ACCELERON PHARMA INC
Form 10-Q
October 30, 2018
Table of Contents

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

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2018
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number: 001-36065

ACCELERON PHARMA INC.
(Exact name of registrant as specified in its charter)

Delaware	2836	27-0072226
(State or other jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

128 Sidney Street
Cambridge, MA 02139
(617) 649-9200
(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes x No o

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

Non-accelerated filer o Smaller reporting company o

Emerging growth company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

As of October 23, 2018, there were 46,190,344 shares of the registrant's Common Stock, par value $0.001 per share, outstanding.

Table of Contents

TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Acceleron Pharma Inc.
Condensed Consolidated Balance Sheets
(amounts in thousands except share and per share data)
(unaudited)

	September 30, 2018	December 31, 2017
Assets		
Current assets:		
Cash and cash equivalents	$ 112,427	$ 100,150
Collaboration receivables (all amounts are with related party)	3,258	3,570
Prepaid expenses and other current assets	7,093	4,446
Short-term investments	195,545	177,077
Total current assets	318,323	285,243
Property and equipment, net	6,270	6,966
Restricted cash	1,597	1,132
Other assets	92	113
Long-term investments	11,835	95,723
Total assets	$ 338,117	$ 389,177
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$ 1,289	$ 1,086
Accrued expenses	13,144	14,936
Deferred revenue	—	541
Deferred rent	248	182
Total current liabilities	14,681	16,745
Deferred revenue, net of current portion	—	3,161
Deferred rent, net of current portion	2,293	1,818
Warrants to purchase common stock	2,031	2,236
Total liabilities	19,005	23,960
Commitments and contingencies (Note 14)		
Stockholders' equity:		
Undesignated preferred stock, $0.001 par value: 25,000,000 shares authorized and no shares issued or outstanding	—	—
Common stock, $0.001 par value: 175,000,000 shares authorized; 46,185,529 and 45,261,175 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively	47	46
Additional paid-in capital	871,643	839,090
Accumulated deficit	(551,815)	(473,024)
Accumulated other comprehensive loss	(763)	(895)
Total stockholders' equity	319,112	365,217
Total liabilities and stockholders' equity	$ 338,117	$ 389,177

See accompanying notes to these condensed consolidated financial statements.

Table of Contents

Acceleron Pharma Inc.
Condensed Consolidated Statements of Operations and Comprehensive Loss
(amounts in thousands except per share data)
(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Revenue:				
Collaboration revenue:				
License and milestone	$—	$135	$—	$406
Cost-sharing, net	3,258	2,879	10,175	9,370
Total revenue (all amounts are with related party)	3,258	3,014	10,175	9,776
Costs and expenses:				
Research and development	24,667	21,059	74,027	64,387
General and administrative	8,653	7,533	23,756	26,735
Total costs and expenses	33,320	28,592	97,783	91,122
Loss from operations	(30,062)	(25,578)	(87,608)	(81,346)
Other expense, net	(342)	(410)	(592)	(683)
Interest income	1,413	496	4,073	1,474
Total other income, net	1,071	86	3,481	791
Loss before income taxes	(28,991)	(25,492)	(84,127)	(80,555)
Income tax benefit (provision)	12	41	(9)	29
Net loss	$(28,979)	$(25,451)	$(84,136)	$(80,526)
Net loss per share- basic and diluted	$(0.63)	$(0.65)	$(1.84)	$(2.08)
Weighted-average number of common shares used in computing net loss per share- basic and diluted	46,051	39,361	45,787	38,804
Other comprehensive loss:				
Net loss	$(28,979)	$(25,451)	$(84,136)	$(80,526)
Net unrealized holding gains on short-term and long-term investments during the period, net of tax of $37 thousand for the three and nine months ended September 30, 2018, and $59 thousand for the three and nine months ended September 30, 2017	317	100	170	170
Comprehensive loss	$(28,662)	$(25,351)	$(83,966)	$(80,356)

See accompanying notes to these condensed consolidated financial statements.

Table of Contents

Acceleron Pharma Inc.
Condensed Consolidated Statements of Cash Flows
(amounts in thousands)
(unaudited)

	Nine Months Ended September 30,	
	2018	2017
Operating Activities		
Net loss	$(84,136)	$(80,526)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,868	2,023
Stock-based compensation	18,062	21,877
Change in fair value of warrants	592	683
Other non-cash items	492	211
Changes in assets and liabilities:		
Prepaid expenses and other assets	(2,626)	426
Collaboration receivables (all amounts are with a related party)	312	355
Accounts payable	80	(566)
Accrued expenses	(1,863)	160
Deferred revenue	—	(407)
Deferred rent	541	22
Net cash used in operating activities	(65,678)	(55,742)
Investing Activities		
Purchases of investments	(73,570)	(245)
Proceeds from sales and maturities of investments	138,631	86,001
Purchases of property and equipment	(1,901)	(3,639)
Net cash provided by investing activities	63,160	82,117
Financing Activities		
Proceeds from issuance of common stock from public offering, net of issuance costs	—	187,986
Payments for withholding taxes on restricted stock units	(729)	(226)
Payments for capital lease expenditures	(78)	—
Proceeds from exercise of stock options and warrants to purchase common stock	14,982	3,233
Proceeds from issuances of common stock related to employee stock purchase plan	1,085	827
Net cash provided by financing activities	15,260	191,820
Net increase in cash, cash equivalents and restricted cash	12,742	218,195
Cash, cash equivalents and restricted cash at beginning of period	101,282	21,896
Cash, cash equivalents and restricted cash at end of period	$114,024	$240,091
Supplemental Disclosure of Non-Cash Investing and Financing Activities:		
Purchase of property and equipment included in accounts payable and accrued expenses	$133	$395
Capitalized follow-on public offering costs included in accrued expenses	$—	$337
Reclassification of warrant liability to additional paid-in capital	$797	$—
Acquisition of capital lease	$139	$—

See accompanying notes to these condensed consolidated financial statements.

Table of Contents

Acceleron Pharma Inc.
Notes to Condensed Consolidated Financial Statements
(unaudited)

1. Nature of Business

Acceleron Pharma Inc. (Acceleron or the Company) is a Cambridge, Massachusetts-based clinical stage biopharmaceutical company dedicated to the discovery, development, and commercialization of therapeutics to treat serious and rare diseases. The Company's leadership in the understanding of TGF-beta biology and protein engineering generates innovative compounds that engage the body's ability to regulate cellular growth and repair.

The Company is subject to risks common to companies in the biotechnology industry, including, but not limited to, the risk that the Company never achieves profitability, the need for substantial additional financing, risk of relying on third parties, risks of clinical trial failures, dependence on key personnel, protection of proprietary technology and compliance with government regulations.

2. Basis of Presentation

The accompanying interim condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP). Any reference in these notes to applicable guidance is meant to refer to the authoritative United States generally accepted accounting principles as found in the Accounting Standards Codification (ASC) and Accounting Standards Update (ASU) of the Financial Accounting Standards Board (FASB).

The accompanying interim condensed consolidated financial statements are unaudited and reflect the application of certain significant accounting policies as described below and elsewhere in these notes to the financial statements. As of September 30, 2018, the Company's significant accounting policies and estimates, which are detailed in the Company's Annual Report on Form 10-K for the year ended December 31, 2017, have not changed, and the unaudited interim financial statements have been prepared on the same basis as the audited annual financial statements as of and for the year ended December 31, 2017, except for the adoption of Accounting Standards Updates (ASU) No. 2016-18, Restricted Cash, which did not have a material impact, ASU No. 2018-07, Compensation - Stock Compensation: Improvements to Nonemployee Share-Based Payment Accounting, which is discussed further in Note 16, and Topic No. 606, Revenue from Contracts with Customers, as discussed below. In the opinion of management, the accompanying interim condensed consolidated financial statements reflect all adjustments, consisting of normal recurring adjustments, necessary for the fair presentation of the Company's financial position as of September 30, 2018, the results of its operations for the three and nine months ended September 30, 2018 and 2017, and its cash flows for the nine months ended September 30, 2018 and 2017.

The results for the three and nine months ended September 30, 2018 are not necessarily indicative of the results to be expected for the year ending December 31, 2018, any other interim periods, or any future year or period. These interim financial statements should be read in conjunction with the audited financial statements as of and for the year ended December 31, 2017, and the notes thereto, together with Management's Discussion and Analysis of Financial Condition and Results of Operations, contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Revenue Recognition

Effective January 1, 2018, the Company adopted Accounting Standards Codification Topic 606, Revenue from Contracts with Customers, (ASC 606), using the modified retrospective transition method. Under this method, results for reporting periods beginning January 1, 2018 are presented under ASC 606, while prior period amounts are not adjusted and continue to be reported in accordance with ASC 605.

The Company has primarily generated revenue through collaboration, license and research arrangements, which are within the scope of ASC 606, with collaboration partners for the development and commercialization of therapeutic candidates. The arrangements generally contain performance obligations, which may include (1) licenses, or options to obtain licenses, to the Company's technology, (2) research and development activities performed for the collaboration partners (3) participation on joint development committees (JDCs), and (4) the manufacturing of clinical or preclinical material. Payments pursuant to these arrangements typically include non-refundable, upfront payments,

milestone payments upon achieving significant development events, research and development reimbursements, sales milestones, exercises of options, and royalties on future product sales.

Amounts received prior to satisfying the revenue recognition criteria are recorded as deferred revenue in the Company's consolidated balance sheets. Amounts expected to be recognized as revenue within the 12 months following the balance sheet date are classified as deferred revenue, current portion. Amounts not expected to be recognized as revenue within the 12

Table of Contents

months following the balance sheet date are classified as deferred revenue, net of current portion. Amounts recognized as revenue, but not yet received or invoiced are generally recognized as contract assets, including collaboration receivables.

To determine revenue recognition for arrangements within the scope of ASC 606, the Company performs the following five steps: (i) identify the contract(s) with the customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction price to the performance obligations in the contract; and (v) recognize revenue when (or as) the entity satisfies a performance obligation. The Company only applies the five-step model to contracts when it is probable that the entity will collect the consideration it is entitled to in exchange for the goods or services it transfers to the customer. At contract inception, once the contract is determined to be within the scope of ASC 606, the Company assesses the goods or services promised within each contract, determines those that are performance obligations, and assesses whether each promised good or service is distinct. The Company then recognizes as revenue the amount of the transaction price that is allocated to the respective performance obligation when (or as) the performance obligation is satisfied. Depending on the nature of the performance obligation these assessments require management to make significant judgments and estimates.

Exclusive Licenses

If the license to the Company’s intellectual property is determined to be distinct from the other promises or performance obligations identified in the arrangement, the Company recognizes revenue from non-refundable, upfront fees allocated to the license when the license is transferred and the customer is able to use and benefit from the license. In order to assess whether the license is distinct, the Company considers the capabilities of the collaboration partner and the availability of the necessary expertise in the general marketplace to determine whether the collaboration partner can benefit from the license for its intended purpose without the receipt of the remaining elements. For licenses determined not to be distinct the Company utilizes judgment to assess the nature of the combined performance obligation to determine whether the combined performance obligation is satisfied over or at a point in time and, if over time, the appropriate method of measuring progress for purposes of recognizing revenue. The Company evaluates the measure of progress each reporting period and, if necessary, adjusts the measure of performance and related revenue recognition. The measure of progress, and thereby periods over which revenue should be recognized, are subject to estimates by management and may change over the course of the research and development and licensing agreement.

Research and Development Services

The promises under the Company’s collaboration and license agreements generally include research and development services to be performed by the Company on behalf of the collaboration partner. As the provision of research and development services is a part of the Company’s central operations, when the Company is principally responsible for the performance of these services under the agreements, the Company recognizes revenue on a gross basis for research and development services in accordance with the ASC 606 framework described above.

Customer Options

The Company's agreements may contain options which provide the collaboration partner the right to obtain additional licenses. If an arrangement is determined to contain customer options, the goods and services underlying the customer options are not considered to be performance obligations at the inception of the arrangement, and the associated option fees are not included in the transaction price. The Company evaluates the customer options to determine if they represent material rights, which may include options to acquire additional goods or services for free or at a discount. If the customer options are determined to represent a material right, the material right is recognized as a separate performance obligation at the outset of the arrangement. The Company allocates the transaction price to material rights based on the relative standalone selling price, which is determined based on the identified discount and the probability that the customer will exercise the option. Amounts allocated to a material right are not recognized as revenue until, at the earliest, the option is exercised.

Milestone Payments

At the inception of each arrangement that includes milestone payments, the Company evaluates whether the milestones are considered probable of being achieved and estimates the amount to be included in the transaction price using the most likely amount method. The Company evaluates factors such as the scientific, clinical, regulatory,

commercial, and other risks that must be overcome to achieve the respective milestone in making this assessment. If it is probable that a significant revenue reversal would not occur, the associated milestone value is included in the transaction price. Milestone payments that are not within the control of the Company or the licensee, such as regulatory approvals, are not considered probable of being achieved until those approvals are received. At the end of each subsequent reporting period, the Company reevaluates the probability of achievement of all milestones subject to constraint and, if necessary, adjusts its estimate of the overall transaction price. Any such adjustments are recorded on a cumulative catch-up basis, which would affect revenues and earnings in the period of adjustment. If a milestone or other variable consideration relates specifically to the Company's efforts to satisfy a single

Table of Contents

performance obligation or to a specific outcome from satisfying the performance obligation, the Company generally allocates the milestone amount entirely to that performance obligation.

Royalties

For arrangements that include sales-based royalties, including milestone payments based on a level of sales, and the license is deemed to be the predominant item to which the royalties relate, the Company recognizes revenue at the later of (i) when the related sales occur, or (ii) when the performance obligation to which some or all of the royalty has been allocated has been satisfied (or partially satisfied). To date, the Company has not recognized any royalty revenue resulting from any of its licensing arrangements.

For a complete discussion of accounting for collaboration revenues, see Note 15.

3. Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts expensed during the reporting period.

Management considers many factors in selecting appropriate financial accounting policies and controls, and in developing the estimates and assumptions that are used in the preparation of these consolidated financial statements. Management must apply significant judgment in this process. In addition, other factors may affect estimates, including: expected business and operational changes, sensitivity and volatility associated with the assumptions used in developing estimates, and whether historical trends are expected to be representative of future trends. The estimation process often may yield a range of potentially reasonable estimates of the ultimate future outcomes and management must select an amount that falls within that range of reasonable estimates. This process may result in actual results differing materially from those estimated amounts used in the preparation of the consolidated financial statements if these results differ from historical experience, or other assumptions do not turn out to be substantially accurate, even if such assumptions are reasonable when made. In preparing these consolidated financial statements, management used significant estimates in the following areas, among others: revenue recognition and the related evaluation of any constrained milestones, stock-based compensation expense, the determination of the fair value of stock-based awards, the fair value of liability-classified warrants, and accrued expenses.

4. Segment Information

Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision maker, or decision making group, in making decisions on how to allocate resources and assess performance. The Company’s chief operating decision maker is the chief executive officer. The Company and the chief executive officer view the Company’s operations and manage its business as one operating segment, which is the discovery, development and commercialization of highly innovative therapeutics to treat serious and rare diseases.

5. Cash Equivalents and Short-term and Long-term Investments

The Company considers all highly liquid investments purchased with original maturities of 90 days or less at acquisition to be cash equivalents. Cash and cash equivalents include cash held in banks and amounts held in interest-bearing money market accounts. Cash equivalents are carried at cost, which approximates their fair market value.

The Company determines the appropriate classification of marketable securities at the time of purchase and reevaluates such designation at each balance sheet date. The Company has classified all of its marketable securities at September 30, 2018 as “available-for-sale” pursuant to ASC 320, Investments – Debt and Equity Securities. The Company records available-for-sale securities at fair value, with the unrealized gains and losses included in accumulated other comprehensive income (loss) in stockholders’ equity. There were no realized gains or losses on marketable securities for the three and nine months ended September 30, 2018 and 2017.

Investments not classified as cash equivalents are presented as either short-term or long-term investments based on both their maturities as well as the time period the Company intends to hold such securities.

The Company adjusts the cost of available-for-sale debt securities for amortization of premiums and accretion of discounts to maturity. The Company includes such amortization and accretion in interest income. The cost of securities sold is based on the specific identification method. The Company includes in interest income interest and

dividends on securities classified as available-for-sale.

The Company reviews marketable securities for other-than-temporary impairment whenever the fair value of a marketable security is less than the amortized cost and evidence indicates that a marketable security's carrying amount is not recoverable

Table of Contents

within a reasonable period of time. Other-than-temporary impairments of investments are recognized in the consolidated statements of operations if the Company has experienced a credit loss, has the intent to sell the marketable security, or if it is more likely than not that the Company will be required to sell the marketable security before recovery of the amortized cost basis. Evidence considered in this assessment includes reasons for the impairment, compliance with the Company's investment policy, the severity and the duration of the impairment and changes in value subsequent to the end of the period.

The aggregate fair value of securities held by the Company in an unrealized loss position for less than twelve months as of September 30, 2018 and December 31, 2017 was $155.0 million and $193.6 million, respectively. The aggregate fair value of securities held by the Company in an unrealized loss position for more than twelve months as of September 30, 2018 and December 31, 2017 was $48.5 million and $67.0 million, respectively. The aggregate unrealized loss for those securities in an unrealized loss position for more than twelve months is $0.1 million and $0.3 million, respectively. As a result, the Company determined it did not hold any investments with any other-than-temporary impairment as of September 30, 2018 and December 31, 2017.

The following is a summary of cash, cash equivalents and available-for-sale securities as of September 30, 2018 and December 31, 2017, (in thousands):

	September 30, 2018			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents due in 90 days or less	$112,442	$ —	$ (15)	$112,427
Available-for-sale securities:				
Corporate obligations due in one year or less	93,554	—	(356)	93,198
Corporate obligations due in more than one year	3,962	—	(8)	3,954
U.S. Treasury securities due in one year or less	54,301	—	(121)	54,180
U.S. Treasury securities due in more than one year	4,937	—	(22)	4,915
Certificates of deposit due in one year or less	3,861	—	—	3,861
Certificates of deposit due in more than one year	—	—	—	—
Mortgage and other asset backed securities due in one year or less	44,476	—	(170)	44,306
Mortgage and other asset backed securities due in more than one year	2,999	—	(33)	2,966
Total available-for-sale securities	$208,090	$ —	$ (710)	$207,380
Total cash, cash equivalents and available-for-sale securities	$320,532	$ —	$ (725)	$319,807

	December 31, 2017			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Cash and cash equivalents due in 90 days or less	$100,150	$ —	$ —	$100,150
Available-for-sale securities:				
Corporate obligations due in one year or less	99,792	—	(219)	99,573
Corporate obligations due in more than one year	57,537	—	(261)	57,276
U.S. Treasury securities due in one year or less	27,987	—	(93)	27,894
U.S. Treasury securities due in more than one year	9,968	—	(48)	9,920
Certificates of deposit due in one year or less	10,529	—	—	10,529
Certificates of deposit due in more than one year	1,715	—	—	1,715
Mortgage and other asset backed securities due in one year or less	39,236	—	(155)	39,081
Mortgage and other asset backed securities due in more than one year	26,931	—	(119)	26,812
Total available-for-sale securities	$273,695	$ —	$ (895)	$272,800
Total cash, cash equivalents and available-for-sale securities	$373,845	$ —	$ (895)	$372,950

6. Restricted Cash

9

Table of Contents

On January 1, 2018, the Company adopted ASU 2016-18, Statement of Cash Flows - Restricted Cash (Topic 230). This new standard requires companies to include amounts generally described as restricted cash and restricted cash equivalents in cash and cash equivalents when reconciling beginning-of-period and end-of-period total amounts shown on the statement of cash flows. As a result of the adoption, there was no impact to cash flows from investing or financing activities for the nine months ended September 30, 2018 and September 30, 2017. The $1.1 million of restricted cash related to collateral for the Company's facility lease obligation and its credit cards, which was previously reported as an adjustment to net loss in cash flows used in operating activities for the nine months ended September 30, 2017, is no longer presented within the net change in cash, cash equivalents, and restricted cash, as it is considered part of cash, cash equivalents, and restricted cash.

The following table provides a reconciliation of cash, cash equivalents, and restricted cash reported within the condensed consolidated balance sheet that sum to the total of the same such amounts shown in the statement of cash flows (in thousands):

	September 30,	
	2018	2017
Cash and cash equivalents	$112,427	$238,959
Restricted cash	1,597	1,132
Total cash, cash equivalents and restricted cash shown in the statement of cash flows	$114,024	$240,091

As of September 30, 2018 and December 31, 2017, the Company maintained letters of credit totaling $1.6 million and $1.1 million, respectively, held in the form of certificates of deposit and money market funds as collateral for the Company's facility lease obligation and its credit cards.

7. Concentrations of Credit Risk and Off-Balance Sheet Risk

The Company has no off-balance sheet risk, such as foreign exchange contracts, option contracts, or other foreign hedging arrangements. Financial instruments that potentially subject the Company to concentrations of credit risk are primarily cash, cash equivalents, restricted cash, short-term and long-term investments and collaboration receivables. The Company maintains its cash and cash equivalent balances and short-term and long-term investments with financial institutions that management believes are creditworthy. Short-term and long-term investments consist of investment grade corporate obligations, treasury notes, asset backed securities, and certificates of deposit. The Company’s investment policy includes guidelines on the quality of the institutions and financial instruments and defines allowable investments that the Company believes minimizes the exposure to concentrations of credit risk. The Company routinely assesses the creditworthiness of its customers and collaboration partners. The Company has not experienced any material losses related to receivables from individual customers and collaboration partners, or groups of customers. The Company does not require collateral. Due to these factors, no additional credit risk beyond amounts provided for collection losses is believed by management to be probable in the Company’s collaboration receivables.

Table of Contents

8. Fair Value Measurements

The following tables set forth the Company's financial instruments carried at fair value using the lowest level of input applicable to each financial instrument as of September 30, 2018 and December 31, 2017 (in thousands):

	September 30, 2018			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Money market funds	$61,561	$ —	$ —	$61,561
Corporate obligations	—	137,550	—	137,550
U.S. Treasury securities	—	61,593	—	61,593
Certificates of deposit	—	3,861	—	3,861
Mortgage and other asset backed securities	—	47,272	—	47,272
Restricted cash	1,597	—	—	1,597
Total assets	$63,158	$ 250,276	$ —	$313,434
Liabilities:				
Warrants to purchase common stock	$—	$ —	$ 2,031	$2,031
Total liabilities	$—	$ —	$ 2,031	2,031

	December 31, 2017			
	Quoted Prices in Active Markets for Identical Items (Level 1)	Significant other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Money market funds	$90,702	$ —	$ —	$90,702
Corporate obligations	—	158,849	—	158,849
U.S. Treasury securities	—	37,813	—	37,813
Certificates of deposit	—	12,244	—	12,244
Mortgage and other asset backed securities	—	67,888	—	67,888
Restricted cash	1,132	—	—	1,132
Total assets	$91,834	$ 276,794	$ —	$368,628
Liabilities:				
Warrants to purchase common stock	$—	$ —	$ 2,236	$2,236
Total liabilities	$—	$ —	$ 2,236	$2,236

The money market funds noted above are included in cash and cash equivalents in the accompanying condensed consolidated balance sheets. The Company recognizes transfers between levels of the fair value hierarchy as of the end of the reporting period. There were no transfers within the hierarchy during the nine months ended September 30, 2018 or the year ended December 31, 2017.

Items measured at fair value on a recurring basis include short-term and long-term investments (Note 5), and warrants to purchase common stock (Note 13). During the periods presented, the Company has not changed the manner in which it values assets and liabilities that are measured at fair value using Level 3 inputs.

The following table sets forth a summary of changes in the fair value of the Company's common stock warrant liabilities, which represent a recurring measurement that is classified within Level 3 of the fair value hierarchy, wherein fair value is estimated using significant unobservable inputs (in thousands):

Table of Contents

	Nine Months Ended September 30,	
	2018	2017
Beginning balance	$2,236	$1,244
Change in fair value	592	683
Exercises	(797)	—
Ending balance	$2,031	$1,927

The fair value of the warrants to purchase common stock on the date of issuance and on each re-measurement date for those warrants classified as liabilities was estimated using either the Monte Carlo simulation framework, which incorporates future financing events over the remaining life of the warrants to purchase common stock, or for certain re-measurement dates, due to the warrants being deeply in the money, the Black-Scholes option pricing model. Due to the nature of these inputs, the valuation of the warrants is considered a Level 3 measurement. At each reporting period, the Company evaluates the best valuation methodology. At September 30, 2018, the Black-Scholes option pricing model was used.

The Company measures eligible assets and liabilities at fair value, with changes in value recognized in earnings. Fair value treatment may be elected either upon initial recognition of an eligible asset or liability or, for an existing asset or liability, if an event triggers a new basis of accounting. The Company did not elect to re-measure any of its existing financial assets or liabilities, and did not elect the fair value option for any financial assets and liabilities transacted in the nine months ended September 30, 2018 or the year ended December 31, 2017.

9. Net Loss Per Share

The following common stock equivalents were excluded from the calculation of diluted net loss per share for the periods indicated because their inclusion would have had an anti-dilutive effect (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Outstanding stock options	3,519	3,459	3,519	3,459
Common stock warrants	39	64	39	64
Shares issuable under employee stock purchase plan	18	19	18	19
Outstanding restricted stock units (1)	648	551	648	551
	4,224	4,093	4,224	4,093

(1) This balance is comprised of both the restricted stock units and performance-based restricted stock units described in Note 16.

10. Comprehensive Loss

Comprehensive loss is defined as the change in equity of a business enterprise during a period from transactions, other events, and circumstances from non-owner sources. Comprehensive loss consists of net loss and other comprehensive loss, which includes certain changes in equity that are excluded from net loss. Comprehensive loss has been disclosed in the accompanying consolidated statements of operations and comprehensive loss. Accumulated other comprehensive loss is presented separately on the consolidated balance sheets and consists entirely of unrealized holding gains and losses on investments as of September 30, 2018 and December 31, 2017.

11. Subsequent Events

The Company considers events or transactions that occur after the balance sheet date but prior to the issuance of the financial statements to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. The Company has evaluated all subsequent events and determined that there are no material recognized or unrecognized subsequent events requiring disclosure.

12. Recent Accounting Pronouncements

From time to time, new accounting pronouncements are issued by the Financial Accounting Standards Board (FASB) or other standard setting bodies and adopted by the Company as of the specified effective date. Unless otherwise discussed, the Company believes that the impact of recently issued standards that are not yet effective will not have a material impact on its financial position or results of operations upon adoption.

Table of Contents

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), Amendments to the FASB Accounting Standards Codification, which replaces the existing guidance for leases. ASU 2016-02 requires the identification of arrangements that should be accounted for as leases by lessees. In general, for lease arrangements exceeding a twelve month term, these arrangements must now be recognized as assets and liabilities on the balance sheet of the lessee. Under ASU 2016-02, a right-of-use asset and lease obligation will be recorded for all leases, whether operating or financing, while the income statement will reflect lease expense for operating leases and amortization/interest expense for financing leases. The balance sheet amount recorded for existing leases at the date of adoption of ASU 2016-02 must be calculated using the applicable incremental borrowing rate at the date of adoption.

ASU 2016-02 is effective for annual and interim periods beginning after December 15, 2018 and requires modified retrospective application in which the new guidance is applied on the date of initial application. In July 2018, the FASB issued ASU 2018-11, Leases - Targeted Improvements, intended to ease the implementation of the new lease standard for financial statement preparers by, among other things, allowing for an additional transition method. In lieu of presenting transition requirements to comparative periods, as previously required, an entity may now elect to show a cumulative effect adjustment on the date of adoption without the requirement to recast prior period financial statements or disclosures presented in accordance with ASU 2016-02. The Company expects to adopt the new standard and elect to use the cumulative effect adjustment transition option effective January 1, 2019, which will be the initial date of application.

The Company currently expects to elect the available package of practical expedients which allows the Company to not reassess previous accounting conclusions around whether arrangements are or contain leases, the classification of leases, and the treatment of initial direct costs. The Company also expects it will make an accounting policy election to keep leases with an initial term of 12 months or less off of the balance sheet. The Company is continuing to assess the impact that adopting the new standard and its amendments will have on its consolidated financial statements and related disclosures.

13. Warrants

Below is a summary of the number of shares issuable upon exercise of outstanding warrants and the terms and accounting treatment for the outstanding warrants (in thousands, except per share data):

	Warrants as of		Weighted-Average Exercise		Balance Sheet Classification	
	September 30, 2018	December 31, 2017	Price Per Share	Expiration	September 30, 2018	December 31, 2017
Warrants to purchase common stock	39	61	$ 5.88	June 10, 2020 - July 9, 2020	Liability (1)	Liability (1)
All warrants	39	61	$ 5.88			

(1) In January 2018, warrant holders exercised warrants to purchase 21,258 shares of Common Stock on a net basis, resulting in the issuance of 18,449 shares of Common Stock.

14. Commitments and Contingencies

Legal Proceedings

The Company, from time to time, may be party to litigation arising in the ordinary course of its business. The Company was not subject to any material legal proceedings during the three months ended September 30, 2018, and, to the best of its knowledge, no material legal proceedings are currently pending or threatened.

Other

The Company is also party to various agreements, principally relating to licensed technology, that require future payments relating to milestones not met at September 30, 2018 and December 31, 2017, or royalties on future sales of

specified products. No milestones or royalty payments under these agreements are expected to be payable in the immediate future. See Note 15 for discussion of these arrangements.

The Company enters into standard indemnification agreements in the ordinary course of business. Pursuant to the agreements, the Company indemnifies, holds harmless, and agrees to reimburse the indemnified party for losses suffered or incurred by the indemnified party, generally the Company's business partners or customers, in connection with any U.S. patent or any copyright or other intellectual property infringement claim by any third party with respect to the Company's products.

Table of Contents

The term of these indemnification agreements is generally perpetual any time after execution of the agreement. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is unlimited. The Company has never incurred costs to defend lawsuits or settle claims related to these indemnification agreements.

15. Significant Agreements

Celgene

Overview

On February 20, 2008, the Company entered into an agreement with Celgene relating to sotatercept (the Original Sotatercept Agreement), which was amended on August 2, 2011 (as amended, the Amended Sotatercept Agreement). The Company further amended and restated the Original Sotatercept Agreement in its entirety on September 18, 2017, (the Restated Sotatercept Agreement). On August 2, 2011, the Company entered into a second agreement with Celgene for luspatercept, (the Luspatercept Agreement).

Since December 31, 2017, there have been no material changes to the key terms of the above agreements. For further information on the terms of the agreements, please see the notes to the consolidated financial statements included in the Company’s Form 10-K for the year ended December 31, 2017.

Restated Sotatercept Agreement

The Restated Sotatercept Agreement provides Celgene with an exclusive license to sotatercept outside of the field of pulmonary hypertension, referred to as the PH field, and provides the Company with the worldwide rights to develop and commercialize sotatercept in the PH field.

In connection with the Restated Sotatercept Agreement, Celgene agreed not to develop or commercialize in the PH field any compound developed under the Restated Sotatercept Agreement or the Luspatercept Agreement, and the Company agreed not to develop or commercialize any compound developed under the Restated Sotatercept Agreement or the Luspatercept Agreement in any field outside the PH field. The Company has the right to license, transfer, or sell its rights to develop and commercialize sotatercept in the PH field, subject to Celgene's first right of negotiation.

Luspatercept Agreement

Under the terms of the Luspatercept Agreement, the Company and Celgene collaborate worldwide for the joint development and commercialization of luspatercept. The Company also granted Celgene an option for future products for which the Company files an Investigational New Drug application for the treatment of anemia.

The Company retained responsibility for research and development through the end of Phase 1 and the Company's initial luspatercept beta-thalassemia and luspatercept MDS Phase 2 clinical trials, as well as manufacturing the clinical supplies for these studies. Celgene will conduct subsequent Phase 2 and Phase 3 clinical studies and will be responsible for overseeing the manufacture of Phase 3 and commercial supplies by third party contract manufacturing organizations.

Beginning in November 2013, the Company agreed to conduct certain extension studies for the benefit of the luspatercept program, which included certain clinical and non-clinical services. These studies were mutually agreed to by both parties and are directed by the JDC. The Company is reimbursed for these services under the same terms and rates of the existing agreements.

Both Agreements

Under both agreements, Celgene is responsible for paying 100% of worldwide development costs and 100% of any commercialization costs worldwide for sotatercept (outside of the pulmonary hypertension field) and luspatercept. The Company has the right to co-promote sotatercept (outside of the pulmonary hypertension field), luspatercept and future products in North America. The Company will receive tiered royalties in the low-to-mid 20% range on net sales of sotatercept (outside of the pulmonary hypertension field) and luspatercept, and these royalty schedules are the same for both agreements.

Accounting Analysis

On January 1, 2018, the Company adopted ASC 606, Revenue from Contracts with Customers, using the modified retrospective transition method, and has elected to use the practical expedient related to contract modifications that is permitted under the rules of adoption. The practical expedient included in the transition guidance allows companies to

determine and allocate the transaction price of a modified contract as of the beginning of the earliest period presented instead of requiring them to separately evaluate the effects of every modification of the contract and eliminates the requirement to retrospectively

Table of Contents

restate a contract that has been modified at the date of adoption as is generally required under ASC 606. This practical expedient was applied in the assessment of the Restated Sotatercept Agreement and Luspatercept Agreement as of the date of adoption.

The Company identified the following material promises under the Restated Sotatercept Agreement and Luspatercept Agreement: (1) licenses to develop and commercialize sotatercept and luspatercept; (2) performance of research and development services; (3) participation in the JDCs; and (4) the performance of the manufacturing services. The Company determined that the licenses to sotatercept and luspatercept technology, the research and development activities, participation in the JDCs and the manufacturing services are each distinct performance obligations. The option rights to future products related to the treatment of anemia under the Luspatercept Agreement are not considered to represent a material right as this right is a protective provision akin to exclusivity and does not represent a customer option to receive the rights or services at a discount. In addition, the Company is under no obligation to discover, develop, or deliver any new compounds that modulate anemia. Therefore, the option right under the Luspatercept Agreement is not a performance obligation. Commercialization support for each of sotatercept and luspatercept is considered to be a participatory right and not a performance obligation. The Company concluded that services provided for the extension studies do not represent a contract modification or a performance obligation but rather a separate services arrangement, which is accounted for as a separate contract. Each study includes one promise, the completion of the study, which is distinct from the performance obligations in the Restated Sotatercept Agreement and Luspatercept Agreement that is satisfied over time, and the consideration for each study approximates the stand-alone selling price. Revenue is recognized as the services for each study are provided.

Future potential milestone payments were excluded from the transaction price as they are still subject to completion of on-going clinical studies or other risks that are outside of the Company's control and therefore the risk of significant reversal has not been resolved. The next likely clinical milestone payment for luspatercept would be $25.0 million and result from U.S. Food and Drug Administration (FDA) or European Medicines Agency (EMA) acceptance of a Biologics Licensing Application or equivalent for luspatercept in either myelodysplastic syndromes or beta-thalassemia. The Company and Celgene plan to submit market applications for luspatercept in the United States and Europe in the first half of 2019. Following application submission, the FDA will determine the acceptance of the application for "filing" by 60 days from the submission date. Similarly, the EMA will validate the application within 10 days of submission. In accordance with the Company's accounting policy regarding revenue recognition as described in Note 2, the revenue associated with this milestone will be recognized once it is probable that the applications are accepted for review by either the FDA or EMA. Milestone payments that are not within the control of the Company or the licensee are not considered probable of being achieved until those approvals are received. The acceptance of the application is not within the control of the Company or the licensee, and therefore, as of September 30, 2018, the Company cannot determine if it is probable that a regulatory agency will accept the application.

The transaction price includes the following payments received under the Restated Sotatercept and Luspatercept Agreement through the adoption date of December 31, 2017 for a total of $192.3 million, as follows:

- $25.0 million upfront fee in connection with the closing of the Luspatercept Agreement;
- $45.0 million of nonrefundable, upfront license and option payments in connection with the closing of the Original and Amended Sotatercept Agreements;
- $14.9 million received for sotatercept development and manufacturing activities;
- $47.9 million received for luspatercept development and manufacturing activities; and
- $59.5 million milestone payments pursuant to the agreements.

The Company allocated the total transaction price to the identified performance obligations (both satisfied and unsatisfied) using the estimated standalone selling price of each performance obligation as of the adoption date of ASC 606. The Company’s estimate of the standalone selling price requires judgment, in particular in estimating the value of the license rights for luspatercept and sotatercept, which includes assumptions over the projected revenues and expenses, probability of technical and regulatory success and appropriate discount rates.

As of the ASC 606 adoption date, the only remaining undelivered element is participation in the JDC for which there was a deferred revenue balance of $3.7 million. The transaction price allocated to participation in the JDC based on the established standalone selling price of all performance obligations was de minimis as the sotatercept and luspatercept licenses carried the most significant portion of the value included in the agreements, and the Company's remaining effort on the JDC is minimal.

Table of Contents

As a result of adopting ASC 606 on January 1, 2018, the Company has recorded a cumulative-effect reduction to opening accumulated deficit of $3.7 million as of January 1, 2018 and a corresponding decrease to deferred revenue, of which $0.5 million was recorded to current deferred revenue and $3.2 million was recorded to long-term deferred revenue. License and milestone revenue for the three and nine months ended September 30, 2018 was zero, and zero, respectively, as compared to the $0.1 million and $0.4 million, respectively, that would have been recorded under ASC 605. Deferred revenue as of September 30, 2018 was zero under ASC 606, as compared to a balance of $3.3 million, which would have resulted under ASC 605.

Through September 30, 2018, under all Celgene arrangements the Company has received net cost-share payments and milestones of $109.6 million and $44.5 million for luspatercept and sotatercept, respectively. The Company recorded net cost-sharing revenue of $3.3 million and $2.9 million during the three months ended September 30, 2018 and 2017, respectively, and $10.2 million and $9.4 million during the nine months ended September 30, 2018 and 2017, respectively.

Other Agreements

Other

In 2004, the Company entered into a license agreement with a non-profit institution for an exclusive, sublicensable, worldwide, royalty-bearing license to certain patents developed by the institution (Primary Licensed Products). In addition, the Company was granted a non-exclusive, non-sub-licensable license for Secondary Licensed Products. As compensation for the licenses, the Company issued 62,500 shares of its common stock to the institution, the fair value of which was $25,000, and was expensed during 2004, to research and development expense. The Company also agreed to pay specified development milestone payments totaling up to $2.0 million for sotatercept and $0.7 million for luspatercept. In addition, the Company is obligated to pay milestone fees based on the Company’s research and development progress, and U.S. sublicensing revenue ranging from 10%-25%, as well as royalties ranging from 1.0%-3.5% of net sales on any products under the licenses. During the three months ended September 30, 2018 and 2017, the Company expensed zero and zero, respectively, and during the nine months ended September 30, 2018 and 2017, the Company expensed $0.1 million and $0.1 million, respectively, of milestones and fees defined under the agreement.

In May 2014, the Company executed a collaboration agreement with a research technology company. The Company paid an upfront research fee of $0.3 million upon execution of the agreement. The Company also received an option to obtain a commercial license to the molecules developed during the collaboration. During the three months ended September 30, 2018 and 2017, the Company expensed $43 thousand and $0.9 million, respectively, and during the nine months ended September 30, 2018 and 2017, the Company expensed $43 thousand and $1.2 million, respectively, of milestones and fees, which is recorded as research and development expense.

16. Stock-Based Compensation

The Company recognized stock-based compensation expense related to the 2003 Stock Option and Restricted Stock Plan (the 2003 Plan), the 2013 Equity Incentive Plan (the 2013 Plan), and the 2013 Employee Stock Purchase Plan (the 2013 ESPP) in the consolidated statements of operations and comprehensive loss during the three and nine months ended September 30, 2018 and 2017, respectively, as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Research and development	$3,346	$3,173	$ 9,264	$