$358.2 million for the six months ended October 26, 2013, from \$248.5 million for the six months ended October 27, 2012. The Automotive segment net sales increased \$78.4 million, or 51.9%, to \$229.6 million for the first half of fiscal 2014, from \$151.2 million for the first half of fiscal 2013, primarily related to the GM Center Console Program, which launched in the first quarter of fiscal 2014, higher sales volumes for steering-angle sensor, and visible and hidden switch product lines. The Interconnect segment net sales increased \$22.3 million, or 34.3%, to \$87.3 million for the first half of fiscal 2014, compared to

\$65.0 million for the first half of fiscal 2013, primarily due to higher sales volumes in appliance and data products. The Power Products segment net sales increased \$11.5 million, or 46.7%, to \$36.1 million for the first half of fiscal 2014, compared to \$24.6 million for the first half of fiscal 2013, primarily due to higher sales volumes for cabling and busbar products. The Other segment net sales decreased \$2.7 million, or 35.1%, to \$5.0 million for the first half of fiscal 2014, as compared to \$7.7 million for the first half of fiscal

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2013, primarily due to lower sales volumes for our torque-sensing products. Translation of foreign operations net sales for the six months ended October 26, 2013 increased reported net sales by \$3.0 million or 0.8% due to average currency rate fluctuations in the first half of fiscal 2014, compared to the first half of fiscal 2013, primarily due to the strengthening of the Euro compared to the U.S. dollar.

Cost of Products Sold. Consolidated cost of products sold increased \$78.1 million, or 38.2%, to \$282.8 million for the six months ended October 26, 2013, compared to \$204.7 million for the six months ended October 27, 2012.

Consolidated cost of products sold as a percentage of sales was 79.0% for the first half of fiscal 2014, compared to 82.4% for the first half of fiscal 2013. The Automotive segment experienced a decrease in cost of goods sold as a percentage of sales due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding operation into our manufacturing processes. The Interconnect segment experienced an increase in cost of products sold as a percentage of sales primarily due to manufacturing inefficiencies related to lower sales volumes for our European sensor products. The Power Products segment experienced a decrease in cost of products sold as a percentage of sales primarily due to lower development costs, favorable commodity pricing for raw materials and favorable product sales mix.

Gross Profit. Consolidated gross profit increased \$31.6 million, or 72.1%, to \$75.4 million for the six months ended October 26, 2013, as compared to \$43.8 million for the six months ended October 27, 2012. Gross margins as a percentage of net sales increased to 21.0% for the six months ended October 26, 2013, compared to 17.6% for the six months ended October 27, 2012. The increase is primarily due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding facility in our manufacturing process in the Automotive segment. The Interconnect segment experienced an decrease in gross margins as a percentage of sales primarily due to manufacturing inefficiencies related to lower sales volumes for our European sensor products. The Power Products segment experienced an increase in gross margins as a percentage of sales primarily due to favorable commodity pricing for raw materials and favorable product sales mix.

Selling and Administrative Expenses. Selling and administrative expenses increased by \$6.1 million, or 18.8%, to \$38.6 million for the six months ended October 26, 2013, compared to \$32.5 million for the six months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales decreased to 10.8% for the six months ended October 26, 2013 from 13.1% for the six months ended October 27, 2012. The decrease is primarily due to higher sales volumes. The selling and administrative expenses in the first half of fiscal 2013 benefitted from a \$1.1 million reversal of various accruals related to a customer bankruptcy. In the first half of fiscal 2014, performance-based compensation expense increased \$4.4 million, primarily related to increased sales and net income levels. In addition, other general expenses for marketing, travel, stock award and intangible asset amortization increased \$1.4 million, partially offset by lower legal expenses of \$0.8 million.

Income From Settlement. In September 2012, the Company and various Delphi parties settled all Delphi related litigation matters. In addition to resolving all claims between the parties, the Company assigned certain patents to Delphi and entered into a non-compete agreement with respect to the related technology. In exchange, the Company received a payment of \$20.0 million, half of which was paid in October 2012 and the other half was paid in January 2013. The Company recorded the entire gain in the second quarter of fiscal 2013, in the income from settlement section of our consolidated statement of operations.

Interest Expense, Net. Interest expense, net increased to \$0.2 million for the six months ended October 26, 2013, compared to break-even for the six months ended October 27, 2012.

Other Expense, Net. Other expense, net was constant at \$0.5 million for both the six months ended October 26, 2013 and October 27, 2012. All amounts for both the six months ended October 26, 2013 and October 27, 2012 relate to currency rate fluctuations. The functional currencies of these operations are the British pound, Chinese yuan, Euro,

Indian Rupee, Mexican peso, Singapore dollar and Swiss Franc. Some foreign operations have transactions denominated in currencies other than their functional currencies, primarily sales in U.S. dollars and Euros, creating exchange rate sensitivities.

Income Tax Expense. Income tax expense decreased \$1.0 million, or 27.0%, to \$2.7 million for the six months ended October 26, 2013, compared to \$3.7 million for the six months ended October 27, 2012. The income tax expense for both the first half of fiscal 2014 and the first half of fiscal 2013 relates to income taxes on foreign profits.

Net Income Attributable to Methode Electronics, Inc. Net income attributable to Methode Electronics, Inc. increased \$6.2 million, or 22.8%, to \$33.4 million for the six months ended October 26, 2013, compared to \$27.2 million for the six months ended October 27, 2012. The six months ended October 27, 2013 benefitted from the GM Center Console Program launch, higher sales volumes, realized manufacturing efficiencies related to the increased sales volumes and the vertical

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integration of our paint and decorative molding facility in our manufacturing process. The six months ended October 27, 2012 benefitted from the \$20.0 million settlement and the \$1.1 million reversal of various accruals related to a customer bankruptcy.

Operating Segments

Automotive Segment Results

Below is a table summarizing results for the six months ended:
(\$ in millions)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$229.6	\$151.2	\$78.4	51.9	%
Cost of products sold	186.2	129.9	56.3	43.3	%
Gross profit	43.4	21.3	22.1	103.8	%
Selling and administrative expenses	13.0	12.2	0.8	6.6	%
Income from settlement	—	(20.0)	20.0	N/M	
Income from operations	\$30.4	\$29.1	\$1.3	4.5	%
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	81.1	% 85.9	%		
Gross margins	18.9	% 14.1	%		
Selling and administrative expenses	5.7	% 8.1	%		
Income from settlement	—	% (13.2)	%		
Income from operations	13.2	% 19.2	%		

Net Sales. Automotive segment net sales increased \$78.4 million, or 51.9%, to \$229.6 million for the six months ended October 26, 2013, from \$151.2 million for the six months ended October 27, 2012. Net sales increased in North America by \$59.4 million, or 117.4%, to \$110.0 million in the first half of fiscal 2014, compared to \$50.6 million in the first half of fiscal 2013 related to the GM Center Console Program, which launched during the first quarter of fiscal 2014 and increased sales volumes for our transmission lead-frame assembly. Net sales increased in Europe by \$14.0 million, or 21.4%, to \$79.4 million in the first half of fiscal 2014, compared to \$65.4 million in the first half of fiscal 2013, primarily due to hidden and visible switch products as well as currency rate fluctuations. Net sales in Asia increased \$5.0 million, or 14.2%, to \$40.2 million in the first half of fiscal 2014, compared to \$35.2 million in the first half of fiscal 2013, primarily due to increased sales volumes for our steering-angle sensor and transmission lead-frame assembly products. Translation of foreign operations net sales for the six months ended October 26, 2013 increased reported net sales by \$2.9 million, or 1.3%, due to average currency rates in the first half of fiscal 2014, compared to the average currency rates in the first half of fiscal 2013, primarily due to the strengthening of the Euro as compared to the U.S. dollar.

Cost of Products Sold. Automotive segment cost of products sold increased \$56.3 million, or 43.3%, to \$186.2 million for the six months ended October 26, 2013, from \$129.9 million for the six months ended October 27, 2012. The Automotive segment cost of products sold as a percentage of sales decreased to 81.1% in the first half of fiscal

2014, compared to 85.9% in the first half of fiscal 2013. The decrease is primarily due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding operation into our manufacturing processes.

Gross Profit. Automotive segment gross profit increased \$22.1 million, or 103.8%, to \$43.4 million for the six months ended October 26, 2013, as compared to \$21.3 million for the six months ended October 27, 2012. The Automotive segment gross margins as a percentage of net sales were 18.9% for the six months ended October 26, 2013, as compared to 14.1% for the six months ended October 27, 2012. The increase is primarily due to increased manufacturing efficiencies related to the increased sales volumes and the vertical integration of our paint and decorative molding facility in our manufacturing process.

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Selling and Administrative Expenses. Selling and administrative expenses increased \$0.8 million, or 6.6%, to \$13.0 million for the six months ended October 26, 2013, compared to \$12.2 million for the six months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales were 5.7% for the six months ended October 26, 2013 and 8.1% for the six months ended October 27, 2012. The selling and administrative expenses in the first half of fiscal 2013 benefitted from a \$1.1 million reversal of various accruals related to a customer bankruptcy. Legal expenses decreased \$1.0 million due to the settlement of the Delphi litigation in the second quarter of fiscal 2013, partially offset with higher selling and administrative expenses at our China and European operation of \$0.2 million and \$0.3 million, respectively and \$0.2 million of severance costs at our North American automotive operation.

Income From Settlement. In September 2012, the Company and various Delphi parties settled all Delphi related litigation matters. In addition to resolving all claims between the parties, the Company assigned certain patents to Delphi and entered into a non-compete agreement with respect to the related technology. In exchange, the Company received a payment of \$20.0 million, half of which was paid in October 2012 and the other half was paid in January 2013. The Company recorded the entire gain in the second quarter of fiscal 2013, in the income from settlement section of our consolidated statement of operations.

Income from Operations. Automotive segment income from operations increased \$1.3 million, or 4.5%, to \$30.4 million for the six months ended October 26, 2013, compared to \$29.1 million for the six months ended October 27, 2012. The six months ended October 26, 2013 benefitted from the GM Center Console Program, higher sales volumes and manufacturing efficiencies. The six months ended October 27, 2012 benefitted from the \$20.0 million settlement and the \$1.1 million reversal of various accruals related to a customer bankruptcy.

Interconnect Segment Results

Below is a table summarizing results for the six months ended:
(\$ in millions)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$87.3	\$65.0	\$22.3	34.3	%
Cost of products sold	64.4	47.1	17.3	36.7	%
Gross profit	22.9	17.9	5.0	27.9	%
Selling and administrative expenses	8.6	8.8	(0.2)	(2.3))%
Income from operations	\$14.3	\$9.1	\$5.2	57.1	%
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	73.8	% 72.5	%		
Gross margins	26.2	% 27.5	%		
Selling and administrative expenses	9.9	% 13.5	%		
Income from operations	16.4	% 14.0	%		

Net Sales. Interconnect segment net sales increased \$22.3 million, or 34.3%, to \$87.3 million for the six months ended October 26, 2013, from \$65.0 million for the six months ended October 27, 2012. Net sales increased in North America by \$23.1 million, or 50.1%, to \$69.2 million in the first half of fiscal 2014, compared to \$46.1 million in the first half of fiscal 2013, primarily due to stronger sales volumes for our appliance, data solutions and radio remote control products. Net sales in Europe decreased \$0.2 million, or 1.7%, to \$11.5 million in the first half of fiscal 2014, compared to \$11.7 million in the first half of fiscal 2013, primarily due to lower sensor sales volumes. Net sales in Asia decreased \$0.6 million, or 8.3%, to \$6.6 million in the first half of fiscal 2014, compared to \$7.2 million in the first half of fiscal 2013, primarily due to lower sales from certain legacy products resulting from the planned exit of a product line.

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Cost of Products Sold. Interconnect segment cost of products sold increased 17.3 million, or 36.7%, to \$64.4 million for the six months ended October 26, 2013, compared to \$47.1 million for the six months ended October 27, 2012. Interconnect segment cost of products sold as a percentage of net sales increased to 73.8% for the six months ended October 26, 2013, compared to 72.5% for the six months ended October 27, 2012. The increase in cost of products sold as a percentage of sales is primarily due to lower sales volumes for our European sensor products.

Gross Profit. Interconnect segment gross profit increased \$5.0 million, or 27.9%, to \$22.9 million for the six months ended October 26, 2013, compared to \$17.9 million for the six months ended October 27, 2012. Gross margins as a percentage of net sales decreased to 26.2% for the six months ended October 26, 2013, from 27.5% for the six months ended October 27, 2012. The decrease in gross margins is primarily due to lower sales volumes for our European sensor products.

Selling and Administrative Expenses. Selling and administrative expenses decreased \$0.2 million, or 2.3%, to \$8.6 million for the six months ended October 26, 2013, compared to \$8.8 million for the six months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales decreased to 9.9% for the six months ended October 26, 2013, from 13.5% for the six months ended October 27, 2012. The decrease is primarily due to lower commission expense.

Income from Operations. Interconnect segment income from operations increased \$5.2 million, or 57.1%, to \$14.3 million for the six months ended October 26, 2013, compared to \$9.1 million for the six months ended October 27, 2012, primarily due to higher sales volumes and slightly lower selling and administrative expenses.

Power Products Segment Results

Below is a table summarizing results for the six months ended:
(\$ in millions)

	October 26, 2013	October 27, 2012	Net Change	Net Change	
Net sales	\$36.1	\$24.6	\$11.5	46.7	%
Cost of products sold	27.4	21.1	6.3	29.9	%
Gross profit	8.7	3.5	5.2	148.6	%
Selling and administrative expenses	2.7	3.5	(0.8) (22.9)%
Income from operations	\$6.0	\$—	\$6.0	N/M	
Percent of sales:	October 26, 2013	October 27, 2012			
Net sales	100.0	% 100.0	%		
Cost of products sold	75.9	% 85.8	%		
Gross margins	24.1	% 14.2	%		
Selling and administrative expenses	7.5	% 14.2	%		
Income from operations	16.6	% —	%		

Net Sales. Power Products segment net sales increased \$11.5 million, or 46.7%, to \$36.1 million for the six months ended October 26, 2013, compared to \$24.6 million for the six months ended October 27, 2012. Net sales increased in North America by \$4.0 million, or 24.5%, to \$20.3 million in the first half of fiscal 2014, compared to \$16.3 million in the first half of fiscal 2013, primarily due to higher sales volumes for our cabling and busbar products, partially offset by lower sales volumes for our heat sink products. Net sales in Europe increased \$5.3 million, or 588.9%, to \$6.2 million in the first half of fiscal 2014, compared to \$0.9 million in the first half of fiscal 2012, due to launches of a by-pass switch for a substation and busbars for electric vehicles, both of which launched in the second half of fiscal 2013. Net sales in Asia increased \$2.2 million, or 29.7%, to \$9.6 million in the first half of fiscal 2014, compared to \$7.4 million in the first half of fiscal 2013, primarily due to increased sales volumes of busbar and cabling assemblies.

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Cost of Products Sold. Power Products segment cost of products sold increased \$6.3 million, or 29.9%, to \$27.4 million for the six months ended October 26, 2013, compared to \$21.1 million for the six months ended October 27, 2012. The Power Products segment cost of products sold as a percentage of sales decreased to 75.9% for the six months ended October 26, 2013, from 85.8% for the six months ended October 27, 2012. The decrease in cost of products sold as a percentage of sales is primarily due to higher sales volumes, favorable commodity pricing for raw materials and favorable product sales mix.

Gross Profit. Power Products segment gross profit increased \$5.2 million, or 148.6%, to \$8.7 million in the first half of fiscal 2014, compared to \$3.5 million in the first half of fiscal 2013. Gross margins as a percentage of net sales increased to 24.1% for the six months ended October 26, 2013 from 14.2% for the six months ended October 27, 2012. The increase in gross margins is primarily due to favorable commodity pricing for raw materials and favorable product sales mix.

Selling and Administrative Expenses. Selling and administrative expenses decreased \$0.8 million, or 22.9%, to \$2.7 million for the six months ended October 26, 2013, compared to \$3.5 million for the six months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales decreased to 7.5% for the six months ended October 26, 2013 from 14.2% for the six months ended October 27, 2012. Selling and administrative expenses decreased due to lower commission and bonus expense in North America.

Income From Operations. Power Products segment income from operations increased \$6.0 million, to \$6.0 million for the six months ended October 26, 2013, compared to break-even for the six months ended October 27, 2012, due to higher sales, favorable commodity pricing for raw materials, favorable product sales mix and lower selling and administrative expenses.

Other Segment Results

Below is a table summarizing results for the six months ended:

(\$ in millions)

	October 26, 2013	October 27, 2012	Net Change	Net Change
Net sales	\$5.0	\$7.7	\$(2.7)	(35.1)%
Cost of products sold	3.9	5.0	(1.1)	(22.0)%
Gross profit	1.1	2.7	(1.6)	(59.3)%
Selling and administrative expenses	1.2	1.2	—	— %
Income/(loss) from operations	\$(0.1)	\$1.5	\$(1.6)	(106.7)%
Percent of sales:	October 26, 2013	October 27, 2012		
Net sales	100.0	% 100.0	%	
Cost of products sold	78.0	% 64.9	%	
Gross margins	22.0	% 35.1	%	
Selling and administrative expenses	24.0	% 15.6	%	
Income/(loss) from operations	(2.0)	% 19.5	%	

Net Sales. The Other segment net sales decreased \$2.7 million, or 35.1%, to \$5.0 million for the six months ended October 26, 2013, compared to \$7.7 million for the six months ended October 27, 2012. Net sales from our torque-sensing business decreased 62.6% in the first half of fiscal 2014, compared to the first half of fiscal 2013, primarily due to the planned exit of certain product lines and lower demand in the e-bike and motorcycle markets. Net sales from our testing facilities increased 3.1% in the first half of fiscal 2014, compared to the first half of fiscal 2013.

Cost of Products Sold. Other segment cost of products sold decreased \$1.1 million, or 22.0%, to \$3.9 million for the six months ended October 26, 2013, compared to \$5.0 million for the six months ended October 27, 2012. Cost of products sold as a percentage of sales increased to 78.0% in the first half of fiscal 2014, compared to 64.9% in the first half of fiscal

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2013. The increase in cost of products sold as a percentage of sales is primarily due to manufacturing inefficiencies as a result of lower sales volumes in our torque-sensing business. In addition, our torque sensing business experienced additional manufacturing inefficiencies due to a planned move of production from our North American facility to our Malta facility.

Gross Profit. The Other segment gross profit decreased \$1.6 million, or 59.3%, to \$1.1 million for the six months ended October 26, 2013, compared to \$2.7 million for the six months ended October 27, 2012. The decrease in gross margins as a percentage of sales is primarily due to efficiencies caused by significantly lower sales volumes and the planned move of production.

Selling and Administrative Expenses. Selling and administrative expenses were flat at \$1.2 million for both the six months ended October 26, 2013 and the six months ended October 27, 2012. Selling and administrative expenses as a percentage of net sales increased to 24.0% for the six months ended October 26, 2013, from 15.6% for the six months ended October 27, 2012.

Income/(Loss) From Operations The Other segment income/(loss) from operations decreased \$1.6 million, or 106.7%, to a loss of \$0.1 million for the six months ended October 26, 2013, compared to income of \$1.5 million for the six months ended October 27, 2012. The decrease was primarily due to lower sales volumes and production inefficiencies.

Liquidity and Capital Resources

We believe our current world-wide cash balances together with expected future cash flows to be generated from operations and our committed credit facility will be sufficient to support current operations. Due to the shifting of operations from the U.S. to foreign locations, a significant amount of cash and expected future cash flows are located outside of the U.S. Of the \$87.8 million of cash and cash equivalents, as of October 26, 2013, \$81.2 million was held in subsidiaries outside the U.S. and all of this amount is deemed to be permanently reinvested and therefore not available to fund our domestic operations. We currently have \$28.1 million of net operating loss carry-forwards in the U.S. which would reduce the cash tax obligation (if the carry-forward has not otherwise been used) upon any future repatriation of funds.

We are party to an Amended and Restated Credit Agreement with Bank of America, N.A., as administrative agent, and certain other financial institutions, which has a maturity of September 21, 2017. The credit facility is in the aggregate principal amount of \$100.0 million, with an option to increase the principal amount by an additional \$50.0 million, subject to customary conditions and approval of the lender(s) providing new commitment(s). The credit facility provides for variable rates of interest based on the type of borrowing and the Company's debt to EBITDA financial ratio. The Amended and Restated Credit Agreement is guaranteed by certain of our U.S. subsidiaries. At October 26, 2013, the interest rate on the credit facility was 1.5% plus LIBOR. At October 26, 2013, we were in compliance with the covenants of the agreement. During the first half of fiscal 2014, we had borrowings of \$21.5 million and payments of \$14.0 million, which includes interest of \$0.5 million under this credit facility. As of October 26, 2013, there were outstanding balances against the credit facility of \$51.5 million. There was \$48.5 million available to borrow under the credit facility as of October 26, 2013, which does not include the option to increase the principal amount.

Cash Flow Operating Activities

Net cash provided by operating activities increased \$8.1 million to \$30.8 million for the first half of fiscal 2014, compared to \$22.7 million for the first half of fiscal 2013, primarily due by the increase of \$6.2 million in net income, to \$33.4 million in the first half of fiscal 2014, compared to \$27.1 million in first half of fiscal 2013. The first half of

fiscal 2013 includes the first cash payment of \$10.0 million received in October 2012 related to the legal settlement. The net changes in assets and liabilities resulted in a cash use of \$16.2 million in first half of fiscal 2014, compared to cash use of \$14.9 million in the first half of fiscal 2013. The increased cash use in the first half of fiscal 2014 compared to the first half of fiscal 2013 is primarily driven by increased sales and overall business levels in the first half of fiscal 2014, as compared to the first half of fiscal 2013. The cash use of \$14.9 million in the first half of fiscal 2013 is primarily due to the receivable recorded for the second \$10.0 million payment related to the income from settlement.

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Cash Flow Investing Activities

Net cash used in investing activities decreased by \$8.5 million due to purchases of property, plant and equipment of \$16.5 million for the six months ended October 26, 2013, compared to \$23.6 million for the six months ended October 27, 2012. Purchases for both periods primarily relate to plant expansion and equipment purchases in Europe and North America for products which launched in fiscal 2013 and the first quarter of fiscal 2014. In the first six months of fiscal 2013, we acquired the Hetronic Italy business for \$1.4 million.

Cash Flow Financing Activities

Net cash provided by financing activities increased \$12.3 million to cash provided of \$5.1 million in the first six months of fiscal 2014, compared to cash used of \$7.2 million for the first six months of fiscal 2013. During the first six months of fiscal 2014, the Company had net borrowings against the credit facility of \$8.0 million, compared to net repayments of \$2.0 million in the first six months of fiscal 2013. We paid dividends of \$5.2 million for both the first six months of fiscal 2014 and 2013. The first six months of fiscal 2014 includes \$2.4 million of proceeds for the exercise of stock options.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, other than operating leases and purchase obligations entered into in the normal course of business.

Item 3. Quantitative And Qualitative Disclosures About Market Risk

Certain of our foreign operations enter into transactions in currencies other than their functional currency, primarily the U.S. dollar and the Euro. A 10% change in foreign currency exchange rates from balance sheet date levels could impact our income before income taxes by \$2.7 million as of October 26, 2013 and \$2.5 million as of April 27, 2013. We also have foreign currency exposure arising from the translation of our net equity investment in our foreign operations to U.S. dollars. We generally view our investments in foreign operations with functional currencies other than the U.S. dollar as long-term. The currencies to which we are exposed are the British pound, Chinese yuan, Euro, Indian Rupee, Mexican peso, Singapore dollar and Swiss franc. A 10% change in foreign currency exchange rates from balance sheet date levels could impact our net foreign investments by \$22.6 million at October 26, 2013 and \$19.5 million at April 27, 2013.

We are exposed to market risk from changes in interest rates. The interest rate risk for our credit agreement, under which we had \$51.5 million of net borrowings at October 26, 2013, is variable and is determined based on LIBOR. We estimate that a one percentage point change in interest rates would not have a material impact on our results of operations for fiscal 2014 based upon our current and expected levels of our debt.

Item 4. Controls And Procedures

As of the end of the period covered by this quarterly report on Form 10-Q, we performed an evaluation under the supervision and with the participation of the Company's management, including our Chief Executive Officer and our Chief Financial Officer, of our "disclosure controls and procedures" (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). The Company's disclosure controls and procedures are designed to ensure that the information required to be disclosed by the Company in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's applicable rules and forms. As a result of this evaluation, our Chief Executive

Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

There have been no changes in our internal control over financial reporting during the quarter ended October 26, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 6. Exhibits

Exhibit Number	Description
31.1	Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer
31.2	Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer
32	Certification of Periodic Financial Report Pursuant to 18 U.S.C. Section 1350
101	Interactive Data File *

* As provided in Rule 406 of Regulation S-T, this information is deemed not filed as part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, and is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, and is otherwise not subject to liability under those sections.

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SIGNATURES

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

METHODE ELECTRONICS, INC.

By: /s/ Douglas A. Koman
Douglas A. Koman
Chief Financial Officer
(principal financial officer)

Dated: December 5, 2013

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INDEX TO EXHIBITS

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