

Epizyme, Inc.  
Form 10-Q  
August 08, 2016  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

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

**For the quarterly period ended June 30, 2016**

**OR**

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

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

**Commission File Number: 001-35945**

**EPIZYME, INC.**

**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**

**26-1349956**  
**(I.R.S. Employer**  
**Identification No.)**

**400 Technology Square, Cambridge, Massachusetts**  
**(Address of principal executive offices)**

**02139**  
**(Zip code)**

**617-229-5872**

**(Registrant's telephone number, including area code)**

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

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

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

Large accelerated filer  Accelerated filer

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

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

The number of shares outstanding of the registrant's common stock as of August 3, 2016: 57,956,977 shares.

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**Forward-looking Information**

This Quarterly Report on Form 10-Q contains forward-looking statements that involve substantial risks and uncertainties. These statements may be identified by such forward-looking terminology as anticipate, believe, estimate, expect, intend, may, plan, predict, project, target, potential, will, would, could, statements or variations of such terms. Our forward-looking statements are based on a series of expectations, assumptions, estimates and projections about our company, are not guarantees of future results or performance and involve substantial risks and uncertainty. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements. Actual results or events could differ materially from the plans, intentions and expectations disclosed in these forward-looking statements. Our business and our forward-looking statements involve substantial known and unknown risks and uncertainties, including the risks and uncertainties inherent in our statements regarding:

our plans to develop and commercialize novel epigenetic therapies for cancer patients;

our ongoing and planned clinical trials, including the timing of initiation and enrollment in the trials, the timing of availability of data from the trials and the anticipated results of the trials;

our ability to receive anticipated milestones under our collaborations;

the timing of and our ability to obtain and maintain regulatory approvals for our product candidates;

the rate and degree of market acceptance and clinical utility of our products;

our commercialization, marketing and manufacturing capabilities and strategy;

our intellectual property position; and

our estimates regarding expenses, future revenue, capital requirements and needs for additional financing. All of our forward-looking statements are as of the date of this Quarterly Report on Form 10-Q only. In each case, actual results may differ materially from such forward-looking information. We can give no assurance that such expectations or forward-looking statements will prove to be correct. An occurrence of or any material adverse change in one or more of the risk factors or risks and uncertainties referred to in this Quarterly Report on Form 10-Q or included in our other public disclosures or our other periodic reports or other documents or filings filed with or furnished to the Securities and Exchange Commission, or the SEC, could materially and adversely affect our business, prospects, financial condition and results of operations. Except as required by law, we do not undertake or plan to update or revise any such forward-looking statements to reflect actual results, changes in plans, assumptions, estimates or projections or other circumstances affecting such forward-looking statements occurring after the date of this Quarterly Report on Form 10-Q, even if such results, changes or circumstances make it clear that any

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forward-looking information will not be realized. Any public statements or disclosures by us following this Quarterly Report on Form 10-Q which modify or impact any of the forward-looking statements contained in this Quarterly Report on Form 10- will be deemed to modify or supersede such statements in this Quarterly Report on Form 10-Q.

Our management's discussion and analysis of our financial condition and results of operations are based upon our unaudited consolidated financial statements included in this Quarterly Report on Form 10-Q, which have been prepared by us in accordance with accounting principles generally accepted in the United States of America, or GAAP, for interim periods and with Regulation S-X promulgated under the Securities Exchange Act of 1934, as amended, or the Exchange Act. This discussion and analysis should be read in conjunction with these unaudited consolidated financial statements and the notes thereto as well as in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 31, 2015, or our Annual Report. The three months ended June 30, 2016 and 2015 are referred to as the second quarter of 2016 and 2015, respectively. Unless the context indicates otherwise, all references herein to our company include our wholly-owned subsidiary.

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements****EPIZYME, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)****(Amounts in thousands except per share data)**

	<b>June 30, 2016</b>	<b>December 31, 2015</b>
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 89,480	\$ 208,323
Marketable securities	199,136	
Accounts receivable	60	262
Prepaid expenses and other current assets	7,930	4,478
<b>Total current assets</b>	<b>296,606</b>	<b>213,063</b>
Property and equipment, net	3,617	4,089
Restricted cash and other assets	635	751
<b>Total Assets</b>	<b>\$ 300,858</b>	<b>\$ 217,903</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current Liabilities:		
Accounts payable	\$ 3,673	\$ 4,653
Accrued expenses	10,942	11,335
Current portion of capital lease obligation	590	561
Current portion of deferred revenue	956	1,900
<b>Total current liabilities</b>	<b>16,161</b>	<b>18,449</b>
Capital lease obligation, net of current portion	427	730
Deferred revenue, net of current portion	28,809	28,809
Other long-term liabilities	297	383
Commitments and contingencies		
Stockholders Equity:		
Preferred stock, \$0.0001 par value; 5,000 shares authorized; 0 shares issued and outstanding		
Common stock \$0.0001 par value; 125,000 shares authorized; 57,937 shares and 41,786 shares issued and outstanding, respectively	6	4
Additional paid-in capital	549,454	412,989
Accumulated other comprehensive income	25	

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Accumulated deficit	(294,321)	(243,461)
Total stockholders' equity	255,164	169,532
Total Liabilities and Stockholders' Equity	\$ 300,858	\$ 217,903

See notes to consolidated financial statements.

**Table of Contents****EPIZYME, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS****(UNAUDITED)****(Amounts in thousands except per share data)**

	<b>Three Months Ended June 30</b>		<b>Six Months Ended June 30</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
Collaboration revenue	\$ 473	\$ 736	\$ 945	\$ 1,647
Operating expenses:				
Research and development	21,450	20,551	39,190	77,602
General and administrative	7,424	5,970	13,270	11,207
Total operating expenses	28,874	26,521	52,460	88,809
Loss from operations	(28,401)	(25,785)	(51,515)	(87,162)
Other income, net:				
Interest income, net	404	6	624	37
Other income	16	20	31	40
Other income, net	420	26	655	77
Net loss	\$ (27,981)	\$ (25,759)	\$ (50,860)	\$ (87,085)
Other Comprehensive loss:				
Unrealized gain on available for sale securities	25		25	
Comprehensive loss	\$ (27,956)	\$ (25,759)	\$ (50,835)	\$ (87,085)
Loss per share allocable to common stockholders:				
Basic	\$ (0.49)	\$ (0.63)	\$ (0.90)	\$ (2.29)
Diluted	\$ (0.49)	\$ (0.63)	\$ (0.90)	\$ (2.29)
Weighted average shares outstanding:				
Basic	57,352	41,087	56,250	38,056
Diluted	57,352	41,087	56,250	38,056

See notes to consolidated financial statements.



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## EPIZYME, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

(Amounts in thousands)

	<b>Six Months Ended, June 30,</b>	
	<b>2016</b>	<b>2015</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (50,860)	\$ (87,085)
Adjustments to reconcile net loss to net cash used in operating activities:		
Acquired in-process research and development		40,000
Depreciation and amortization	791	653
Stock-based compensation	5,126	4,910
Amortization of discount on investments	(27)	
Loss on disposal of property and equipment		6
Changes in operating assets and liabilities:		
Accounts receivable	202	1,352
Prepaid expenses and other current assets	(3,095)	829
Accounts payable	(980)	(5,212)
Accrued expenses	(393)	2,433
Deferred revenue	(944)	(1,528)
Restricted cash and other assets	116	(136)
Other long-term liabilities	(86)	(11)
<b>Net cash used in operating activities</b>	<b>(50,150)</b>	<b>(43,789)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of available for sale securities	(199,441)	
Acquisition of in-process research and development		(40,000)
Purchases of property and equipment	(319)	(229)
<b>Net cash used in investing activities</b>	<b>(199,760)</b>	<b>(40,229)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payment under capital lease obligation	(274)	(181)
Proceeds from public offering, net of commissions	130,067	130,712
Proceeds from stock options exercised	1,498	215
Issuance of shares under employee stock purchase plan	150	239
Payment of public offering costs	(374)	(367)
<b>Net cash provided by financing activities</b>	<b>131,067</b>	<b>130,618</b>
Net increase in cash and cash equivalents	(118,843)	46,600
Cash and cash equivalents, beginning of period	208,323	190,095

Cash and cash equivalents, end of period	\$ 89,480	\$ 236,695
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**SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:**

Equipment acquired under capital lease		1,732
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See notes to consolidated financial statements.

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**EPIZYME, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**1. Overview**

Epizyme, Inc. (collectively referred to with its wholly owned, controlled subsidiary, Epizyme Securities Corporation, as Epizyme or the Company) is a clinical stage biopharmaceutical company that discovers, develops and plans to commercialize novel epigenetic therapies for cancer patients. The Company's lead product candidate, tazemetostat, is a potent and selective inhibitor of the EZH2 HMT, an enzyme that plays an important role in various cancers. The Company owns the global development and commercialization rights to tazemetostat outside of Japan. Eisai Co. Ltd (Eisai) holds the rights to develop and commercialize tazemetostat in Japan, and holds a limited right of first negotiation for the rest of Asia.

The Company has additional programs in development, including pinometostat, a clinical program that is subject to a collaboration with Celgene Corporation and Celgene RIVOT Ltd., an affiliate of Celgene Corporation (Celgene) (refer to Note 8, *Collaborations*), three preclinical programs for small molecule HMT inhibitors that are subject to a collaboration with Celgene, three preclinical programs for small molecule HMT inhibitors that are subject to a collaboration with Glaxo Group Limited, an affiliate of GlaxoSmithKline (GSK) (refer to Note 8, *Collaborations*), and multiple novel targets for which the Company retains worldwide global development and commercialization rights.

Through June 30, 2016, the Company has raised an aggregate of \$722.2 million to fund its operations, of which \$201.6 million was non-equity funding through its collaboration agreements, \$444.6 million was from the sale of common stock in the Company's public offerings and \$76.0 million was from the sale of redeemable convertible preferred stock in private financings prior to the Company's initial public offering in May 2013. As of June 30, 2016, the Company had \$288.6 million in cash, cash equivalents, and marketable securities.

The Company commenced active operations in early 2008. Since its inception, the Company has generated an accumulated deficit of \$294.3 million through June 30, 2016 and will require substantial additional capital to fund its research and development. The Company is subject to risks common to companies in the biotechnology industry, including, but not limited to, risks of failure of clinical trials and preclinical studies, the need to obtain additional financing to fund the future development of tazemetostat and the rest of its pipeline, the need to obtain marketing approval for its product candidates, the need to successfully commercialize and gain market acceptance of its product candidates, dependence on key personnel, protection of proprietary technology, compliance with government regulations, development by competitors of technological innovations and ability to transition from pilot-scale manufacturing to large-scale production of products.

**2. Summary of Significant Accounting Policies**

***Basis of Presentation***

The condensed consolidated financial statements of the Company included herein have been prepared, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted from this report, as is permitted

by such rules and regulations. Accordingly, these condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015 (the Annual Report).

The unaudited condensed consolidated financial statements include the accounts of Epizyme, Inc. and its wholly owned, controlled subsidiary, Epizyme Securities Corporation. All intercompany transactions and balances of subsidiaries have been eliminated in consolidation. In the opinion of management, the information furnished reflects all adjustments, all of which are of a normal and recurring nature, necessary for a fair presentation of the results for the reported interim periods. The Company considers events or transactions that occur after the balance sheet date but before the consolidated financial statements are issued to provide additional evidence relative to certain estimates or to identify matters that require additional disclosure. The three months ended June 30, 2016 and 2015 are referred to as the second quarter of 2016 and 2015, respectively. The results of operations for interim periods are not necessarily indicative of results to be expected for the full year or any other interim period.

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**Table of Contents*****Significant Accounting Policies******Research and Development Expenses***

As the clinical development plan for tazemetostat progresses, the Company expects research and development expenses and, in particular, the accounting for clinical trial accruals to be an increasingly significant accounting policy. Research and development expenses are expensed as incurred. Research and development expenses are comprised of costs incurred in providing research and development activities, including salaries and benefits, facilities costs, overhead costs, contract research and development services, and other outside costs. Nonrefundable advance payments for goods and services that will be used in future research and development activities are expensed when the activity has been performed or when the goods have been received rather than when the payment is made.

External research and development expenses associated with the Company's programs include clinical trial site costs, clinical manufacturing costs, costs incurred for consultants and other outside services, such as data management and statistical analysis support, and materials and supplies used in support of the clinical and preclinical programs. Internal costs of the Company's clinical programs include salaries, stock based compensation, and the portion of the Company's facility costs allocated to research and development expense. When third-party service providers' billing terms do not coincide with the Company's period-end, the Company is required to make estimates of its obligations to those third parties, including clinical trial and pharmaceutical development costs, contractual services costs and costs for supply of its drug candidates, incurred in a given accounting period and record accruals at the end of the period. The Company bases its estimates on its knowledge of the research and development programs, services performed for the period, past history for related activities and the expected duration of the third-party service contract, where applicable.

The Company generally accrues expenses related to research and development activities based on the services received and efforts expended pursuant to contracts with multiple contract research organizations that conduct and manage clinical trials, as well as other vendors that provide research and development services. The financial terms of these agreements are subject to negotiation, vary from contract to contract and may result in uneven payment flows. There may be instances in which payments made to vendors will exceed the level of services provided and result in a prepayment of the clinical expense. Payments under some of these contracts depend on factors such as the successful enrollment of subjects and the completion of clinical trial milestones. In accruing service fees, the Company estimates the time period over which services will be performed and the level of effort to be expended in each period. If the actual timing of the performance of services or the level of effort varies from estimates, the Company would adjust the accrual or prepaid accordingly in future periods.

***Cash and cash equivalents***

The Company considers all highly liquid securities with original final maturities of three months or less from the date of purchase to be cash equivalents. Cash and cash equivalents are comprised of funds in money market accounts, commercial paper and corporate notes.

***Marketable securities***

The Company classifies marketable securities with a remaining maturity when purchased of greater than three months as available for sale. Available for sale securities are maintained by the Company's investment managers and may consist of commercial paper, high-grade corporate notes, U.S. Treasury securities, U.S. government agency securities, and certificates of deposit. Available for sale securities are carried at fair value with the unrealized gains and losses included in other comprehensive income (loss) as a component of stockholders' equity until realized. Any premium or

discount arising at purchase is amortized and/or accreted to interest income and/or expense over the life of the instrument. Realized gains and losses are determined using the specific identification method and are included in other income (expense).

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If any adjustment to fair value reflects a decline in value of the investment, the Company considers all available evidence to evaluate the extent to which the decline is other-than-temporary and, if so, mark the investment to market through a charge to the Company's statement of operations and comprehensive loss.

There have been no other material changes or other required disclosures to the Company's significant accounting policies during the three and six months ended June 30, 2016, as compared to the significant accounting policies disclosed in Note 2, *Summary of Significant Accounting Policies*, of the Company's financial statements included in the Annual Report.

***Recent Accounting Pronouncements***

In May 2014, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2014-09, *Revenue From Contracts With Customers*. ASU 2014-09 amends Accounting Standards Codification ( ASC ) 605, *Revenue Recognition*, by outlining a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. In addition, the FASB recently issued ASUs 2016-10 and 2016-12, which provide clarifying amendments to ASU 2014-09. ASU 2014-09 and its related amendments will be effective for the Company for interim and annual periods beginning after December 15, 2017. The Company is evaluating the impact that this ASU may have on its consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties About an Entity's Ability to Continue as a Going Concern*. ASU 2014-15 amends ASC 205-40, *Presentation of Financial Statements - Going Concern*, by providing guidance on determining when and how reporting entities must disclose going-concern uncertainties in their financial statements, including requiring management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date of issuance of the entity's financial statements and providing certain disclosures if there is substantial doubt about the entity's ability to continue as a going concern. ASU 2014-15 will be effective for the Company for annual periods ending after December 15, 2016 and interim periods within annual periods beginning after December 15, 2016. If this standard had been adopted as of June 30, 2016, the Company believes it would have concluded there was not substantial doubt about its ability to continue as a going concern. However, the Company's disclosures in future periods may be affected by the adoption of this accounting standard.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which requires lessees to recognize a right-of-use asset and lease liability for most lease arrangements. The new standard is effective for annual reporting periods beginning after December 15, 2018 with early adoption permitted. The Company is currently evaluating the potential changes from this ASU to the Company's future financial reporting and disclosures.

In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*. The standard will revise accounting for share-based compensation arrangements, including the income tax impact and classification on the statement of cash flows. Additionally, under the new standard, entities will have to elect whether to account for forfeitures as they occur or estimate the number of awards expected to be forfeited and adjust the estimate when it is no longer probable that the award will vest. ASU 2016-09 will be effective for the Company for interim and annual periods beginning after December 15, 2016. The Company is currently evaluating the potential impact that this standard may have on its financial position, results of operations and statement of cash flows.

**3. Marketable Securities**

The following table summarizes the available for sale securities held at June 30, 2016 (in thousands):

<b>Description</b>	<b>Amortized Cost</b>	<b>Unrealized Gains</b>	<b>Unrealized Losses</b>	<b>Fair Value</b>
Commercial paper	\$ 89,598	\$	\$ (40)	\$ 89,558
Corporate notes	69,660	16		69,676
U.S. government agency securities and U.S. Treasuries	39,853	49		39,902
Total	\$ 199,111	\$ 65	\$ (40)	\$ 199,136



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The Company did not hold any available for sale securities prior to the second quarter of 2016.

The amortized cost of available for sale securities is adjusted for amortization of premiums and accretion of discounts to maturity. At June 30, 2016, the balance in the Company's accumulated other comprehensive loss was composed solely of activity related to the Company's available for sale marketable securities. There were no realized gains or losses recognized on the sale or maturity of available-for-sale securities during the three months ended June 30, 2016, and as a result, the Company did not reclassify any amounts out of accumulated other comprehensive loss for the same period.

The aggregate fair value of available for sale securities held by the Company in an unrealized loss position for less than twelve months as of June 30, 2016 was \$107.4 million. The aggregate unrealized loss for those securities in an unrealized loss position for less than twelve months as of June 30, 2016 was less than \$0.1 million. The Company determined that there was no material change in the credit risk of any of its investments. As a result, the Company determined it did not hold any investments with any other-than-temporary impairment as of June 30, 2016. The weighted average maturity of the Company's portfolio was approximately six months at June 30, 2016.

**4. Fair Value Measurements**

The Company's financial instruments as of June 30, 2016 consisted primarily of cash and cash equivalents, marketable securities and accounts receivable and accounts payable. The Company's financial instruments as of December 31, 2015 consisted primarily of cash and cash equivalents, accounts receivable and accounts payable. As of June 30, 2016 and December 31, 2015, the Company's financial assets recognized at fair value consisted of the following:

	<b>Fair Value as of June 30, 2016</b>			
	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
	<b>(In thousands)</b>			
Cash equivalents	\$ 80,191	\$ 71,092	\$ 9,099	\$
Marketable securities:				
Commercial paper	89,558		89,558	
Corporate notes	69,676		69,676	
U.S. government agency securities and treasuries	39,902		39,902	
Total	\$ 279,327	\$ 71,092	\$ 208,235	\$
	<b>Fair Value as of December 31, 2015</b>			
	<b>Total</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>
	<b>(In thousands)</b>			
Cash equivalents	\$ 197,023	\$ 197,023	\$	\$
Total	\$ 197,023	\$ 197,023	\$	\$

Cash equivalents and marketable securities have been initially valued at the transaction price and subsequently valued, at the end of each reporting period, utilizing third-party pricing services or other market observable data.

The Company measures its cash equivalents at fair value on a recurring basis. The Company classifies its cash equivalents within Level 1 of the fair value hierarchy because they are valued using observable inputs that reflect quoted prices for identical assets in active markets. The Company measures its marketable securities at fair value on a recurring basis and classifies those instruments within Level 2 of the fair value hierarchy. The pricing services utilize industry standard valuation models, including both income and market based approaches and observable market inputs to determine value of marketable securities.

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Prepaid expenses and other current assets consisted of the following:

	<b>June 30, 2016</b>	<b>December 31, 2015</b>
	<b>(In thousands)</b>	
Prepaid clinical and manufacturing costs	\$ 3,499	\$ 2,400
Interest receivable on available for sale securities	372	
Other prepaid expenses and other receivables	4,059	2,078
Total prepaid expenses and other current assets	\$ 7,930	\$ 4,478

Accrued expenses consisted of the following:

	<b>June 30, 2016</b>	<b>December 31, 2015</b>
	<b>(In thousands)</b>	
Employee compensation and benefits	\$ 2,276	\$ 3,314
Research and development expenses	7,929	6,518
Professional services and other	737	1,503
Accrued expenses	\$ 10,942	\$ 11,335

**6. Income Taxes**

The Company did not record a federal or state income tax provision or benefit for the three and six months ended June 30, 2016 and 2015 due to the expected loss before income taxes to be incurred for the years ended December 31, 2016 and 2015, as well as the Company's continued maintenance of a full valuation allowance against its net deferred tax assets.

**7. Commitments and Contingencies**

There have been no significant changes to the Company's commitments and contingencies in the three and six months ended June 30, 2016, as compared to those disclosed in Note 6, *Commitments and Contingencies* included in its Annual Report, except as summarized below.

The Company made a \$3.0 million milestone payment in the first quarter of 2016 under the second amendment to the companion diagnostic agreement with Roche Molecular Systems, Inc. (Roche).

In May 2016, the Company entered into the second amendment to its lease arrangement with ARE-TECH Square, LLC to extend the term of the leased headquarters facility by six months, from November 30, 2017 to May 31, 2018.

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In addition, the second amendment extended the Company's five year renewal option notice date by six months, from February 28, 2017 to August 31, 2017. An extension fee of \$0.2 million will be due and payable on November 30, 2017 if the Company does not (i) exercise its five year option to renew the headquarter lease on November 30, 2017 or (ii) sign a new lease with its existing landlord for a location with increased square footage.

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**8. Collaborations**

*Celgene*

In April 2012, the Company entered into a collaboration and license agreement with Celgene. In July 2015, the Company entered into an amendment and restatement of its collaboration and license agreement with Celgene.

*Agreement Structure*

Under the original agreement, the Company granted Celgene an exclusive license, for all countries other than the United States, to small molecule HMT inhibitors targeting DOT1L, including pinometostat, and an option, on a target-by-target basis, to exclusively license, for all countries other than the United States, rights to small molecule HMT inhibitors targeting any other HMT targets, excluding EZH2 and targets covered by the collaboration and license agreement with GSK. Under the original agreement, Celgene's option was exercisable during an option period that would have expired in July 2015. Under the amended and restated collaboration and license agreement:

Celgene retains its exclusive license to small molecule HMT inhibitors targeting DOT1L, including pinometostat,

Celgene's option rights have been narrowed to HMT inhibitors targeting three predefined targets (the Option Targets ),

The exclusive licenses to HMT inhibitors targeting two of the Option Targets that Celgene may acquire have been expanded to include the United States, with the exclusive license to the third Option Target continuing to be for all countries other than the United States,

Celgene's option period has been extended for each of the Option Targets and is exercisable at the time of the Company's Investigational New Drug ( IND ) filing for an HMT inhibitor targeting the applicable Option Target, upon the payment by Celgene at such time of a pre-specified development milestone-based license payment,

Celgene's license may be maintained beyond the end of phase 1 clinical development for each of the Option Targets, upon payment by Celgene at such time of a pre-specified development milestone-based license payment, and

The Company's research and development obligations with respect to each Option Target under the amended agreement have been extended for at least an additional three years, subject to Celgene exercising its option with respect to such Option Target at the time of the IND filing. Subject to the Company's opt-out rights, the Company's research and development obligations have been expanded to include the completion of a phase 1 clinical trial as to each Option Target following Celgene's exercise of its option at time of the IND filing.

The amended and restated agreement eliminated the right of first negotiation that the Company had granted to Celgene under the original agreement with respect to business combination transactions that the Company may desire to pursue

with third parties.

The Company is primarily responsible for the research strategy under the collaboration. During each applicable option period the Company is required to use commercially reasonable efforts to carry out a mutually agreed-upon research plan for each Option Target. Subject to the Company's opt-out right, for the DOT1L target and each of the Option Targets, the Company is required to conduct and solely fund development costs of the Phase 1 clinical trials for HMT inhibitors directed to such targets. After the completion of Phase 1 development, as to DOT1L and the Option Target for which the Company retains U.S. rights, Celgene and the Company will equally co-fund global development and each party will solely fund territory-specific development costs for its respective territory; and, as to the other two Option Targets, after the completion of Phase 1 development, Celgene will solely fund all development costs on a worldwide basis.

Under the original agreement, the Company received a \$65.0 million upfront payment and \$25.0 million from the sale of its series C redeemable convertible preferred stock to an affiliate of Celgene, of which \$3.0 million was considered a premium and included as collaboration arrangement consideration for a total upfront payment of \$68.0 million. In addition, the Company has received a \$25.0 million clinical development milestone payment and \$6.9 million of global development co-funding through June 30, 2016. Under the amended agreement, the Company

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received a \$10.0 million upfront payment in exchange for the Company's extension of Celgene's option rights to the Option Targets and the Company's research and development obligations. In addition, the Company is eligible to earn an aggregate of up to \$75.0 million in development milestone and license payments, up to \$365.0 million in regulatory milestone payments and up to \$170.0 million in sales milestone payments related to the three Option Targets. The Company remains eligible to earn \$35.0 million in an additional clinical development milestone payment and up to \$100.0 million in regulatory milestone payments related to DOT1L. The Company is also eligible to receive royalties on each of the Option Targets as specified in the amended and restated agreement. Due to the uncertainty of pharmaceutical development and the high historical failure rates generally associated with drug development, the Company may not receive any additional milestone or royalty payments from Celgene.

*Collaboration Revenue*

Through June 30, 2016, the Company has recognized \$73.4 million of total collaboration revenue since the inception of the collaboration, including \$0.5 million and \$0.1 million in the three months ended June 30, 2016 and 2015, respectively, and \$0.9 million and \$0.2 million in the six months ended June 30, 2016 and 2015, respectively. The Company recognized total global development co-funding as a reduction to research and development expense of less than \$0.1 million and \$0.4 million in the three months ended June 30, 2016 and 2015, respectively, and less than \$0.1 million and \$0.9 million in the six months ended June 30, 2016 and 2015, respectively.

***GSK***

In January 2011, the Company entered into a collaboration and license agreement with GSK, to discover, develop and commercialize novel small molecule HMT inhibitors directed to available targets from the Company's platform. Under the terms of the agreement, the Company granted GSK exclusive worldwide license rights to HMT inhibitors directed to three targets. Additionally, as part of the research collaboration, the Company agreed to provide research and development services related to the licensed targets pursuant to agreed upon research plans during a research term that ended January 8, 2015. In March 2014, the Company and GSK amended certain terms of this agreement for the third licensed target, revising the license terms with respect to candidate compounds and amending the corresponding financial terms, including reallocating milestone payments and increasing royalty rates as to the third target. The Company substantially completed all research obligations under this agreement by the end of the first quarter of 2015 and completed the transfer of the remaining data and materials for these programs to GSK in the second quarter of 2015.

*Agreement Structure*

Under the agreement, the Company recorded a \$20.0 million upfront payment, a \$3.0 million payment upon the execution of the March 2014 agreement amendment, \$6.0 million of fixed research funding, \$15.0 million of preclinical research and development milestone payments and \$9.0 million for research and development services. The Company is eligible to receive up to \$18.0 million in additional preclinical research and development milestone payments, up to \$109.0 million in clinical development milestone payments, up to \$275.0 million in regulatory milestone payments and up to \$218.0 million in sales-based milestone payments. In addition, GSK is required to pay the Company royalties, at percentages from the mid-single digits to the low double-digits, on a licensed product-by-licensed product basis, on worldwide net product sales, subject to reduction in specified circumstances. Due to the uncertainty of pharmaceutical development and the high historical failure rates generally associated with drug development, the Company may not receive any additional milestone payments or royalty payments from GSK. Due to the varying stages of development of each licensed target, the Company is not able to determine the next milestone that might be achieved under this agreement, if any. GSK became solely responsible for development and commercialization for each licensed target in the collaboration when the research term ended on January 8, 2015.

*Collaboration Revenue*

Through June 30, 2016, the Company has received a total of \$53.0 million in cash under the GSK agreement, which the Company recognized as collaboration revenue in the condensed consolidated statements of operations and comprehensive loss, including \$0.6 million and \$1.4 million in the three and six months ended June 30, 2015. As of December 31, 2015, the Company did not have any remaining deferred revenue related to this agreement and any future revenues will relate to any milestone payments and royalties received under the agreement, if any.



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### ***Eisai***

In April 2011, the Company entered into a collaboration and license agreement with Eisai under which the Company granted Eisai an exclusive worldwide license to its small molecule HMT inhibitors directed to the EZH2 HMT, including the Company's product candidate tazemetostat, while retaining an opt-in right to co-develop, co-commercialize and share profits with Eisai as to licensed products in the United States. Additionally, as part of the research collaboration, the Company provided research and development services related to the licensed compounds through December 31, 2014.

As of December 31, 2014, the Company had completed its performance obligations under the original agreement.

In March 2015, the Company entered into an amended and restated collaboration and license agreement with Eisai, under which the Company reacquired worldwide rights, excluding Japan, to its EZH2 program, including tazemetostat. Under the amended and restated agreement, the Company is responsible for global development, manufacturing and commercialization outside of Japan of tazemetostat and any other EZH2 product candidates, with Eisai retaining development and commercialization rights in Japan, as well as a right to elect to manufacture tazemetostat and any other EZH2 product candidates in Japan.

Under the original agreement, Eisai was solely responsible for funding all research, development and commercialization costs for EZH2 compounds. Under the amended and restated agreement, the Company is solely responsible for funding global development, manufacturing and commercialization costs for EZH2 compounds outside of Japan, including the remaining development costs due under a Roche companion diagnostic agreement, and Eisai is solely responsible for funding Japan-specific development and commercialization costs for EZH2 compounds.

The Company recorded the reacquisition of worldwide rights, excluding Japan, to the EZH2 program, including tazemetostat, under the amended and restated agreement with Eisai as an acquisition of an in-process research and development asset. As this asset was acquired without corresponding processes or activities that would constitute a business, had not achieved regulatory approval for marketing and, absent obtaining such approval, had no alternative future use, the Company recorded the \$40.0 million upfront payment made to Eisai in March 2015 as research and development expense in the consolidated statements of operations and comprehensive loss. The Company has also agreed to pay Eisai up to \$20.0 million in clinical development milestone payments, up to \$50.0 million in regulatory milestone payments and royalties at a percentage in the mid-teens on worldwide net sales of any EZH2 product, excluding net sales in Japan. The Company is eligible to receive from Eisai royalties at a percentage in the mid-teens on net sales of any EZH2 product in Japan.

### ***LYSA***

In May 2016, the Company entered into a collaboration agreement with the Lymphoma Academic Research Organisation ( LYSARC ), for the first planned combination trial of tazemetostat. LYSARC is the operational arm of the Lymphoma Study Association ( LYSA ), a premier cooperative group in France dedicated to clinical and translational research for lymphoma. This phase 1b/2 study will evaluate tazemetostat in combination with R-CHOP, the standard of care front-line combination treatment for diffuse large B-cell lymphoma (DLBCL), as a front-line treatment in elderly, high-risk patients with DLBCL and is being sponsored by LYSARC. LYSA is managing the study operations for the trial, and the Company is recognizing its share of the related expenses as those costs are incurred over the duration of the trial.

### ***Genentech***

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In June 2016, the Company entered into a collaboration agreement with Genentech Inc. ( Genentech ), a member of the Roche Group, to conduct a phase 1b clinical trial to investigate the anti-cancer effects of the Company s EZH2 inhibitor, tazemetostat, and Genentech s recently approved anti-PD-L1 cancer immunotherapy, Tecentriq

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(atezolizumab), when used in combination. The trial will evaluate this combination regimen for the treatment of patients with relapsed or refractory DLBCL. Under the agreement, each company will supply its respective anti-cancer agent to support the trial and share equally in the trial costs. Genentech is managing the study operations for the trial, and the Company is recognizing its share of the related expenses as those costs are incurred over the duration of the trial.

**Companion Diagnostics**

**Roche.** In December 2012, Eisai and the Company entered into an agreement with Roche under which Eisai and the Company engaged Roche to develop a companion diagnostic to identify patients who possess certain point mutations of EZH2. In October 2013, this agreement was amended to include additional point mutations in EZH2. The development costs due under the amended agreement with Roche were the responsibility of Eisai until the execution of the amended and restated collaboration and license agreement with Eisai in March 2015, at which time the Company assumed responsibility for the remaining development costs due under the agreement. In December 2015, the Company entered into the second amendment to the companion diagnostic agreement with Roche. The Company is responsible for the remaining development costs of \$12.0 million due under the second amendment as of June 30, 2016. The Company expects the remaining development costs under the second amendment to be paid and incurred through 2019.

Under the agreement with Roche, Roche is obligated to use commercially reasonable efforts to develop and to make commercially available the companion diagnostic. Roche has exclusive rights to commercialize the companion diagnostic.

The agreement with Roche will expire when the Company is no longer developing or commercializing tazemetostat. The Company may terminate the agreement by giving Roche 90 days written notice if the Company discontinues development and commercialization of tazemetostat or determines, in conjunction with Roche, that the companion diagnostic is not needed for use with tazemetostat. Either the Company or Roche may also terminate the agreement in the event of a material breach by the other party, in the event of material changes in circumstances that are contrary to key assumptions specified in the agreement or in the event of specified bankruptcy or similar circumstances. Under specified termination circumstances, Roche may become entitled to specified termination fees.

**9. Stock-Based Compensation**

Total stock-based compensation expense related to stock options, restricted stock units and the employee stock purchase plan was \$2.8 million and \$2.5 million for the three months ended June 30, 2016 and 2015, respectively, and \$5.1 million and \$4.9 million for the six months ended June 30, 2016 and 2015, respectively.

Stock-based compensation expense is classified in the consolidated statements of operations and comprehensive loss as follows:

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
	<b>(In thousands)</b>			
Research and development	\$ 1,366	\$ 1,437	\$ 2,613	\$ 2,795
General and administrative	1,387	1,057	2,513	2,115

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Total	\$ 2,753	\$ 2,494	\$ 5,126	\$ 4,910
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**Table of Contents****Stock Options**

The weighted-average grant date fair value of options, estimated as of the grant date using the Black-Scholes option pricing model, was \$7.27 and \$12.46 per option for those options granted during the three months ended June 30, 2016 and 2015, respectively, and \$6.43 and \$14.68 per option for those options granted during the six months ended June 30, 2016 and 2015, respectively. Key assumptions used to apply this pricing model were as follows:

	Three Months Ended June 30		Six Months Ended June 30	
	2016	2015	2016	2015
Risk-free interest rate	1.3%	1.4%	1.2%	1.5%
Expected life of options	6 years			
Expected volatility of underlying stock	79.0%	82.2%	78.9%	84.2%
Expected dividend yield	0.0%	0.0%	0.0%	0.0%

The following is a summary of stock option activity for the six months ended June 30, 2016:

	Number of Options (In thousands)	Weighted Average Exercise Price per Share	Weighted Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at December 31, 2015	3,100	\$ 15.20		
Granted	1,923	9.48		
Exercised	(758)	1.98		
Forfeited or expired	(338)	17.04		
Outstanding at June 30, 2016	3,927	\$ 14.87	8.6	\$ 4,603
Exercisable at June 30, 2016	898	\$ 17.90	6.5	\$ 2,383

As of June 30, 2016, there was \$22.4 million of unrecognized compensation cost related to stock options that are expected to vest. These costs are expected to be recognized over a weighted average remaining vesting period of 3.1 years.

**Restricted Stock Units**

The following is a summary of restricted stock unit activity for the six months ended June 30, 2016:

	Number of Units	Weighted Average Grant Date Fair Value
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		<b>per Unit</b>	
Outstanding at December 31, 2015	37,313	\$	18.49
Granted	80,732	\$	9.29
Vested	(39,349)		12.20
Outstanding at June 30, 2016	78,696	\$	12.20

In February 2016 the Company granted 80,732 restricted stock units with a grant date fair value of \$9.29 per unit, in accordance with the Company's chief financial officer's employment agreement. One quarter of these restricted stock units vested on February 9, 2016 and the remaining three quarters are vesting on a straight line basis over 36 months. As of June 30, 2016 there was \$0.7 million of unrecognized compensation cost related to restricted stock units that are expected to vest. These costs are expected to be recognized over a weighted average remaining vesting period of 2.6 years.

**Table of Contents****10. Loss Per Share**

Basic and diluted loss per share allocable to common stockholders are computed as follows:

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
	<b>(In thousands except per share data)</b>			
Net loss	\$ (27,981)	\$ (25,759)	\$ (50,860)	\$ (87,085)
Weighted average shares outstanding	57,352	41,087	56,250	38,056
Basic and diluted loss per share allocable to common stockholders	\$ (0.49)	\$ (0.63)	\$ (0.90)	\$ (2.29)

In January 2016, the Company issued an additional 15,333,334 shares of common stock in connection with a public offering. The issuance of these shares contributed to a significant increase in the Company's shares outstanding as of June 30, 2016 and in the weighted average shares outstanding for the three and six months ended June 30, 2016 when compared to the comparable prior year periods, and is expected to continue to impact the year-over-year comparability of the Company's (loss) earnings per share calculations through 2016.

The following common stock equivalents were excluded from the calculation of diluted loss per share allocable to common stockholders because their inclusion would have been anti-dilutive:

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2016</b>	<b>2015</b>	<b>2016</b>	<b>2015</b>
	<b>(In thousands)</b>			
Stock options	3,927	3,349	3,927	3,349
Unvested restricted stock units	79	37	79	37
Shares issuable under employee stock purchase plan	24	7	24	7
	4,030	3,393	4,030	3,393

**11. Related Party Transactions**

Celgene has made a series of equity investments in the Company, owning 3,674,640 shares of common stock representing 6.3% of the Company's common stock as of June 30, 2016. Refer to Note 8, *Collaborations* for additional information regarding the Company's original agreement with Celgene entered into in April 2012 and the amended and restated agreement with Celgene entered into in July 2015.

The Company recognized \$0.5 million and \$0.9 million of collaboration revenue in the three and six months ended June 30, 2016, respectively, and \$0.1 million and \$0.2 million of collaboration revenue in the three and six months ended June 30, 2015, respectively. The Company did not recognize any revenue from the Celgene collaboration in the three months ended June 30, 2015. As of June 30, 2016 and December 31, 2015, the Company's deferred revenue balances included \$29.8 million and \$30.7 million, respectively, related to the Celgene amended and restated agreement and original agreement. Additionally, the Company recorded less than \$0.1 million in each of the three and

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six months ended June 30, 2016, and \$0.4 million and \$0.9 million in the three and six months ended June 30, 2015, respectively, in global development co-funding from Celgene.



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**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**  
***Management Overview***

We are a clinical stage biopharmaceutical company that discovers, develops and plans to commercialize novel epigenetic therapies for cancer patients. We are leaders in discovering and developing small molecule inhibitors of a class of enzymes known as histone methyltransferases, or HMTs. We are also expanding our development efforts beyond HMTs and are developing small molecule inhibitors of other chromatin modifying proteins, or CMPs. CMPs mediate selective and reversible modifications to chromatin, a complex of chromosomal DNA and histone proteins that controls gene expression. This chromatin remodeling and its resultant control of gene expression are part of a larger regulatory system, commonly referred to as epigenetics. Genetic alterations within CMPs or that indirectly affect CMPs can result in changes to their activity and drive multiple types of cancer, including hematological cancers and solid tumors. We believe that inhibiting altered CMPs presents the opportunity to create, develop and commercialize multiple targeted therapeutics.

Our lead product candidate, tazemetostat, is a potent and selective inhibitor of the EZH2 HMT, an enzyme that plays an important role in various cancers. In our ongoing phase 1 clinical trial of tazemetostat in patients with relapsed or refractory non-Hodgkin lymphoma, or NHL, or in patients with advanced solid tumors, tazemetostat has shown meaningful clinical activity as a monotherapy, with an acceptable safety profile, in both NHL and in certain genetically-defined solid tumors. We are currently evaluating tazemetostat in a phase 2 study in adults with relapsed or refractory NHL, and a phase 2 study in adults and a phase 1 study in children with certain genetically-defined solid tumors, which include INI1-negative or SMARCA4-negative rhabdoid tumors, renal medullary carcinoma, epithelioid sarcoma, other INI1-negative tumors, and synovial sarcoma. We have also entered into collaborations to evaluate tazemetostat in combination with other therapies being used or investigated for the treatment of NHL. The first of these studies is being conducted in collaboration with the Lymphoma Study Association, or LYSA, a premier cooperative French lymphoma group, to evaluate tazemetostat in combination with R-CHOP, the standard of care front-line combination treatment for diffuse large B-cell lymphoma, or DLBCL, an aggressive form of NHL, in front line elderly patients with DLBCL. The second of these studies is being conducted in collaboration with Genentech, a member of the Roche Group, to investigate tazemetostat and Genentech's recently approved anti-PD-L1 cancer immunotherapy, Tecentriq (atezolizumab), when used in combination. The study will evaluate this combination regimen for the treatment of patients with relapsed or refractory DLBCL. In addition, clinical sites are open for enrollment in our phase 2 study of tazemetostat in patients with mesothelioma characterized by a loss-of-function of BAP1. We are continuing to explore in preclinical testing other tumor types that may be sensitive to tazemetostat.

We own the global development and commercialization rights to tazemetostat outside of Japan. Eisai Co. Ltd, or Eisai, holds the rights to develop and commercialize tazemetostat in Japan, and holds a limited right of first negotiation for the rest of Asia. Tazemetostat is protected by U.S. composition of matter patents, which are expected to expire in 2032. In February 2016, tazemetostat was granted orphan drug designation by the FDA for the treatment of malignant rhabdoid tumors, or MRT. The orphan drug designation applies to INI1-negative MRT as well as SMARCA4-negative malignant rhabdoid tumor of ovary, or MRTO.

Pinometostat, an inhibitor of the DOT1L HMT, is our other product candidate in clinical development. We are conducting a phase 1 clinical trial of pinometostat for the treatment of children with MLL-r, an acute leukemia with genetic alterations of the MLL gene. Enrollment in the study is complete and we anticipate presenting the data at a future medical conference. Under our collaboration with Celgene Corporation and Celgene RIVOT Ltd., an affiliate of Celgene Corporation, which we collectively refer to as Celgene, we own commercialization rights to pinometostat in the United States and Celgene owns commercialization rights to pinometostat outside the United States. Along with Celgene, we are also investigating in preclinical studies combinations of pinometostat with other targeted therapies for the treatment of adults with MLL-r.

We have additional small molecule HMT inhibitors that are being developed under our collaborations with Glaxo Group Limited (an affiliate of GlaxoSmithKline), or GSK, and Celgene. Under our collaboration with GSK, GSK is developing small molecule inhibitors against three novel HMT targets including protein arginine methyltransferase 5, or PRMT5. We discovered these HMT inhibitors using our proprietary drug discovery platform. GSK has worldwide rights to the inhibitors of the three HMT targets that we delivered to them under the collaboration. Under our collaboration with Celgene, we are developing small molecule inhibitors directed to three other HMT targets in addition to pinometostat. Under the collaboration, we are responsible for all preclinical discovery work as well as phase 1 clinical development for all three targets. Celgene has the option to license worldwide rights to inhibitors

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directed at two of the three targets, and the option to license ex-U.S. rights to inhibitors directed to the third target. We retain rights to develop and commercialize the third target in the United States. Beyond tazemetostat and pinometostat, and the partnered programs with GSK and Celgene, we have also identified multiple novel epigenetic targets for which we are developing small molecule inhibitors in preclinical drug discovery. We own the global development and commercialization rights to these programs. All of our novel targets have been identified internally using our proprietary drug discovery platform, and all of our small molecule inhibitors have been discovered internally.

We commenced active operations in early 2008, and since inception, have incurred significant operating losses. As of June 30, 2016, our accumulated deficit totaled \$294.3 million. As a clinical stage company, we expect to continue to incur significant expenses and operating losses over the next several years. Our net losses may fluctuate significantly from quarter to quarter and year to year. We expect our expenses to increase in connection with our ongoing activities, including as we execute on our clinical development plans for tazemetostat.

**Tazemetostat Development Program Update**

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The following table summarizes selected current and near-term planned studies for tazemetostat:

**Tazemetostat Clinical Program**

**Tazemetostat NHL Program**

We are evaluating tazemetostat in a five arm phase 2 study of 270 patients with relapsed or refractory NHL. The three arms enrolling patients with DLBCL are enrolling 60 patients each, and the two arms enrolling patients with follicular lymphoma (FL) are enrolling 45 patients each. The Independent Data Monitoring Committee, or IDMC, has confirmed that a pre-specified futility hurdle had been surpassed in four of the five study arms to date:

DLBCL with Germinal Center B-cell, or GCB, subtype and EZH2 mutations;

DLBCL with GCB subtype and wild-type EZH2;

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DLBCL with non-GCB subtype; and,

FL with EZH2 mutations.

The fifth cohort enrolling patients with FL with wild-type EZH2 is ongoing, but has not yet reached a point where futility can be assessed. Surpassing the pre-specified futility hurdle in each of the DLBCL arms was based on observing at least one objective response in the first ten patients enrolled. Surpassing the pre-specified futility hurdle in each of the FL arms is based on observing at least two objective responses in the first ten patients enrolled. The primary endpoint of the phase 2 study is overall response rate, and secondary endpoints include progression-free survival and duration of response. We now have sites open for enrollment in the United States, Europe, Australia and Canada and plan to open additional sites through the end of 2016.

In June 2016, we presented early data from this ongoing, international, registration supporting five-arm phase 2 study of tazemetostat in patients with relapsed or refractory NHL at the American Society of Hematology, or ASH, Meeting on Lymphoma Biology. Early data from the phase 2 clinical trial indicated that tazemetostat demonstrated a favorable safety profile and clinical activity consisting of objective responses in a heavily pre-treated patient population.

Overall trial enrollment is on track and consistent with incidence rates for NHL subtypes, with approximately 20% of enrolled DLBCL with GCB subtype and FL patients having an EZH2 mutation. As of the data cutoff date of May 27, 2016, 82 patients across all five study arms were evaluable for safety. Efficacy was assessed on 47 evaluable patients from the four cohorts confirmed to have surpassed their pre-specified futility hurdles. The non-evaluable patients included 16 patients in the arms that have surpassed futility that are too early for efficacy evaluation or for whom data are not yet entered and 19 patients from the fifth cohort who have FL with wild-type EZH2.

Tazemetostat demonstrated a favorable safety profile in all patients treated, consistent with the experience observed in the phase 1 trial. The majority of adverse events were grade 1 or grade 2 within the 82 safety-evaluable patients. The most common treatment-related adverse events (35%) were nausea, asthenia, thrombocytopenia, neutropenia and fatigue, of which seven were grade 3 or higher. All adverse events resulted in low rates of both dose reductions (4%) and dose discontinuations (6%).

Among the 47 efficacy-evaluable patients, objective responses, which consist of either a complete response (CR) or a partial response (PR) were observed. In addition, stable disease (SD) was also observed in a significant percentage of patients. In the phase 1 experience, Epizyme observed responses that evolved over time from SD to PRs and CRs. As of the data cutoff, best responses across the four cohorts were as follows:

DLBCL with GCB subtype and EZH2 mutations (n=5): one PR and two SD;

DLBCL with GCB subtype and wild-type EZH2 (n=19): two CRs, one PR and six SD;

DLBCL with non-GCB subtype (n=20): two CRs, four PRs and five SD; and,

FL with EZH2 mutations (n=3): three PRs.

All of the patients who had achieved a CR and the majority of patients who had achieved a PR or SD as best response were still on tazemetostat treatment as of the data cutoff date.

In addition, at the ASH Meeting on Lymphoma Biology, we also presented an update on the patients with relapsed or refractory NHL in the ongoing phase 1 study of tazemetostat. As of the data cutoff date of May 27, 2016, three patients with NHL remained on study, all with CRs, including one patient whose response evolved from PR to CR at 22 months.

We plan on presenting an updated assessment of tazemetostat's efficacy and safety from our five-arm phase 2 study, including objective responses, durability of responses and differences between the patient cohorts, in the first half of 2017.

*Tazemetostat Genetically Defined Solid Tumor Program*

Overall enrollment in our phase 2 study of tazemetostat in adult patients with genetically defined solid tumors is progressing well. The phase 2 study is evaluating tazemetostat in five study arms: INI1-negative or SMARCA4-

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negative rhabdoid tumors; renal medullary carcinoma; epithelioid sarcoma; other INI1-negative tumors; and synovial sarcoma, with each arm enrolling up to 30 patients. We plan on presenting an assessment of tazemetostat's efficacy and safety from this phase 2 study in the first half of 2017.

In addition, the phase 1 dose-escalation and expansion study of tazemetostat in up to 108 pediatric patients with certain INI1-negative tumors, including rhabdoid tumors and synovial sarcomas, is enrolling well. The study is currently in the dose escalation stage of the trial. In June 2016, we were invited to speak at the FDA Pediatric Subcommittee of the Oncologic Drugs Advisory Committee meeting to review our ongoing phase 1 pediatric study. We received valuable feedback from Committee members on developing tazemetostat to treat rare and extremely aggressive cancers in pediatric patients.

### Tazemetostat Combination Studies and Other Indications

We are also exploring the use of tazemetostat in combination for the treatment of DLBCL. We are collaborating with LYSA to undertake a phase 1b/2 study to evaluate tazemetostat in combination with R-CHOP as a front-line treatment in elderly, high-risk patients with DLBCL. Clinical sites are expected to begin enrolling and dosing patients in the second half of 2016.

In June 2016, we entered into a collaboration agreement with Genentech to conduct a phase 1b clinical trial to investigate the anti-cancer effects of tazemetostat and Tecentriq when used in combination. The trial will evaluate this combination regimen for the treatment of patients with relapsed or refractory DLBCL. Under the agreement, each company will supply its respective anti-cancer agent to support the trial and share in the trial costs. Genentech is managing the study operations for the trial, which is expected to begin enrolling and dosing patients in the second half of 2016.

We have recently initiated a multi-center phase 2 study evaluating tazemetostat as a monotherapy treatment for adult patients with mesothelioma characterized by BAP1 loss-of-function. The international study recently opened for enrollment in the U.S. and is expected to enroll approximately 70 patients.

### **Corporate Strategy**

Our goal is to become a fully integrated development and commercial oncology company developing novel epigenetic therapies for cancer patients. We have a robust proprietary drug discovery platform and the demonstrated ability to move candidates into clinical development. As we prepare to commercially launch tazemetostat, if approved, we plan to build out the infrastructure necessary to support the successful launch and marketing of this compound. The key elements of our strategy to achieve this goal are to:

**Rapidly Advance the Clinical Development of Tazemetostat.** We are executing a comprehensive clinical development program of tazemetostat for NHL and certain genetically-defined solid tumors. If we see sufficient evidence of a therapeutic effect in any of these trials, we plan to meet with regulatory authorities to discuss the possibility of an expedited clinical development and regulatory pathway for the applicable program. If sufficiently safe and active in the target patient populations, we believe that tazemetostat may be able to rely on an expedited regulatory approval process.

**Seek to Expand the Range of Potential Indications for Tazemetostat.** Our R-CHOP combination study is designed to investigate the utility of tazemetostat in front line treatment of elderly patients with DLBCL, which would expand the potential commercial opportunity for tazemetostat. We also have over two dozen academic collaborations which are investigating the role of tazemetostat in other cancer types in preclinical models. If we see strong preclinical evidence of sensitivity of specific tumors to EZH2 inhibition, and if a medical need exists, we will consider initiating proof of concept human clinical trials. Our goal is to initiate clinical development of tazemetostat in five new indications over the next five years. The first of these studies is our phase 2 study evaluating tazemetostat in adult patients with mesothelioma characterized by BAP1 loss-of-function.

**Establish Commercialization and Marketing Capabilities in the United States.** We have retained commercialization rights in the United States for all of our programs, other than the three programs that are the subject of our GSK collaboration and two of the programs that are the subject of our



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collaboration with Celgene. We plan to retain commercialization rights in the United States and possibly selected foreign jurisdictions in connection with any future oncology collaborations. We intend to build a focused specialty sales force and marketing capabilities to commercialize any of our oncology drugs that receive regulatory approval in the United States, and the capability of leading global commercial strategy.

**Use Our Drug Discovery Platform to Build a Pipeline of Proprietary CMP Inhibitors.** Using our proprietary drug discovery platform, we are developing additional novel, small molecule inhibitors of disease associated CMPs, with the goal of delivering three new, wholly-owned programs into the clinic by 2020. We currently hold U.S. development and commercialization rights to one of our three preclinical programs subject to Celgene's option under our collaboration. In addition, we have identified multiple novel CMP targets against which we are developing small molecule inhibitors in preclinical drug discovery, for which we own all development and commercialization rights.

**Leverage Collaborations.** Our therapeutic collaborations with Celgene, GSK, Eisai, LYSA and Genentech provide us with access to the considerable scientific, development, regulatory and commercial capabilities of our collaborators. Our collaborations with Celgene and GSK potentially provide us with significant funding. We believe that collaborations like these can contribute to our ability to rapidly advance our product candidates, build our product platform and concurrently progress a wide range of discovery and development programs, and we may seek to enter into additional therapeutic collaborations in the future.

**Develop Companion Diagnostics for Use with Our Therapeutic Product Candidates.** We plan to seek to develop companion diagnostics for use in connection with our therapeutic product candidates where appropriate. We believe that this approach may enable us to accelerate the clinical development and regulatory timelines for our therapeutic product candidates and, for any of our therapeutic product candidates that receive marketing approval, improve patient care by identifying patients who are more likely to benefit from the therapy. We intend to develop diagnostics based on currently available diagnostic technologies to the extent possible in order to minimize development and regulatory risk of our diagnostic programs. We are working with Roche Molecular Systems, Inc., or Roche, to develop a companion diagnostic, based on currently available technology, for use with tazemetostat for NHL patients with EZH2 point mutations and are relying on existing laboratory tests for use with pinometostat to identify MLL-r patients. We also plan to develop a companion diagnostic to identify BAP1 loss-of-function in patients' tumors for our mesothelioma program, if needed.

### ***Collaborations***

Refer to Note 8, *Collaborations*, of the notes to our consolidated financial statements included in this Quarterly Report on Form 10-Q for a description of the key terms of our arrangements with Eisai, Celgene GSK, LYSA and Genentech, as well as the related accounting and revenue and expense recognition considerations.

### ***Results of Operations***

#### ***Collaboration Revenue***

The following is a comparison of collaboration revenue for the three and six months ended June 30, 2016 and 2015:

	<b>Three Months Ended</b>			<b>Six Months Ended</b>		
	<b>June 30,</b>			<b>June 30,</b>		
	<b>2016</b>	<b>2015</b>	<b>Change</b>	<b>2016</b>	<b>2015</b>	<b>Change</b>

(In millions)

Collaboration revenue	\$ 0.5	\$ 0.7	\$ (0.2)	\$ 0.9	\$ 1.6	\$ (0.7)
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Our revenue consists of collaboration revenue, including amounts recognized from deferred revenue related to upfront payments for licenses or options to obtain licenses in the future, research and development services revenue earned and milestone payments earned under collaboration and license agreements with our collaboration partners.

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The following table summarizes our collaboration revenue, by collaboration, for the three and six months ended June 30, 2016 and 2015:

Collaboration Partner	Three Months Ended			Six Months Ended		
	June 30, 2016	2015	Change	June 30, 2016	2015	Change
(in millions)						
<b>Celgene</b>						
Upfront revenue:	0.5	0.1	0.4	0.9	0.2	0.7
<b>GSK</b>						
Upfront revenue:		0.4	(0.4)		0.9	(0.9)
Research and development and other revenue:		0.2	(0.2)		0.5	(0.5)
	0.5	0.7	(0.2)	0.9	1.6	(0.7)

*Celgene.* Collaboration revenue attributed to the Celgene collaboration increased in the three and six months ended June 30, 2016 compared to the three and six months ended June 30, 2015, primarily due to the recognition of deferred revenue attributed to the pinometostat clinical trial services as part of the accounting for the amended and restated Celgene agreement, which was entered into during the third quarter of 2015.

As of June 30, 2016, all of our deferred revenue related to our Celgene collaboration. The recognition of deferred revenue under the amended and restated Celgene agreement is largely dependent on the future development of the non-pinometostat targets that are subject to the collaboration, as \$28.8 million of the \$29.8 million of total deferred revenue as of June 30, 2016 relates to the non-pinometostat targets. We do not expect to recognize any of the remaining \$28.8 million of deferred revenue as of June 30, 2016 related to the three non-pinometostat targets for the next several years, unless or until Celgene exercises their option rights with respect to those targets or those option rights lapse. We expect to recognize the other \$1.0 million of deferred revenue related to the Celgene agreement through December 31, 2016, as we provide the remaining research and development services related to the pinometostat phase 1 clinical trials.

*GSK.* We did not recognize collaboration revenue attributable to the GSK collaboration in the three and six months ended June 30, 2016, primarily due to the substantial completion of research obligations under the collaboration in the prior year. Since we have no further performance obligations under the GSK collaboration, future revenues will relate to milestone payments and royalties received under the agreement, if any.

*Research and Development*

Research and development expenses consist of expenses incurred in performing research and development activities, including clinical trial and related clinical manufacturing expenses, fees paid to external providers of research and development services, third party clinical research organizations, or CROs, compensation and benefits for full-time research and development employees, facilities expenses, overhead expenses, and other outside expenses. Most of our research and development costs are external costs, which we track on a program-by-program basis. Our internal research and development costs are primarily compensation expenses for our full-time research and development employees, including stock-based compensation expense.

In our early-stage research, we identify and prioritize novel HMTs and other CMPs that are implicated in cancer and other diseases, and develop potent and selective small molecule inhibitors of these targets. During this phase of research, our external costs primarily relate to lead discovery, biology, drug metabolism and pharmacokinetics and chemistry services from third party providers. As product candidates progress into preclinical and clinical development, external costs are driven by clinical trial costs, manufacturing expenses, and third-party research and development expenses. Our research and development team is organized such that the strategy, design, management and evaluation of results of our research and development plans is accomplished internally while a significant portion of our research and development activities are executed using our multinational network of external providers of research and development services.

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In circumstances where our collaboration and license agreements provide for equally co-funded global development under joint risk sharing collaborations, and where we are the study sponsor, such as our Celgene collaboration, amounts received for co-funding are recorded as a reduction to research and development expense.

The following is a comparison of research and development expenses for the three and six months ended June 30, 2016 and 2015:

	Three Months Ended June 30,			Six Months Ended June 30,		
	2016	2015	Change	2016	2015	Change
	(In millions)					
Research and development	\$ 21.5	\$ 20.6	\$ 0.9	\$ 39.2	\$ 77.6	\$ (38.4)

During the three months ended June 30, 2016, total research and development expenses increased by \$0.9 million, primarily due to expansion of the tazemetostat clinical program and internal research and development expenses which more than offset the period-over-period reduction of pinometostat costs. During the six months ended June 30, 2016 total research and development expenses decreased by \$38.4 million, primarily due to the \$40.0 million upfront payment that we made in the first quarter of 2015 to Eisai to reacquire the worldwide rights, excluding Japan, to the EZH2 program, including tazemetostat.

The following table illustrates the components of our research and development expenses:

Product Program	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
	(In millions)			
External research and development expenses:				
Tazemetostat and related EZH2 programs	\$ 9.7	\$ 8.6	\$ 16.2	\$ 50.0
Pinometostat and related DOT1L programs	0.2	1.4	1.1	3.4
Discovery and preclinical stage product programs, collectively	3.8	3.5	7.0	9.7
Internal research and development expenses	7.8	7.1	14.9	14.5
Total research and development expenses	\$ 21.5	\$ 20.6	\$ 39.2	\$ 77.6

External research and development costs include ongoing phase 1 and phase 2 clinical trial costs, discovery and preclinical research in support of the tazemetostat program, expenses associated with our companion diagnostic program, and external manufacturing costs related to the acquisition of active pharmaceutical ingredient and manufacturing of clinical drug supply. External research and development expenses for tazemetostat for the three months ended June 30, 2016 increased by \$1.1 million compared to the three months ended June 30, 2015. After adjusting for the prior year first quarter payment of \$40.0 million to Eisai, external research and development expenses for tazemetostat increased \$6.2 million during the six months ended June 2016, as compared to the three months ended June 30, 2015. The increase in tazemetostat related spending in the three and six months ended June 30, 2016 is primarily a result of the increase in tazemetostat clinical trial activity, the impact of which was partially offset by manufacturing related costs related to the reacquisition of tazemetostat from Eisai in the first half of 2015.

External research and development expenses for pinometostat decreased by \$1.2 million and \$2.3 million for the three and six months ended June 30, 2016, respectively, as compared to the three and six months ended June 30, 2015, respectively. The decline in program spending reflects our completion of enrollment in the pinometostat adult and pediatric clinical trials and the associated reduction in costs. We completed enrollment in our pinometostat adult phase 1 clinical trial in the third quarter of 2015 and the pediatric phase 1 clinical trial in the first quarter of 2016. Research and development expenses for pinometostat for each of the three and six months ended June 30, 2016 are net of less than \$0.1 million of global development co-funding from Celgene, as compared to \$0.4 million and \$0.9 million for the three and six months ended June 30, 2015, respectively.

External research and development expenses for discovery and preclinical stage product programs increased \$0.3 million for the three months ended June 30, 2016 as compared to the three months ended June 30, 2015. This

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compares to a \$2.7 million decrease for the six months ended June 30, 2016 as compared to the six months ended June 30, 2015. The three and six month fluctuations were driven by the reprioritization of our discovery and preclinical programs in the first quarter of 2015.

Internal research and development expenses are primarily compensation expenses for our full-time research and development employees. Internal research and development expenses increased by \$0.7 million and \$0.4 million for the three and six months ended June 30, 2016, respectively, as compared to the three and six months ended June 30, 2015, respectively. The increase was driven by increased compensation related expenses associated with increased hiring to support the expansion of the tazemetostat program and our preclinical research efforts.

We expect that research and development expenses will increase significantly in the remainder of 2016. This increase will be driven by the planned expansion of clinical trial activity for tazemetostat, including the initiation of a study in mesothelioma, the initiation of two combination trials in DLBCL, the expansion of our ongoing studies in NHL and solid tumors. In addition, we expect our discovery and preclinical research costs to increase throughout the remainder of 2016 as we continue the research effort for our partnered targets and expand research efforts on our novel epigenetic targets.

*General and Administrative*

The following is a comparison of general and administrative expenses for the three and six months ended June 30, 2016 and 2015:

	<b>Three Months Ended June 30,</b>			<b>Six Months Ended June 30,</b>		
	<b>2016</b>	<b>2015</b>	<b>Change</b>	<b>2016</b>	<b>2015</b>	<b>Change</b>
	<b>(In millions)</b>					
General and administrative	\$ 7.4	\$ 6.0	\$ 1.4	\$ 13.3	\$ 11.2	\$ 2.1

General and administrative expenses consist primarily of salaries and related benefits, including stock-based compensation, related to our executive, finance, intellectual property, business development and support functions. Other general and administrative expenses include allocated facility-related costs not otherwise included in research and development expenses, travel expenses and professional fees for auditing, tax and legal services, including intellectual property and related legal services.

For the three and six months ended June 30, 2016, our general and administrative expenses increased compared to the three and six months ended June 30, 2015, primarily due to higher compensation-related expenses associated with the staffing of key leadership roles in the second quarter of 2016. We expect that general and administrative expenses will increase modestly over the remainder of 2016.

*Other Income, net*

Other income (expense), net consists of interest income earned on our cash equivalents and marketable securities, net of imputed interest expense paid under our capital lease obligation, and other income recorded from a tax incentive award received in 2013. Interest income, net increased \$0.4 and \$0.6 million for the three and six months ended June 30, 2016, respectively, compared to the three and six months ended June 30, 2015, respectively, primarily due to our increased cash balance as a result of the January 2016 financing.

*Income Tax Expense*

We did not record a federal or state income tax provision or benefit for the three and six months ended June 30, 2016 and 2015 due to the expected loss before income taxes to be incurred for the years ended December 31, 2016 and 2015, as well as our continued maintenance of a full valuation allowance against our net deferred tax assets.

**Liquidity and Capital Resources**

Through June 30, 2016, we have raised an aggregate of \$722.2 million to fund our operations, of which \$201.6 million was non-equity funding through our collaboration agreements, \$444.6 million was from the sale of common stock in our public offerings and \$76.0 million was from the sale of redeemable convertible preferred stock. As of June 30, 2016, we had \$288.6 million in cash, cash equivalents and marketable securities.



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On April 15, 2016, we entered into a Sales Agreement with Cowen and Company, LLC, or Cowen, to sell, from time to time, shares of our common stock having an aggregate sales price of up to \$50,000,000 through an ATM offering program under which Cowen would act as sales agent, which we refer to as the ATM Offering. The shares that may be sold under the Sales Agreement, if any, would be issued and sold pursuant to the Company's \$250,000,000 universal shelf registration statement on Form S-3 that was declared effective by the Securities and Exchange Commission on April 29, 2016. Through August 8, 2016, we have not sold any shares of our common stock in the ATM Offering. We have no obligation to sell any of our common stock under the Sales Agreement.

In addition to our existing cash, cash equivalents and marketable securities, we may receive research and development co-funding and are eligible to earn a significant amount of option exercise and milestone payments under our collaboration agreements. Our ability to earn these payments and the timing of earning these payments is dependent upon the outcome of our research and development activities and is uncertain at this time.

## ***Funding Requirements***

Our primary uses of capital are, and we expect will continue to be, clinical trial costs, third party research and development services, compensation and related expenses, laboratory and related supplies, our potential future milestone payment obligations to Eisai and Roche under the amended Eisai collaboration agreement and Roche companion diagnostic agreement, legal and other regulatory expenses and general overhead costs.

Because our product candidates are in various stages of clinical and preclinical development and the outcome of these efforts is uncertain, we cannot estimate the actual amounts necessary to successfully complete the development and commercialization of our product candidates or whether, or when, we may achieve profitability. Until such time, if ever, as we can generate substantial product revenues, we expect to finance our cash needs through a combination of equity or debt financings and collaboration arrangements. Except for any obligations of our collaborators to make license, milestone or royalty payments under our agreements with them, we do not have any committed external sources of liquidity. To the extent that we raise additional capital through the future sale of equity or debt, the ownership interest of our stockholders may be diluted, and the terms of these securities may include liquidation or other preferences that adversely affect the rights of our existing common stockholders. Debt financing and preferred equity financing, if available, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, making capital expenditures or declaring dividends. If we raise additional funds through collaboration arrangements in the future, we may have to relinquish valuable rights to our technologies, future revenue streams or product candidates or grant licenses on terms that may not be favorable to us. If we are unable to raise any additional funds that may be needed through equity or debt financings when needed, we may be required to delay, limit, reduce or terminate our product development or future commercialization efforts or grant rights to develop and market product candidates that we would otherwise prefer to develop and market ourselves.

## ***Outlook***

Based on our research and development plans and our timing expectations related to the progress of our programs, we expect that our existing cash, cash equivalents and marketable securities as of June 30, 2016, will be sufficient to fund our planned operating expenses and capital expenditure requirements into at least the second quarter of 2018, without giving effect to any potential option exercise fees or milestone payments we may receive under our collaboration agreements. We have based this estimate on assumptions that may prove to be wrong, particularly as the process of testing drug candidates in clinical trials is costly and the timing of progress in these trials is uncertain. As a result, we could use our capital resources sooner than we expect.



**Table of Contents*****Cash Flows***

The following is a summary of cash flows for the six months ended June 30, 2016 and 2015:

	<b>Six Months Ended June 30,</b>	
	<b>2016</b>	<b>2015</b>
	<b>(In millions)</b>	
Net cash used in operating activities	\$ (50.2)	\$ (43.8)
Net cash used in investing activities	(199.8)	(40.2)
Net cash provided by financing activities	131.1	130.6

***Net cash used in operating activities***

The increase in net cash used in operating activities during the six months ended June 30, 2016, primarily relates to a higher net loss in the period, after adjusting for the \$40.0 million payment made to Eisai in the prior year, which is classified as an investing cash outflow, and an increase in prepaid expenses and deferred costs in the period.

Net cash used in operating activities for the six months ended June 30, 2016 primarily relates to our net loss of \$50.9 million and a net \$5.2 million use of cash from changes in working capital, which was offset by non-cash stock based compensation of \$5.1 million and depreciation of \$0.8 million. The most significant items affecting working capital in the six months ended June 30, 2016 include increased clinical related prepaid costs, other prepaid expenses, and a decreased level of accounts payable and accrued expenses.

Net cash used in operating activities for the six months ended June 30, 2015 reflects the cash payments made for research and development and general administrative expenses, excluding the \$40.0 million upfront payment made to Eisai upon the execution of our amended and restated collaboration and license agreement in March 2015, which is classified as an investing activity in the consolidated statement of cash flows, and a net use of cash related to working capital changes of \$2.2 million, partially offset by non-cash stock based compensation of \$4.9 million and depreciation of \$0.7 million.

***Net cash used in investing activities***

Net cash used in investing activities during the six months ended June 30, 2016 reflect \$199.4 million of purchases of available for sale securities and \$0.3 million of purchases of property and equipment during the period. Net cash used in investing activities during the six months ended June 30, 2015, reflects the \$40.0 million upfront payment made to Eisai upon the execution of our amended and restated collaboration and license agreement, under which we reacquired worldwide rights, excluding Japan, to tazemetostat, as well as \$0.2 million of purchases of property and equipment.

***Net cash provided by financing activities***

Net cash provided by financing activities of \$131.1 million during the six months ended June 30, 2016 primarily reflects net cash received from our January 2016 public offering of our common stock of \$129.7 million as well as cash received from stock option exercises and the purchase of shares under our employee stock purchase plan. This amount was offset in part by the payment of \$0.3 million of principal on our capital lease obligation.

Net cash provided by financing activities of \$130.6 million during the six months ended June 30, 2015 primarily reflects net cash received from our March 2015 public offering of our common stock as well as cash received for stock

option exercises and the purchase of shares under our employee stock purchase plan.

### **Critical Accounting Policies**

Our critical accounting policies are those policies which require the most significant judgments and estimates in the preparation of our consolidated financial statements. Management has determined that our most critical accounting policies are those relating to revenue recognition, stock-based compensation, acquired in-process research and development and research and development expenses, including our accounting for clinical trial expense and accruals. As our clinical development plan for tazemetostat progresses, we expect research and development expenses and, in particular, our accounting for clinical trial accruals to be an increasingly important critical accounting policy. Other than as disclosed with respect to accrued research and development expenses, there have been no material changes or other required disclosures to our critical accounting policies disclosed in our Annual Report on Form 10-K for our fiscal year ended December 31, 2015.

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***Accrued research and development expenses***

As part of the process of preparing our financial statements, we are required to estimate our accrued expenses as of each balance sheet date. This process involves reviewing open contracts and purchase orders, communicating with our personnel to identify services that have been performed on our behalf and estimating the level of service performed and the associated cost incurred for the service when we have not yet been invoiced or otherwise notified of the actual cost. The majority of our service providers invoice us monthly in arrears for services performed or when contractual milestones are met. We make estimates of our accrued expenses as of each balance sheet date in our financial statements based on facts and circumstances known to us at that time. We periodically confirm the accuracy of our estimates with the service providers and make adjustments if necessary. Examples of estimated accrued research and development expenses include fees paid to:

contract research organizations in connection with clinical trials;

investigative sites in connection with clinical trials;

vendors in connection with non-clinical development activities; and

vendors related to product manufacturing, development and distribution of clinical supplies.

We generally accrue expenses related to research and development activities based on the services received and efforts expended pursuant to contracts with multiple contract research organizations that conduct and manage clinical trials on our behalf as well as other vendors that provide research and development services. The financial terms of these agreements are subject to negotiation, vary from contract to contract and may result in uneven payment flows. There may be instances in which payments made to our vendors will exceed the level of services provided and result in a prepayment of the expense. Payments under some of these contracts depend on factors such as the successful enrollment of subjects and the completion of clinical trial milestones. In accruing service fees, we estimate the time period over which services will be performed and the level of effort to be expended in each period. If the actual timing of the performance of services or the level of effort varies from our estimate, we would adjust the accrual or prepaid accordingly. Non-refundable advance payments for goods and services that will be used in future research and development activities are expensed when the activity has been performed or when the goods have been received rather than when the payment is made.

Although we do not expect our estimates to be materially different from amounts actually incurred, if our estimates of the status and timing of services performed differ from the actual status and timing of services performed we may report amounts that are too high or too low in any particular period. To date, there have been no material differences from our estimates to the amount actually incurred.

***Recent Accounting Pronouncements***

In May 2014, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update, or ASU, No. 2014-09, *Revenue From Contracts With Customers*. ASU 2014-09 amends Accounting Standards Codification, or ASC, 605, *Revenue Recognition*, by outlining a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. In addition, the FASB recently issued ASUs 2016-10 and 2016-12,

which provide clarifying amendments to ASU 2014-09. ASU 2014-09 and its related amendments will be effective for us for interim and annual periods beginning after December 15, 2017. We are evaluating the impact that this ASU may have on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties About an Entity's Ability to Continue as a Going Concern*. ASU 2014-15 amends ASC 205-40, *Presentation of Financial Statements - Going Concern*, by providing guidance on determining when and how reporting entities must disclose going-concern uncertainties in their financial statements, including requiring management to perform interim and annual assessments of an entity's ability to continue as a going concern within one year of the date of issuance of the entity's financial statements and providing certain disclosures if there is substantial doubt about the entity's ability to continue as a going concern. ASU 2014-15 will be effective for us for annual periods ending after December 15, 2016 and interim periods within annual periods beginning after December 15, 2016. If this standard had been

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adopted as of June 30, 2016, we believe that we would have concluded there was not substantial doubt about our ability to continue as a going concern. However, our disclosures in future periods may be affected by the adoption of this accounting standard.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*, which requires lessees to recognize a right-of-use asset and lease liability for most lease arrangements. The new standard is effective for annual reporting periods beginning after December 15, 2018 with early adoption permitted. We are currently evaluating the potential changes from this ASU to our future financial reporting and disclosures.

In March 2016, the FASB issued ASU 2016-09, *Improvements to Employee Share-Based Payment Accounting*. The standard will revise accounting for share-based compensation arrangements, including the income tax impact and classification on the statement of cash flows. Additionally, under the new standard, entities will have to elect whether to account for forfeitures as they occur or estimate the number of awards expected to be forfeited and adjust the estimate when it is no longer probable that the award will vest. The standard is effective for annual and interim periods beginning after December 15, 2016. Early adoption is permitted. We are currently evaluating the potential impact that this standard may have on our financial position, results of operations and statement of cash flows.

## **Contractual Obligations**

In December 2012, Eisai and we entered into an agreement with Roche under which Eisai and we engaged Roche to develop a companion diagnostic to identify patients who possess certain point mutations of EZH2. In October 2013, this agreement was amended to include additional point mutations in EZH2. The \$21.5 million of development costs due under the amended agreement with Roche were the responsibility of Eisai until the execution of our amended and restated collaboration and license agreement with Eisai in March 2015, at which time we assumed responsibility for the remaining development costs due under the agreement. In December 2015, we entered into the second amendment to the companion diagnostic agreement with Roche and made a \$3.0 million milestone payment in the first quarter of 2016. We are responsible for the remaining development costs of \$12.0 million due under the second amendment as of June 30, 2016.

In May 2016, we entered into the second amendment to our lease arrangement with ARE-TECH Square, LLC to extend the term of our leased headquarters facility by six months, from November 30, 2017 to May 31, 2018. In addition, the second amendment extends our five year renewal option notice date by six months, from February 28, 2017 to August 31, 2017. An extension fee of \$0.2 million will be due and payable on November 30, 2017 if we do not (i) exercise our five year option to renew our headquarter lease on November 30, 2017 or (ii) sign a new lease with our existing landlord for a location with increased square footage.

Refer to Note 8, *Collaborations*, of the notes to our consolidated financial statements included in this Quarterly Report on Form 10-Q for a description of our arrangements with respect to the LYSA and Genentech collaboration agreements.

There were no other significant changes to our contractual obligations during the six months ended June 30, 2016. For a complete discussion of our contractual obligations, please refer to our *Management's Discussion and Analysis of Financial Condition and Results of Operations* in the Annual Report.

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

The market risk inherent in our financial instruments and in our financial position represents the potential loss arising from adverse changes in interest rates. As of June 30, 2016, we had cash equivalents and available for sale securities of \$279.3 million consisting of money market funds, corporate bonds, commercial paper and government-related obligations. Our primary exposure to market risk is interest rate sensitivity, which is affected by changes in the general level of U.S. interest rates. We estimate that a hypothetical 100-basis point change in market interest rates would impact the fair value of our investment portfolio as of June 30, 2016 by \$1.2 million.

We contract with CROs and manufacturers internationally. Transactions with these providers are predominantly settled in U.S. dollars and, therefore, we believe that we have only minimal exposure to foreign currency exchange risks. We do not hedge against foreign currency risks.



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### **Item 4. Controls and Procedures** **Disclosure Controls and Procedures**

We have established disclosure controls and procedures designed to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and is accumulated and communicated to management, including the principal executive officer (our Chief Executive Officer) and principal financial officer (our Chief Financial Officer), to allow timely decisions regarding required disclosure.

Our management, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Management recognizes that any disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives. Our disclosure controls and procedures have been designed to provide reasonable assurance of achieving their objectives. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of June 30, 2016.

### ***Changes in Internal Control over Financial Reporting***

No change in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) occurred during the three months ended June 30, 2016 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II - OTHER INFORMATION**

### **Item 1A. Risk Factors**

Careful consideration should be given to the following risk factors, in addition to the other information set forth in this Quarterly Report on Form 10-Q and in other documents that we file with the SEC, in evaluating the Company and our business. Investing in our common stock involves a high degree of risk. If any of the following risks and uncertainties actually occurs, our business, prospects, financial condition and results of operations could be materially and adversely affected. The risks described below are not intended to be exhaustive and are not the only risks facing the Company. New risk factors can emerge from time to time, and it is not possible to predict the impact that any factor or combination of factors may have on our business, prospects, financial condition and results of operations.

### **Risks Related to the Discovery and Development of Our Product Candidates**

*Our research and development is focused on the creation of novel epigenetic therapies for cancer patients, which is a rapidly evolving area of science, and the approach we are taking to discover and develop drugs is novel and may never lead to marketable products.*

The discovery of novel epigenetic therapies for cancer patients is an emerging field, and the scientific discoveries that form the basis for our efforts to discover and develop product candidates are relatively new. The scientific evidence to support the feasibility of developing product candidates based on these discoveries is both preliminary and limited. Although epigenetic regulation of gene expression plays an essential role in biological function, few drugs premised on epigenetics have been discovered. Moreover, those drugs based on an epigenetic mechanism that have received

marketing approval are in different target classes than HMTs, where our research and development is principally focused. Although preclinical studies suggest that genetic alterations can result in changes to the activity of HMTs, making them oncogenic, to date no company has translated these biological observations into systematic drug discovery that has yielded a drug that has received marketing approval. We believe that we are the first company to conduct a clinical trial of an HMT inhibitor. Therefore, we do not know if our approach of inhibiting HMTs to treat cancer patients will be successful.

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***We are early in our development efforts and have only two product candidates in clinical trials. All of our other product candidates are still in preclinical development. If we are unable to commercialize our product candidates or experience significant delays in doing so, our business will be materially harmed.***

We are early in our development efforts and have only two product candidates in clinical trials. All of our other product candidates are still in preclinical development. We have invested substantially all our efforts and financial resources in the identification and preclinical and clinical development of inhibitors of HMTs and other CMPs. Our ability to generate product revenues, which we do not expect will occur for several years, if ever, will depend heavily on the successful development and eventual commercialization of our product candidates. The success of our product candidates will depend on several factors, including the following:

successful completion of preclinical studies and clinical trials;

receipt of marketing approvals from applicable regulatory authorities;

obtaining and maintaining patent and trade secret protection and regulatory exclusivity for our product candidates;

making arrangements with third party manufacturers for, or establishing, commercial manufacturing capabilities;

launching commercial sales of the products, if and when approved, whether alone or in collaboration with others;

acceptance of the products, if and when approved, by patients, the medical community and third party payors;

effectively competing with other therapies;

obtaining and maintaining healthcare coverage and adequate reimbursement;

protecting our rights in our intellectual property portfolio; and

maintaining a continued acceptable safety profile of the products following approval.

If we do not achieve one or more of these factors in a timely manner or at all, we could experience significant delays or an inability to successfully commercialize our product candidates, which would materially harm our business.

***We may not be successful in our efforts to use and expand our proprietary drug discovery platform to build a pipeline of product candidates.***

A key element of our strategy is to use and expand our proprietary drug discovery platform to build a pipeline of small molecule inhibitors of HMT and other CMP targets and progress these product candidates through clinical development for the treatment of a variety of different types of cancer. Although our research and development efforts to date have resulted in a pipeline of programs directed to specific HMT and other CMP targets, we may not be able to develop product candidates that are safe and effective CMP inhibitors. Even if we are successful in continuing to build our pipeline, the potential product candidates that we identify may not be suitable for clinical development, including as a result of being shown to have harmful side effects or other characteristics that indicate that they are unlikely to be products that will receive marketing approval and achieve market acceptance. If we do not successfully develop and commercialize product candidates based upon our technological approach, we will not be able to obtain product revenues in future periods, which likely would result in significant harm to our financial position and adversely affect our stock price.

***Clinical drug development involves a lengthy and expensive process, with an uncertain outcome. We may incur additional costs or experience delays in completing, or ultimately be unable to complete, the development and commercialization of our product candidates.***

Two of our product candidates are in clinical development, and our remaining product candidates are in preclinical development. The risk of failure for each of our product candidates is high. It is impossible to predict when or if any of our product candidates will prove effective or safe in humans or will receive regulatory approval. Before

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obtaining marketing approval from regulatory authorities for the sale of any product candidate, we must complete preclinical development and then conduct extensive clinical trials to demonstrate the safety and efficacy of our product candidates in humans.

Product candidates are subject to continued preclinical safety studies, which may be conducted concurrent with our clinical testing. The outcomes of these safety studies may delay the launch of or enrollment in future clinical studies. For example, in the course of our preclinical safety studies of tazemetostat, we observed the development of lymphoma in Sprague Dawley rats. We have informed the relevant international regulatory authorities, the FDA and the clinical investigators of these findings. Expansion of our development of tazemetostat outside of our ongoing indications in the United States or other countries, will require that we submit an IND or international equivalent or that we submit supplemental materials to the FDA or international regulatory authorities and that we address this matter to the satisfaction of the FDA or international regulatory authorities within the context of patient risk-benefit and in view of the safety and efficacy data from our ongoing and completed clinical trials of tazemetostat. For instance, we are currently unable to conduct our phase 2 trial of tazemetostat in follicular lymphoma patients in the United States. If we are unable to adequately address this matter, we may be unable to conduct clinical trials of tazemetostat in patients with other cancers in the United States or in other countries, our trials may be limited to certain patient populations or our ability to conduct other trials in the United States or in other countries may be delayed.

Clinical testing is expensive, difficult to design and implement, can take many years to complete and is uncertain as to outcome. A failure of one or more clinical trials can occur at any stage of testing. The outcome of preclinical testing and early clinical trials may not be predictive of the success of later clinical trials, and interim results of a clinical trial do not necessarily predict final results. For example, the complete responses that were observed in two patients with MLL-r in the fourth dose cohort of the dose escalation portion of our phase 1 clinical trial of pinometostat were not achieved by any other patient treated with pinometostat in the phase 1 clinical trial. We voluntarily ceased patient enrollment into the phase 1 clinical trial in adult patients with MLL-r due to insufficient evidence of efficacy of pinometostat as a monotherapy in the third quarter of 2015. Moreover, preclinical and clinical data are often susceptible to varying interpretations and analyses, and many companies that have believed their product candidates performed satisfactorily in preclinical studies and clinical trials have nonetheless failed to obtain marketing approval of their products.

We may experience numerous unforeseen events during, or as a result of, clinical trials that could delay or prevent our ability to receive marketing approval or commercialize our product candidates, including:

regulators or institutional review boards may not authorize us or our investigators to commence a clinical trial or conduct a clinical trial at a prospective trial site;

we may experience delays in reaching, or fail to reach, agreement on acceptable clinical trial contracts or clinical trial protocols with prospective trial sites;

clinical trials of our product candidates may produce negative or inconclusive results, and we may decide, or regulators may require us, to conduct additional clinical trials or abandon product development programs;

preclinical testing may produce results based on which we may decide, or regulators may require us, to conduct additional preclinical studies before we proceed with certain clinical trials, limit the scope of our clinical trials, halt ongoing clinical trials or abandon product development programs;

the number of patients required for clinical trials of our product candidates may be larger than we anticipate, enrollment in these clinical trials may be slower than we anticipate or participants may drop out of these clinical trials at a higher rate than we anticipate;

our third party contractors may fail to comply with regulatory requirements or meet their contractual obligations to us in a timely manner, or at all;

we may have to suspend or terminate clinical trials of our product candidates for various reasons, including a finding that the participants are being exposed to unacceptable health risks;

regulators or institutional review boards may require that we or our investigators suspend or terminate clinical research for various reasons, including noncompliance with regulatory requirements or a finding that the participants are being exposed to unacceptable health risks;

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the cost of clinical trials of our product candidates may be greater than we anticipate;

the supply or quality of our product candidates or other materials necessary to conduct clinical trials of our product candidates may be insufficient or inadequate; and

our product candidates may have undesirable side effects or other unexpected characteristics, causing us or our investigators, regulators or institutional review boards to suspend or terminate the trials.

If we are required to conduct additional clinical trials or other testing of our product candidates beyond those that we currently contemplate, if we are unable to successfully complete clinical trials of our product candidates or other testing, if the results of these trials or tests are not positive or are only modestly positive or if there are safety concerns, we may:

be delayed in obtaining marketing approval for our product candidates;

not obtain marketing approval at all;

obtain approval for indications or patient populations that are not as broad as intended or desired;

obtain approval with labeling or a risk evaluation mitigation strategy that includes significant use or distribution restrictions or safety warnings;

be subject to additional post-marketing testing requirements; or

have the product removed from the market after obtaining marketing approval.

Our product development costs may also increase if we experience delays in clinical testing or in obtaining marketing approvals. We do not know whether any of our preclinical studies or clinical trials will begin as planned, will need to be restructured or will be completed on schedule, or at all. Significant preclinical or clinical trial delays also could shorten any periods during which we may have the exclusive right to commercialize our product candidates or allow our competitors to bring products to market before we do and impair our ability to successfully commercialize our product candidates and may harm our business and results of operations.

***If we experience delays or difficulties in the enrollment of patients in clinical trials, our receipt of necessary regulatory approvals could be delayed or prevented.***

We may not be able to initiate or continue clinical trials for our product candidates if we are unable to locate and enroll a sufficient number of eligible patients to participate in these trials as required by the FDA or similar regulatory authorities outside of the United States. In particular, because certain of our products may be focused on specific patient populations, our ability to enroll eligible patients may be limited or may result in slower enrollment than we anticipate. In addition, some of our competitors have ongoing clinical trials for product candidates that may treat the

broader patient populations within which our product candidates are being developed for the treatment of a subset of identifiable cancer patients, and patients who would otherwise be eligible for our clinical trials may instead enroll in clinical trials of our competitors' product candidates. For instance, our ongoing clinical trials of tazemetostat in adult and pediatric patients with INI1-negative tumors, certain SMARCA4-negative tumors or synovial sarcoma are targeting rare patient populations. As such, certain arms of these trials may be slow to enroll. In addition, our phase 2 clinical trial of tazemetostat in patients with NHL has two arms targeting patients with EZH2 mutations in their tumors, one in germinal center B-cell, or GCB, DLBCL and one in follicular lymphoma. We believe that patients with these mutations represent between 15% and 25% of the total GCB DLBCL and follicular lymphoma population in the United States and other major reimbursable markets. As such, these arms of the NHL phase 2 study have been, and are likely to continue to be, slower to enroll than the other three arms of the phase 2 NHL clinical trial.

Patient enrollment is affected by other factors including:

the severity of the disease under investigation;

the eligibility criteria for the trial in question;

the perceived risks and benefits of the product candidate under trial;

the efforts to facilitate timely enrollment in clinical trials;



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the patient referral practices of physicians;

the ability to monitor patients adequately during and after treatment;

the proximity and availability of clinical trial sites for prospective patients; and

the ability to identify specific patient population for genetically defined study cohort(s).

Our inability to enroll a sufficient number of patients for our clinical trials would result in significant delays and could require us to abandon one or more clinical trials altogether. Enrollment delays in our clinical trials may result in increased development costs for our product candidates, which may cause the value of our company to decline and limit our ability to obtain additional financing.

***If serious adverse or unacceptable side effects are identified during the development of our product candidates, we may need to abandon or limit our development of some of our product candidates.***

If our product candidates are associated with undesirable side effects in clinical trials or have characteristics that are unexpected in clinical trials or preclinical testing, we may need to abandon their development or limit development to more narrow uses or subpopulations in which the undesirable side effects or other characteristics are less prevalent, less severe or more acceptable from a risk-benefit perspective. In pharmaceutical development, many compounds that initially show promise in early-stage testing for treating cancer are later found to cause side effects that prevent further development of the compound.

***We may expend our limited resources to pursue a particular product candidate or indication and fail to capitalize on product candidates or indications that may be more profitable or for which there is a greater likelihood of success.***

Because we have limited financial and managerial resources, we focus on research programs and product candidates that we identify for specific indications. As a result, we may forego or delay pursuit of opportunities with other product candidates or for other indications that later prove to have greater commercial potential. Our resource allocation decisions may cause us to fail to capitalize on viable commercial products or profitable market opportunities. Our spending on current and future research and development programs and product candidates for specific indications may not yield any commercially viable products. If we do not accurately evaluate the commercial potential or target market for a particular product candidate, we may relinquish valuable rights to that product candidate through collaboration, licensing or other royalty arrangements in cases in which it would have been more advantageous for us to retain sole development and commercialization rights to such product candidate.

***If we are unable to successfully develop companion diagnostics for our therapeutic product candidates when needed, or experience significant delays in doing so, we may not achieve marketing approval or realize the full commercial potential of our therapeutic product candidates.***

We may develop companion diagnostics for our therapeutic product candidates to identify patients for our clinical trials who have the specific cancers that we are seeking to treat as appropriate and when existing, available technology may not be sufficient to identify those patients. We do not have experience or capabilities in developing or commercializing diagnostics and plan to rely in large part on third parties to perform these functions. For example, we have entered into an agreement with Roche to develop and commercialize a companion diagnostic for use with

tazemetostat for NHL patients with EZH2 point mutations. Companion diagnostics are subject to regulation by the FDA and similar regulatory authorities outside of the United States as medical devices and require separate regulatory approval prior to commercialization. If any third parties that we engage to assist us, are unable to successfully develop companion diagnostics that are needed for our therapeutic product candidates, or experience delays in doing so:

the development of our therapeutic product candidates may be adversely affected if we are unable to appropriately select patients for enrollment in our clinical trials;

our therapeutic product candidates may not receive marketing approval if their safe and effective use depends on a companion diagnostic; and

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we may not realize the full commercial potential of any therapeutic product candidates that receive marketing approval if, among other reasons, we are unable to appropriately identify patients with the specific genetic alterations targeted by our therapeutic product candidates.

If any of these events were to occur, our business would be harmed, possibly materially.

**Risks Related to Our Financial Position and Need For Additional Capital**

*We have incurred significant losses since our inception. We expect to incur losses over the next several years and may never achieve or maintain profitability.*

Since inception, we have incurred significant operating losses. Our net loss was \$50.9 million for the six months ended June 30, 2016. As of June 30, 2016, we had an accumulated deficit of \$294.3 million. To date, we have financed our operations primarily through our collaborations, our public offerings, and private placements of our preferred stock. All of our revenue to date has been collaboration revenue. We have devoted substantially all of our financial resources and efforts to research and development, including clinical and preclinical studies. We are still in the early to middle stages of development of our product candidates, and we have not completed development of any drug candidates. We expect to continue to incur significant expenses and operating losses over the next several years. Our net losses may fluctuate significantly from quarter to quarter and year to year. We anticipate that our expenses will continue to increase over the next several years as we:

continue our phase 2 clinical trial of tazemetostat for the treatment of patients with NHL, our phase 2 clinical trial of tazemetostat for the treatment of adult patients with certain genetically-defined solid tumors and our phase 1 clinical trial of tazemetostat for the treatment of pediatric patients with certain genetically-defined solid tumors;

initiate our planned phase 2 clinical trial of tazemetostat in relapsed or refractory patients with mesothelioma characterized by BAP1 loss-of-function;

initiate our planned clinical trials of tazemetostat in combination with R-CHOP in front line elderly patients with DLBCL and in combination with Genentech's anti-PD-L1 cancer immunotherapy, Tecentriq, in patients with relapsed or refractory DLBCL;

continue our phase 1 clinical trial of tazemetostat for the treatment of patients with relapsed or refractory NHL or advanced solid tumors;

initiate a planned rollover study of tazemetostat in certain patients that have completed prior clinical trial protocols;

pay any milestone payments provided for and achieved under the amended and restated collaboration and license agreement with Eisai;

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conduct research and development for Celgene under our amended and restated collaboration and license agreement;

continue the research and development of our other product candidates;

seek to discover and develop additional product candidates;

seek regulatory approvals for any product candidates that successfully complete clinical trials;

ultimately establish a sales, marketing and distribution infrastructure and scale up external manufacturing capabilities to commercialize any products for which we may obtain regulatory approval;

maintain, expand and protect our intellectual property portfolio;

hire additional clinical, quality control and scientific personnel; and

add operational, financial and management information systems and personnel, including personnel to support our product development and planned future commercialization efforts.

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To become and remain profitable, we must succeed in developing, and eventually commercializing, a product or products that generate significant revenue. The ability to achieve this success will require us to be effective in a range of challenging activities, including completing preclinical testing and clinical trials of our product candidates, discovering additional product candidates, obtaining regulatory approval for these product candidates and manufacturing, marketing and selling any products for which we may obtain regulatory approval. We are only in the preliminary stages of most of these activities. We may never succeed in these activities and, even if we do, may never generate revenues that are significant enough to achieve profitability. Because of the numerous risks and uncertainties associated with pharmaceutical product development, we are unable to accurately predict the timing or amount of increased expenses or when, or if, we will be able to achieve profitability. If we are required by the FDA, the European Medicines Agency, or EMA, or other regulatory authorities to perform studies in addition to those currently expected, or if there are any delays in completing our clinical trials or the development of any of our product candidates, our expenses could increase.

Even if we do achieve profitability, we may not be able to sustain or increase profitability on a quarterly or annual basis. Our failure to become and remain profitable would depress the value of our company and could impair our ability to raise capital, expand our business, maintain our research and development efforts, diversify our product offerings or even continue our operations. A decline in the value of our company could cause our stockholders to lose all or part of their investment in our company.

***We will need substantial additional funding. If we are unable to raise capital when needed, we could be forced to delay, reduce or eliminate our product development programs or commercialization efforts.***

We expect our expenses to increase in connection with our ongoing activities, particularly since we have assumed responsibility for the funding of the EZH2 program, including our ongoing phase 2 clinical trial of tazemetostat for the treatment of patients with NHL, our ongoing phase 2 clinical trial of tazemetostat for the treatment of adult patients with certain genetically-defined solid tumors and our ongoing phase 1 clinical trial of tazemetostat for the treatment of pediatric patients with certain genetically-defined solid tumors; initiate our phase 2 study of tazemetostat in relapsed or refractory patients with mesothelioma characterized by BAP1 loss-of-function; initiate our combination clinical trials of tazemetostat in combination with R-CHOP in front line elderly patients with DLBCL and in combination with Tecentriq in patients with relapsed or refractory DLBCL; continue our phase 1 clinical trial of tazemetostat for the treatment of patients with relapsed or refractory NHL or advanced solid tumors and report on our phase 1 clinical trial of pinometostat in pediatric patients with MLL-r; pay any milestone payments provided for and achieved under the amended and restated collaboration and license agreement with Eisai; continue research for Celgene under our amended and restated collaboration and license agreement; and continue research and development and initiate additional clinical trials of, and seek regulatory approval for, any future product candidates. In addition, if we obtain regulatory approval for any of our product candidates, we expect to incur significant commercialization expenses related to product manufacturing, marketing, sales and distribution. Accordingly, we will need to obtain substantial additional funding in connection with our continuing operations. If we are unable to raise capital when needed or on acceptable terms, we could be forced to delay, reduce or eliminate our research and development programs or any future commercialization efforts.

Based on our research and development plans and our timing expectations related to the progress of our programs, we expect that our existing cash, cash equivalents and marketable securities as of June 30, 2016, will be sufficient to fund our planned operating expenses and capital expenditure requirements into at least the second quarter of 2018. We have based these expectations on assumptions that may prove to be wrong, and we could use our capital resources sooner than we expect. Our future capital requirements will depend on many factors, including:

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our remaining collaboration agreements remaining in effect and our ability to obtain global development co-funding and achieve milestones under these agreements;

the progress and results of our ongoing and planned clinical trials;

the number and development requirements of additional indications for tazemetostat, pinometostat and other product candidates that we may pursue, including the scope, progress, results and costs of preclinical development, laboratory testing and clinical trials for such product candidates;

our ongoing research for Celgene under our amended and restated collaboration and license agreement;

the costs, timing and outcome of regulatory review of our product candidates;

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milestones, option exercise fees, license fees, and other collaboration-based revenues, if any;

the costs and timing of future commercialization activities, including product manufacturing, marketing, sales and distribution for any of our product candidates for which we receive marketing approval;

the revenue, if any, received from commercial sales of our product candidates for which we receive marketing approval;

the costs and timing of preparing, filing and prosecuting patent applications, maintaining and enforcing our intellectual property rights and defending any intellectual property-related claims; and

the extent to which we acquire or in-license other products and technologies.

Identifying potential product candidates and conducting preclinical testing and clinical trials is a time-consuming, expensive and uncertain process that takes years to complete, and we may never generate the necessary data or results required to obtain regulatory approval and achieve product sales. In addition, our product candidates, if approved, may not achieve commercial success. Our commercial revenues, if any, will be derived from sales of products that we do not expect to be commercially available for many years, if at all. Accordingly, we will need to continue to rely on additional financing to achieve our business objectives. Adequate additional financing may not be available to us on acceptable terms, or at all. In addition, we may seek additional capital due to favorable market conditions or strategic considerations, even if we believe we have sufficient funds for our current or future operating plans.

***Raising additional capital may cause dilution to our stockholders, restrict our operations or require us to relinquish rights to our technologies or product candidates.***

Until such time, if ever, as we can generate substantial product revenues, we expect to finance our cash needs through a combination of equity offerings, debt financings and license and development agreements with collaboration partners. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the ownership interest of our existing stockholders will be diluted and the terms of these securities may include liquidation or other preferences that adversely affect the rights of our common stockholders. Debt financing and preferred equity financing, if available, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, making capital expenditures or declaring dividends.

If we raise additional funds through collaborations, strategic alliances or marketing, distribution or licensing arrangements with third parties, we may have to relinquish valuable rights to our technologies, future revenue streams, research programs or product candidates or grant licenses on terms that may not be favorable to us. If we are unable to raise additional funds through equity or debt financings when needed, we may be required to delay, limit, reduce or terminate our product development or future commercialization efforts or grant rights to develop and market product candidates that we would otherwise prefer to develop and market ourselves.

***Our limited operating history may make it difficult to evaluate the success of our business to date and to assess our future viability.***

We commenced active operations in early 2008, and our operations to date have been limited to organizing and staffing our company, business planning, raising capital, developing our technology, identifying potential product

candidates, undertaking preclinical studies and, beginning in 2012, conducting clinical trials. All but two of our product candidates are still in preclinical development. We are conducting a phase 2 clinical trial of tazemetostat for the treatment of patients with NHL, a phase 2 clinical trial of tazemetostat for the treatment of adult patients with INI1-negative tumors, certain SMARCA4-negative tumors or synovial sarcoma, a phase 1 clinical trial of tazemetostat for the treatment of pediatric patients with INI1-negative tumors, certain SMARCA4-negative tumors or synovial sarcoma, a phase 1 clinical trial of tazemetostat for the treatment of patients with NHL and solid tumors, a phase 2 clinical trial of tazemetostat in relapsed or refractory adult patients with mesothelioma characterized by BAP1 loss-of-function, and a phase 1 clinical trial of pinometostat in pediatric patients with MLL-r, for which enrollment is complete. We have not yet demonstrated our ability to successfully complete any clinical trials, obtain regulatory approvals, manufacture a commercial scale product, or arrange for a third party to do so on our behalf, or conduct sales and marketing activities necessary for successful product commercialization. Consequently, any predictions about our future success or viability may not be as accurate as they could be if we had a longer operating history.



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In addition, we may encounter unforeseen expenses, difficulties, complications, delays and other known and unknown factors. We will need to transition at some point from a company with a research and development focus to a company capable of supporting commercial activities. We may not be successful in such a transition.

We expect our financial condition and operating results to continue to fluctuate significantly from quarter-to-quarter and year-to-year due to a variety of factors, many of which are beyond our control. Accordingly, the results of any quarterly or annual periods should not be relied upon as indications of future operating performance.

### **Risks Related to the Commercialization of Our Product Candidates**

*Even if any of our product candidates receives marketing approval, it may fail to achieve the degree of market acceptance by physicians, patients, third party payors and others in the medical community necessary for commercial success.*

If any of our product candidates receives marketing approval, it may nonetheless fail to gain sufficient market acceptance by physicians, patients, third party payors and others in the medical community. If our product candidates do not achieve an adequate level of acceptance, we may not generate significant product revenues and we may not become profitable. The degree of market acceptance of our product candidates, if approved for commercial sale, will depend on a number of factors, including:

the efficacy and potential advantages compared to alternative treatments;

our ability to offer our products for sale at competitive prices;

the convenience and ease of administration compared to alternative treatments;

the willingness of the patient population to try new therapies and of physicians to prescribe these therapies;

the strength of marketing and distribution support;

the availability of third party coverage and adequate reimbursement;

the prevalence and severity of any side effects; and

any restrictions on the use of our products together with other medications.

*If we are unable to establish sales, marketing and distribution capabilities, we may not be successful in commercializing our product candidates if and when they are approved.*

We do not have a sales or marketing infrastructure and have no experience in the sale, marketing or distribution of pharmaceutical products. To achieve commercial success for any product for which we have obtained marketing approval, we will need to establish a sales and marketing organization.

In the future, we expect to build a focused sales and marketing infrastructure to market some of our product candidates in the United States, and potentially in international markets, if and when they are approved. There are risks involved with establishing our own sales, marketing and distribution capabilities. For example, recruiting and training a sales force is expensive and time consuming and could delay any product launch. If the commercial launch of a product candidate for which we recruit a sales force and establish marketing capabilities is delayed or does not occur for any reason, we would have prematurely or unnecessarily incurred these commercialization expenses. These efforts may be costly, and our investment would be lost if we cannot retain or reposition our sales and marketing personnel.

Factors that may inhibit our efforts to commercialize our products on our own include:

our inability to recruit, train and retain adequate numbers of effective sales and marketing personnel;

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the inability of sales personnel to obtain access to physicians or persuade adequate numbers of physicians to prescribe any future products;

the lack of complementary products to be offered by sales personnel, which may put us at a competitive disadvantage relative to companies with more extensive product lines; and

unforeseen costs and expenses associated with creating an independent sales and marketing organization. If we are unable to establish our own sales, marketing and distribution capabilities and enter into arrangements with third parties to perform these services, our product revenues and our profitability, if any, are likely to be lower than if we were to market, sell and distribute any products that we develop ourselves. In addition, we may not be successful in entering into arrangements with third parties to sell, market and distribute our product candidates or may be unable to do so on terms that are acceptable to us. We likely will have little control over such third parties, and any of them may fail to devote the necessary resources and attention to sell and market our products effectively. If we do not establish sales, marketing and distribution capabilities successfully, either on our own or in collaboration with third parties, we will not be successful in commercializing our product candidates.

***We face substantial competition, which may result in others discovering, developing or commercializing products before or more successfully than we do.***

The development and commercialization of new drug products is highly competitive. We face competition with respect to our current product candidates, and will likely face competition with respect to any product candidates that we may seek to develop or commercialize in the future, from major pharmaceutical companies, specialty pharmaceutical companies and biotechnology companies worldwide. There are a number of large pharmaceutical and biotechnology companies that currently market and sell products or are pursuing the development of products for the treatment of many of the disease indications for which we are developing our product candidates. Some of these competitive products and therapies are based on scientific approaches that are the same as or similar to our approach, and others are based on entirely different approaches. Potential competitors also include academic institutions, government agencies and other public and private research organizations that conduct research, seek patent protection and establish collaborative arrangements for research, development, manufacturing and commercialization.

Specifically, there are a large number of companies developing or marketing treatments for cancer, including many major pharmaceutical and biotechnology companies. Companies that are developing new epigenetic treatments for cancer that target HMTs include GSK, Novartis AG, Pfizer, Inc., Merck & Co., Inc., Daiichi Sankyo Company Limited, Takeda Pharmaceutical Company Limited, AbbVie Inc., Bayer Schering Pharma AG and Constellation Pharmaceuticals. In addition, many companies are developing cancer therapeutics that work by targeting epigenetic mechanisms other than HMTs, and some including Celgene and Eisai, are now marketing cancer treatments that work by targeting epigenetic mechanisms other than HMTs.

Our commercial opportunity could be reduced or eliminated if our competitors develop and commercialize products that are safer, more effective, have fewer or less severe side effects, are more convenient or are less expensive than any products that we may develop. Our competitors also may obtain FDA or other regulatory approval for their products more rapidly than we may obtain approval for ours, which could result in our competitors establishing a strong market position before we are able to enter the market. In addition, our ability to compete may be affected in many cases by insurers or other third party payors seeking to encourage the use of generic products. Generic products are currently on the market for many of the indications that we are pursuing, and additional products are expected to become available on a generic basis over the coming years. If our product candidates achieve marketing approval, we

expect that they will be priced at a significant premium over competitive generic products.

Many of the companies against which we are competing or against which we may compete in the future have significantly greater financial resources and expertise in research and development, manufacturing, preclinical testing, conducting clinical trials, obtaining regulatory approvals and marketing approved products than we do.

Mergers and acquisitions in the pharmaceutical and biotechnology industries may result in even more resources being concentrated among a smaller number of our competitors. Smaller and other early-stage companies may also prove to be significant competitors, particularly through collaborative arrangements with large and established

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companies. These third parties compete with us in recruiting and retaining qualified scientific and management personnel, establishing clinical trial sites and patient registration for clinical trials, as well as in acquiring technologies complementary to, or necessary for, our programs.

***Even if we are able to commercialize any product candidates, the products may become subject to unfavorable pricing regulations, third party reimbursement practices or healthcare reform initiatives, which could harm our business.***

The regulations that govern marketing approvals, pricing, coverage and reimbursement for new drug products vary widely from country to country. Current and future legislation may significantly change the approval requirements in ways that could involve additional costs and cause delays in obtaining approvals. Some countries require approval of the sale price of a drug before it can be marketed. In many countries, the pricing review period begins after marketing or product licensing approval is granted. In some foreign markets, prescription pharmaceutical pricing remains subject to continuing governmental control even after initial approval is granted. As a result, we might obtain marketing approval for a product in a particular country, but then be subject to price regulations that delay our commercial launch of the product, possibly for lengthy time periods, and negatively impact the revenues we are able to generate from the sale of the product in that country. Adverse pricing limitations may hinder our ability to recoup our investment in one or more product candidates, even if our product candidates obtain marketing approval.

Our ability to commercialize any product candidates successfully also will depend in part on the extent to which coverage and adequate reimbursement for these products and related treatments will be available from government health administration authorities, private health insurers and other organizations. Government authorities and third party payors, such as private health insurers and health maintenance organizations, decide which medications they will pay for and establish reimbursement levels. A primary trend in the U.S. healthcare industry and elsewhere is cost containment. Government authorities and third party payors have attempted to control costs by limiting coverage and the amount of reimbursement for particular medications. Increasingly, third party payors are requiring that drug companies provide them with predetermined discounts from list prices and are challenging the prices charged for medical products. Coverage and reimbursement may not be available for any product that we commercialize and, even if these are available, the level of reimbursement may not be satisfactory. Reimbursement may affect the demand for, or the price of, any product candidate for which we obtain marketing approval. Obtaining and maintaining adequate reimbursement for our products may be difficult. We may be required to conduct expensive pharmacoeconomic studies to justify coverage and reimbursement or the level of reimbursement relative to other therapies. If coverage and adequate reimbursement are not available or reimbursement is available only to limited levels, we may not be able to successfully commercialize any product candidate for which we obtain marketing approval.

There may be significant delays in obtaining reimbursement for newly approved drugs, and coverage may be more limited than the purposes for which the drug is approved by the FDA or similar regulatory authorities outside of the United States. Moreover, eligibility for reimbursement does not imply that a drug will be paid for in all cases or at a rate that covers our costs, including research, development, manufacture, sale and distribution. Interim reimbursement levels for new drugs, if applicable, may also not be sufficient to cover our costs and may not be made permanent. Reimbursement rates may vary according to the use of the drug and the clinical setting in which it is used, may be based on reimbursement levels already set for lower cost drugs and may be incorporated into existing payments for other services. Net prices for drugs may be reduced by mandatory discounts or rebates required by government healthcare programs or private payors and by any future relaxation of laws that presently restrict imports of drugs from countries where they may be sold at lower prices than in the United States. Third party payors often rely upon Medicare coverage policy and payment limitations in setting their own reimbursement policies. Our inability to promptly obtain coverage and adequate reimbursement rates from both government-funded and private payors for any approved products that we develop could have a material adverse effect on our operating results, our ability to raise

capital needed to commercialize products and our overall financial condition.

***Product liability lawsuits against us could cause us to incur substantial liabilities and to limit commercialization of any products that we may develop.***

We face an inherent risk of product liability exposure related to the testing of our product candidates in human clinical trials and will face an even greater risk if we commercially sell any products that we may develop. If we

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cannot successfully defend ourselves against claims that our product candidates or products caused injuries, we will incur substantial liabilities. Regardless of merit or eventual outcome, liability claims may result in:

decreased demand for any product candidates or products that we may develop;

injury to our reputation and significant negative media attention;

withdrawal of clinical trial participants;

significant costs to defend any related litigation;

substantial monetary awards to trial participants or patients;

loss of revenue;

reduced resources of our management to pursue our business strategy; and

the inability to commercialize any products that we may develop.

We currently hold \$20.0 million in product liability insurance coverage in the aggregate, with a per incident limit of \$20.0 million, which may not be adequate to cover all liabilities that we may incur. We may need to increase our insurance coverage as we expand our clinical trials or if we commence commercialization of our product candidates. Insurance coverage is increasingly expensive. We may not be able to maintain insurance coverage at a reasonable cost or in an amount adequate to satisfy any liability that may arise.

## **Risks Related to Our Dependence on Third Parties**

*Our existing therapeutic collaborations are important to our business, and future collaborations may also be important to us. If we are unable to maintain any of these collaborations, or if these collaborations are not successful, our business could be adversely affected.*

We have limited capabilities for drug development and do not yet have any capability for sales, marketing or distribution. Accordingly, we have entered into therapeutic collaborations with other companies that we believe can provide such capabilities, including our collaboration and license agreements with Celgene and GSK. With our reacquisition of tazemetostat rights under our amended and restated collaboration and license agreement with Eisai, we no longer have access to such capabilities for tazemetostat except with Eisai in Japan. Our collaborations have provided us with important funding for our development programs and product platform and we expect to receive additional funding under these collaborations in the future. Our existing therapeutic collaborations, and any future collaborations we enter into, may pose a number of risks, including the following:

collaborators have significant discretion in determining the efforts and resources that they will apply to these collaborations;

collaborators may not have the ability or the development capabilities to perform their obligations as expected;

collaborators may not pursue commercialization of any product candidates that achieve regulatory approval or may elect not to continue or renew development or commercialization programs based on clinical trial results, changes in the collaborators' strategic focus or available funding, or external factors, such as an acquisition, that may divert resources or create competing priorities;

collaborators may delay clinical trials, provide insufficient funding for a clinical trial program, stop a clinical trial or abandon a product candidate, repeat or conduct new clinical trials or require a new formulation of a product candidate for clinical testing;

collaborators could independently develop, or develop with third parties, products that compete directly or indirectly with our products and product candidates if the collaborators believe that the competitive products are more likely to be successfully developed or can be commercialized under terms that are more economically attractive than ours;



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product candidates discovered in collaboration with us may be viewed by our collaborators as competitive with their own product candidates or products, which may cause collaborators to cease to devote resources to the commercialization of our product candidates;

a collaborator may fail to comply with applicable regulatory requirements regarding the development, manufacture, distribution or marketing of a product candidate or product;

a collaborator with marketing and distribution rights to one or more of our product candidates that achieve regulatory approval may not commit sufficient resources to the marketing and distribution of such product or products;

disagreements with collaborators, including disagreements over proprietary rights, contract interpretation or the preferred course of development, might cause delays or terminations of the research, development or commercialization of product candidates, might lead to additional responsibilities for us with respect to product candidates, or might result in litigation or arbitration, any of which would be time-consuming and expensive;

collaborators may not properly maintain or defend our intellectual property rights or may use our proprietary information in such a way as to invite litigation that could jeopardize or invalidate our intellectual property or proprietary information or expose us to potential litigation;

collaborators may infringe the intellectual property rights of third parties, which may expose us to litigation and potential liability; and

collaborations may be terminated for the convenience of the collaborator, and, if terminated, we could be required to raise additional capital to pursue further development or commercialization of the applicable product candidates.

If our therapeutic collaborations do not result in the successful development and commercialization of products or if one of our collaborators terminates its agreement with us, we may not receive any future research funding or milestone or royalty payments under the collaboration. If we do not receive the funding we expect under these agreements, our development of our product platform and product candidates could be delayed and we may need additional resources to develop product candidates and our product platform. All of the risks relating to product development, regulatory approval and commercialization described in this Quarterly Report on Form 10-Q also apply to the activities of our therapeutic collaborators.

Our existing therapeutic collaborations contain restrictions on our engaging in activities that are the subject of the collaboration with third parties for specified periods of time. For example, under our collaboration agreement with Celgene, subject to specified exceptions, we may not, during the option period, research, develop or commercialize inhibitors directed to DOT1L and the three option targets covered by the agreement outside of the collaboration. These restrictions may have the effect of preventing us from undertaking development and other efforts that may appear to be attractive to us.

Additionally, subject to its contractual obligations to us, if a collaborator of ours is involved in a business combination, the collaborator might deemphasize or terminate the development or commercialization of any product candidate licensed to it by us. If one of our collaborators terminates its agreement with us, we may find it more difficult to attract new collaborators and our perception in the business and financial communities could be adversely affected.

For some of our product candidates or for some HMT targets, we may in the future determine to collaborate with pharmaceutical and biotechnology companies for development and potential commercialization of therapeutic products. We face significant competition in seeking appropriate collaborators. Our ability to reach a definitive agreement for a collaboration will depend, among other things, upon our assessment of the collaborator's resources and expertise, the terms and conditions of the proposed collaboration and the proposed collaborator's evaluation of a number of factors. If we are unable to reach agreements with suitable collaborators on a timely basis, on acceptable terms, or at all, we may have to curtail the development of a product candidate, reduce or delay its development program or one or more of our other development programs, delay its potential commercialization or reduce the scope of any sales or marketing activities, or increase our expenditures and undertake development or

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commercialization activities at our own expense. If we elect to fund and undertake development or commercialization activities on our own, we may need to obtain additional expertise and additional capital, which may not be available to us on acceptable terms or at all. If we fail to enter into collaborations and do not have sufficient funds or expertise to undertake the necessary development and commercialization activities, we may not be able to further develop our product candidates or bring them to market or continue to develop our product platform and our business may be materially and adversely affected.

***Failure of our third party collaborators to successfully commercialize companion diagnostics developed for use with our therapeutic product candidates could harm our ability to commercialize these product candidates.***

We do not plan to develop companion diagnostics internally and, as a result, we are dependent on the efforts of our third party collaborators to successfully commercialize companion diagnostics when existing, available technology may not be sufficient to identify patients for treatment with our therapeutic product candidates. Our collaborators:

may not perform their obligations as expected;

may encounter production difficulties that could constrain the supply of the companion diagnostics;

may have difficulties gaining acceptance of the use of the companion diagnostics in the clinical community;

may not pursue commercialization of any therapeutic product candidates that achieve regulatory approval;

may elect not to continue or renew commercialization programs based on changes in the collaborators strategic focus or available funding, or external factors such as an acquisition, that divert resources or create competing priorities;

may not commit sufficient resources to the marketing and distribution of such product or products; and

may terminate their relationship with us.

If companion diagnostics for use with our therapeutic product candidates fail to gain market acceptance, our ability to derive revenues from sales of our therapeutic product candidates could be harmed. If our collaborators fail to commercialize these companion diagnostics, we may not be able to enter into arrangements with another diagnostic company to obtain supplies of an alternative diagnostic test for use in connection with our therapeutic product candidates or do so on commercially reasonable terms, which could adversely affect and delay the development or commercialization of our therapeutic product candidates.

***We rely, and expect to continue to rely, on third parties to conduct our clinical trials, and those third parties may not perform satisfactorily, including failing to meet deadlines for the completion of such trials.***

We currently rely on third party clinical research organizations to conduct our ongoing clinical trials and plan to rely on third party clinical research organizations or third party research collaboratives to conduct our planned clinical trials. We do not plan to independently conduct clinical trials of any future product candidates. We expect to continue to rely on third parties, such as clinical research organizations, clinical data management organizations, medical institutions and clinical investigators, to conduct our clinical trials. These agreements might terminate for a variety of reasons, including a failure to perform by the third parties. If we need to enter into alternative arrangements, our product development activities might be delayed.

Our reliance on these third parties for research and development activities will reduce our control over these activities but will not relieve us of our responsibilities. For example, we will remain responsible for ensuring that each of our clinical trials is conducted in accordance with the general investigational plan and protocols for the trial. Moreover, the FDA requires us to comply with standards, commonly referred to as good clinical practices, or GCPs, for conducting, recording and reporting the results of clinical trials to assure that data and reported results are credible and accurate and that the rights, integrity and confidentiality of trial participants are protected. We also are required to register ongoing clinical trials and post the results of completed clinical trials on a government-sponsored database, ClinicalTrials.gov, within specified timeframes. Failure to do so can result in fines, adverse publicity and civil and criminal sanctions.

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Furthermore, these third parties may also have relationships with other entities, some of which may be our competitors. If these third parties do not successfully carry out their contractual duties, meet expected deadlines or conduct our clinical trials in accordance with regulatory requirements or our stated protocols, we will not be able to obtain, or may be delayed in obtaining, marketing approvals for our product candidates and will not be able to, or may be delayed in our efforts to, successfully commercialize our product candidates.

We also expect to rely on other third parties to store and distribute drug supplies for our clinical trials. Any performance failure on the part of our distributors could delay clinical development or marketing approval of our product candidates or commercialization of our products, producing additional losses and depriving us of potential product revenue.

***We contract with third parties for the manufacture of our product candidates for preclinical and clinical testing and expect to continue to do so for commercialization. This reliance on third parties increases the risk that we will not have sufficient quantities of our product candidates or products or such quantities at an acceptable cost or quality, which could delay, prevent or impair our development or commercialization efforts.***

We do not have any manufacturing facilities and rely, and expect to continue to rely, on third parties for the manufacture of our product candidates for preclinical and clinical testing, as well as for commercial manufacture if any of our product candidates receive marketing approval. This reliance on third parties increases the risk that we will not have sufficient quantities of our product candidates or products or such quantities at an acceptable cost or quality, which could delay, prevent or impair our development or commercialization efforts.

We also expect to rely on third party manufacturers or third party collaborators for the manufacture of commercial supply of any other product candidates for which our collaborators or we obtain marketing approval.

We may be unable to establish any agreements with third party manufacturers or to do so on acceptable terms. Even if we are able to establish agreements with third party manufacturers, reliance on third party manufacturers entails additional risks, including:

reliance on the third party for regulatory compliance and quality assurance;

the possible breach of the manufacturing agreement by the third party;

the possible misappropriation of our proprietary information, including our trade secrets and know-how; and

the possible termination or nonrenewal of the agreement by the third party at a time that is costly or inconvenient for us.

Third party manufacturers may not be able to comply with current good manufacturing practices, or cGMP, regulations or similar regulatory requirements outside of the United States. Our failure, or the failure of our third party manufacturers, to comply with applicable regulations could result in sanctions being imposed on us, including clinical holds, fines, injunctions, civil penalties, delays, suspension or withdrawal of approvals, license revocation, seizures or recalls of product candidates or products, operating restrictions and criminal prosecutions, any of which could significantly and adversely affect supplies of our products.

Our product candidates and any products that we may develop may compete with other product candidates and products for access to manufacturing facilities. There are a limited number of manufacturers that operate under cGMP regulations and that might be capable of manufacturing for us.

Any performance failure on the part of our existing or future manufacturers could delay clinical development or marketing approval. We do not currently have arrangements in place for redundant supply or a second source for bulk drug substance. If our current contract manufacturers cannot perform as agreed, we may be required to replace such manufacturers. Although we believe that there are several potential alternative manufacturers who could manufacture our product candidates, we may incur added costs and delays in identifying and qualifying any such replacement.

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Our current and anticipated future dependence upon others for the manufacture of our product candidates or products may adversely affect our future profit margins and our ability to commercialize any products that receive marketing approval on a timely and competitive basis.

### **Risks Related to Our Intellectual Property**

*If we are unable to obtain and maintain patent protection for our technology and products or if the scope of the patent protection obtained is not sufficiently broad, our competitors could develop and commercialize technology and products similar or identical to ours, and our ability to successfully commercialize our technology and products may be impaired.*

Our success depends in large part on our ability to obtain and maintain patent protection in the United States and other countries with respect to our proprietary technology and products. We seek to protect our proprietary position by filing patent applications in the United States and abroad related to our novel technologies and product candidates.

The patent prosecution process is expensive and time-consuming, and we may not be able to file and prosecute all necessary or desirable patent applications at a reasonable cost or in a timely manner. It is also possible that we will fail to identify patentable aspects of our research and development output before it is too late to obtain patent protection. Moreover, in some circumstances, we do not have the right to control the preparation, filing and prosecution of patent applications, or to maintain the patents, covering technology that we license from third parties. Therefore, these patents and applications may not be prosecuted and enforced in a manner consistent with the best interests of our business.

The patent position of biotechnology and pharmaceutical companies generally is highly uncertain, involves complex legal and factual questions and has in recent years been the subject of much litigation. In addition, the laws of foreign countries may not protect our rights to the same extent as the laws of the United States. For example, European patent law restricts the patentability of methods of treatment of the human body more than United States law does. Publications of discoveries in the scientific literature often lag behind the actual discoveries, and patent applications in the United States and other jurisdictions are typically not published until 18 months after filing, or in some cases at all. Therefore, we cannot know with certainty whether we were the first to make the inventions claimed in our owned or licensed patents or pending patent applications, or that we were the first to file for patent protection of such inventions. As a result, the issuance, scope, validity, enforceability and commercial value of our patent rights are highly uncertain. Our pending and future patent applications may not result in patents being issued which protect our technology or products, in whole or in part, or which effectively prevent others from commercializing competitive technologies and products. Changes in either the patent laws or interpretation of the patent laws in the United States and other countries may diminish the value of our patents or narrow the scope of our patent protection.

In the United States, the patent term of a patent that covers an FDA-approved drug may also be eligible for patent term extension, which permits patent term restoration 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 length of time the drug is under regulatory review. Patent 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 non-United States jurisdictions to extend the term of a patent that covers an approved drug. In the future, if and when our drug candidates receive FDA approval, we expect to apply for patent term extensions on patents covering those product candidates. We intend to seek patent term extensions for any of our issued patents in any jurisdiction where they are available, however there is no guarantee that the applicable authorities will agree with our assessment of whether such extensions should be granted, and even if granted, the

length of such extensions.

Recent patent reform legislation could increase the uncertainties and costs surrounding the prosecution of our patent applications and the enforcement or defense of our issued patents. On September 16, 2011, the Leahy-Smith America Invents Act, or the Leahy-Smith Act, was signed into law. The Leahy-Smith Act includes a number of significant changes to United States patent law. These changes include provisions that affect the way patent



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applications are prosecuted and may also affect patent litigation. The United States Patent Office recently developed new regulations and procedures to govern administration of the Leahy-Smith Act, and many of the substantive changes to patent law associated with the Leahy-Smith Act, and in particular, the first to file provisions, only became effective on March 16, 2013. Accordingly, it is not clear what, if any, impact the Leahy-Smith Act will have on the operation of our business. However, the Leahy-Smith Act and its implementation could increase the uncertainties and costs surrounding the prosecution of our patent applications and the enforcement or defense of our issued patents, all of which could have a material adverse effect on our business and financial condition.

Moreover, we may be subject to a third party preissuance submission of prior art to the U.S. Patent and Trademark Office, or become involved in opposition, derivation, reexamination, *inter partes* review, post-grant review or interference proceedings challenging our patent rights or the patent rights of others. An adverse determination in any such submission, proceeding or litigation could reduce the scope of, or invalidate, our patent rights, allow third parties to commercialize our technology or products and compete directly with us, without payment to us, or result in our inability to manufacture or commercialize products without infringing third party patent rights. In addition, if the breadth or strength of protection provided by our patents and patent applications is threatened, it could dissuade companies from collaborating with us to license, develop or commercialize current or future product candidates.

Even if our owned and licensed patent applications issue as patents, they may not issue in a form that will provide us with any meaningful protection, prevent competitors from competing with us or otherwise provide us with any competitive advantage.

Our competitors may be able to circumvent our owned or licensed patents by developing similar or alternative technologies or products in a non-infringing manner.

The issuance of a patent is not conclusive as to its inventorship, scope, validity or enforceability, and our owned and licensed patents may be challenged in the courts or patent offices in the United States and abroad. Such challenges may result in loss of exclusivity or freedom to operate or in patent claims being narrowed, invalidated or held unenforceable, in whole or in part, which could limit our ability to stop others from using or commercializing similar or identical technology and products, or limit the duration of the patent protection of our technology and products. Given the amount of time required for the development, testing and regulatory review of new product candidates, patents protecting such candidates might expire before or shortly after such candidates are commercialized. As a result, our owned and licensed patent portfolio may not provide us with sufficient rights to exclude others from commercializing products similar or identical to ours.

***We may become involved in lawsuits to protect or enforce our patents or other intellectual property, which could be expensive, time consuming and unsuccessful.***

Competitors may infringe our issued patents or other intellectual property. To counter infringement or unauthorized use, we may be required to file infringement claims, which can be expensive and time consuming. Any claims we assert against perceived infringers could provoke these parties to assert counterclaims against us alleging that we infringe their patents. In addition, in a patent infringement proceeding, a court may decide that a patent of ours is invalid or unenforceable, in whole or in part, construe the patent's claims narrowly or refuse to stop the other party from using the technology at issue on the grounds that our patents do not cover the technology in question. An adverse result in any litigation proceeding could put one or more of our patents at risk of being invalidated or interpreted narrowly.

***We may need to license certain intellectual property from third parties, and such licenses may not be available or may not be available on commercially reasonable terms.***

A third party may hold intellectual property, including patent rights, that are important or necessary to the development of our products. It may be necessary for us to use the patented or proprietary technology of third parties to commercialize our products, in which case we may be required to obtain a license from these third parties on commercially reasonable terms, or our business could be harmed, possibly materially.

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***Third parties may initiate legal proceedings alleging that we are infringing their intellectual property rights, the outcome of which would be uncertain and could have a material adverse effect on the success of our business.***

Our commercial success depends upon our ability, and the ability of our collaborators, to develop, manufacture, market and sell our product candidates and use our proprietary technologies without infringing the proprietary rights of third parties. There is considerable intellectual property litigation in the biotechnology and pharmaceutical industries. We may become party to, or threatened with, future adversarial proceedings or litigation regarding intellectual property rights with respect to our products and technology, including interference or derivation proceedings before the U.S. Patent and Trademark Office. Third parties may assert infringement claims against us based on existing patents or patents that may be granted in the future.

If we are found to infringe a third party's intellectual property rights, we could be required to obtain a license from such third party to continue developing and marketing our products and technology. However, we may not be able to obtain any required license on commercially reasonable terms or at all. Even if we were able to obtain a license, it could be non-exclusive, thereby giving our competitors access to the same technologies licensed to us. We could be forced, including by court order, to cease commercializing the infringing technology or product. In addition, we could be found liable for monetary damages, including treble damages and attorneys' fees if we are found to have willfully infringed a patent. A finding of infringement could prevent us from commercializing our product candidates or force us to cease some of our business operations, which could materially harm our business. Claims that we have misappropriated the confidential information or trade secrets of third parties could have a similar negative impact on our business.

***If we fail to comply with our obligations in our intellectual property licenses and funding arrangements with third parties, we could lose rights that are important to our business.***

We are party to license and research agreements that impose, and we may enter into additional licensing and funding arrangements with third parties that may impose, diligence, development and commercialization timelines, milestone payment, royalty, insurance and other obligations on us. Under our existing licensing and funding agreements, we are obligated to pay royalties on net product sales of product candidates or related technologies to the extent they are covered by the agreements. We also had diligence and development obligations under those agreements that we have satisfied. If we fail to comply with our obligations under current or future license and funding agreements, our counterparties may have the right to terminate these agreements, in which event we might not be able to develop, manufacture or market any product that is covered by these agreements or may face other penalties under the agreements. Such an occurrence could materially adversely affect the value of the product candidate being developed under any such agreement. Termination of these agreements or reduction or elimination of our rights under these agreements may result in our having to negotiate new or reinstated agreements with less favorable terms, or cause us to lose our rights under these agreements, including our rights to important intellectual property or technology.

***We may be subject to claims by third parties asserting that our employees or we have misappropriated their intellectual property, or claiming ownership of what we regard as our own intellectual property.***

Many of our employees were previously employed at universities or other biotechnology or pharmaceutical companies, including our competitors or potential competitors. Although we try to ensure that our employees do not use the proprietary information or know-how of others in their work for us, we may be subject to claims that these employees or we have used or disclosed intellectual property, including trade secrets or other proprietary information, of any such employee's former employer. Litigation may be necessary to defend against these claims.

In addition, while it is our policy to require our employees and contractors who may be involved in the development of intellectual property to execute agreements assigning such intellectual property to us, we may be unsuccessful in executing such an agreement with each party who in fact develops intellectual property that we regard as our own. Our and their assignment agreements may not be self-executing or may be breached, and we may be forced to bring claims against third parties, or defend claims they may bring against us, to determine the ownership of what we regard as our intellectual property.

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If we fail in prosecuting or defending any such claims, in addition to paying monetary damages, we may lose valuable intellectual property rights or personnel. Even if we are successful in prosecuting or defending against such claims, litigation could result in substantial costs and be a distraction to management.

***Intellectual property litigation could cause us to spend substantial resources and distract our personnel from their normal responsibilities.***

Even if resolved in our favor, litigation or other legal proceedings relating to intellectual property claims may cause us to incur significant expenses, and could distract our technical and management personnel from their normal responsibilities. In addition, there could be public announcements of the results of hearings, motions or other interim proceedings or developments and if securities analysts or investors perceive these results to be negative, it could have a substantial adverse effect on the price of our common stock. Such litigation or proceedings could substantially increase our operating losses and reduce the resources available for development activities or any future sales, marketing or distribution activities. We may not have sufficient financial or other resources to conduct such litigation or proceedings adequately. Some of our competitors may be able to sustain the costs of such litigation or proceedings more effectively than we can because of their greater financial resources. Uncertainties resulting from the initiation and continuation of patent litigation or other proceedings could compromise our ability to compete in the marketplace.

***If we are unable to protect the confidentiality of our trade secrets, our business and competitive position would be harmed.***

In addition to seeking patents for some of our technology and product candidates, we also rely on trade secrets, including unpatented know-how, technology and other proprietary information, to maintain our competitive position. We seek to protect these trade secrets, in part, by entering into non-disclosure and confidentiality agreements with parties who have access to them, such as our employees, corporate collaborators, outside scientific collaborators, contract manufacturers, consultants, advisors and other third parties. We also enter into confidentiality and invention or patent assignment agreements with our employees and consultants. Despite these efforts, any of these parties may breach the agreements and disclose our proprietary information, including our trade secrets, and we may not be able to obtain adequate remedies for such breaches. Enforcing a claim that a party illegally disclosed or misappropriated a trade secret is difficult, expensive and time-consuming, and the outcome is unpredictable. In addition, some courts inside and outside of the United States are less willing or unwilling to protect trade secrets. If any of our trade secrets were to be lawfully obtained or independently developed by a competitor, we would have no right to prevent them, or those to whom they communicate it, from using that technology or information to compete with us. If any of our trade secrets were to be disclosed to or independently developed by a competitor, our competitive position would be harmed.

**Risks Related to Regulatory Approval of Our Product Candidates and Other Legal Compliance Matters**

***Even if we complete the necessary preclinical studies and clinical trials, the marketing approval process is expensive, time-consuming and uncertain and may prevent us from obtaining approvals for the commercialization of some or all of our product candidates. If we are not able to obtain, or if there are delays in obtaining, required regulatory approvals, we will not be able to commercialize our product candidates, and our ability to generate revenue will be materially impaired.***

Our product candidates and the activities associated with their development and commercialization, including their design, testing, manufacture, safety, efficacy, recordkeeping, labeling, storage, approval, advertising, promotion, sale and distribution, export and import are subject to comprehensive regulation by the FDA and other regulatory agencies in the United States and by the EMA and similar regulatory authorities outside of the United States. Failure to obtain

marketing approval for a product candidate will prevent us from commercializing the product candidate. We have not submitted an application for or received marketing approval for any of our product candidates in the United States or in any other jurisdiction.

We have only limited experience in filing and supporting the applications necessary to gain marketing approvals and expect to rely on third party CROs to assist us in this process. Securing marketing approval requires the submission of extensive preclinical and clinical data and supporting information to regulatory authorities for each therapeutic

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indication to establish the product candidate's safety and efficacy. Securing marketing approval also requires the submission of information about the product manufacturing process to, and inspection of manufacturing facilities by, the regulatory authorities. Our product candidates may not be effective, may be only moderately effective or may prove to have undesirable or unintended side effects, toxicities or other characteristics that may preclude our obtaining marketing approval or prevent or limit commercial use. For example, we voluntarily ceased patient enrollment in our phase 1 clinical trial of pinometostat in adult patients with MLL-r due to insufficient evidence of efficacy with monotherapy treatment. New cancer drugs frequently are indicated only for patient populations that have not responded to an existing therapy or have relapsed.

The process of obtaining marketing approvals, both in the United States and abroad, is expensive, may take many years if additional clinical trials are required, if approval is obtained at all, and can vary substantially based upon a variety of factors, including the type, complexity and novelty of the product candidates involved. Changes in marketing approval policies during the development period, changes in or the enactment of additional statutes or regulations, or changes in regulatory review for each submitted product application, may cause delays in the approval or rejection of an application. Regulatory authorities have substantial discretion in the approval process and may refuse to accept any application or may decide that our data is insufficient for approval and require additional preclinical, clinical or other studies. In addition, varying interpretations of the data obtained from preclinical and clinical testing could delay, limit or prevent marketing approval of a product candidate. Any marketing approval we ultimately obtain may be limited or subject to restrictions or post-approval commitments that render the approved product not commercially viable.

If we experience delays in obtaining approval or if we fail to obtain approval of our product candidates, the commercial prospects for our product candidates may be harmed and our ability to generate revenues will be materially impaired.

***We may not be able to obtain orphan drug exclusivity for our product candidates and, even if we do, that exclusivity may not prevent the FDA or the EMA from approving other competing products.***

Regulatory authorities in some jurisdictions, including the United States and Europe, may designate drugs for relatively small patient populations as orphan drugs. Under the Orphan Drug Act, the FDA may designate a product as an orphan drug if it is a drug intended to treat a rare disease or condition, which is generally defined as a patient population of fewer than 200,000 individuals annually in the United States. We have obtained orphan drug designations for tazemetostat for the treatment of INI1-negative malignant rhabdoid tumors, or MRT as well as SMARCA4-negative MRT of ovary, or MRTO, in the United States and for pinometostat for the treatment of acute lymphoblastic leukemia and acute myeloid leukemia in the United States and Europe. We may not receive orphan drug designation for these product candidates for other indications, or for any other future clinical candidates we may develop.

Generally, if a product with an orphan drug designation subsequently receives the first marketing approval for the indication for which it has such designation, the product is entitled to a period of marketing exclusivity, which precludes the EMA or the FDA from approving another marketing application for the same drug for that time period. The applicable period is seven years in the United States and ten years in Europe. The exclusivity period in Europe can be reduced to six years if a drug no longer meets the criteria for orphan drug designation or if the drug is sufficiently profitable so that market exclusivity is no longer justified. Orphan drug exclusivity may be lost if the FDA or EMA determines that the request for designation was materially defective or if the manufacturer is unable to assure sufficient quantity of the drug to meet the needs of patients with the rare disease or condition.

Even if we obtain orphan drug exclusivity for a product, that exclusivity may not effectively protect the product from competition because different drugs can be approved for the same condition. In addition, even after an orphan drug is approved, the FDA can subsequently approve the same drug for the same condition if the FDA concludes that the later drug is clinically superior in that it is shown to be safer, more effective or makes a major contribution to patient care.



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***A fast track designation by the FDA may not actually lead to a faster development or regulatory review or approval process.***

We intend to seek fast track designation for one or more of our product candidates. If a drug is intended for the treatment of a serious or life-threatening condition and the drug demonstrates the potential to address unmet medical needs for this condition, the drug sponsor may apply for FDA fast track designation. The FDA has broad discretion whether or not to grant this designation, so even if we believe a particular product candidate is eligible for this designation, we cannot assure that the FDA would decide to grant it. Even if we do receive fast track designation, we may not experience a faster development process, review or approval compared to conventional FDA procedures. The FDA may withdraw fast track designation if it believes that the designation is no longer supported by data from our clinical development program.

***A breakthrough therapy designation by the FDA for our product candidates may not lead to a faster development or regulatory review or approval process, and it does not increase the likelihood that our product candidates will receive marketing approval.***

A breakthrough therapy is defined as a drug that is intended, alone or in combination with one or more other drugs, to treat a serious or life-threatening disease or condition, and preliminary clinical evidence indicates that the drug may demonstrate substantial improvement over existing therapies on one or more clinically significant endpoints, such as substantial treatment effects observed early in clinical development. For drugs and biologics that have been designated as breakthrough therapies, interaction and communication between the FDA and the sponsor of the trial can help to identify the most efficient path for clinical development while minimizing the number of patients placed in ineffective control regimens. Drugs designated as breakthrough therapies by the FDA are also eligible for accelerated approval.

Designation as a breakthrough therapy is within the discretion of the FDA. Accordingly, even if we believe one of our product candidates meets the criteria for designation as a breakthrough therapy, the FDA may disagree and instead determine not to make such designation. Even if we receive breakthrough therapy designation, the receipt of such designation for a product candidate may not result in a faster development process, review or approval compared to drugs considered for approval under conventional FDA procedures and does not assure ultimate approval by the FDA. In addition, even if one or more of our product candidates qualify as breakthrough therapies, the FDA may later decide that the products no longer meet the conditions for qualification or decide that the time period for FDA review or approval will not be shortened.

***Failure to obtain marketing approval in foreign jurisdictions would prevent our product candidates from being marketed in that jurisdiction.***

In order to market and sell our products in the European Union and many other foreign jurisdictions, we or our third party collaborators must obtain separate marketing approvals and comply with numerous and varying regulatory requirements. The approval procedure varies among countries and can involve additional testing. The time required to obtain approval may differ substantially from that required to obtain FDA approval. The regulatory approval process outside of the United States generally includes all of the risks associated with obtaining FDA approval. In addition, in many countries outside of the United States, a product must be approved for reimbursement before the product can be approved for sale in that country. We or our third party collaborators may not obtain approvals from regulatory authorities outside of the United States on a timely basis, if at all. Approval by the FDA does not ensure approval by regulatory authorities in other countries or jurisdictions, and approval by one regulatory authority outside of the United States does not ensure approval by regulatory authorities in other countries or jurisdictions or by the FDA. We may not be able to file for marketing approvals and may not receive necessary approvals to commercialize our products in any market.



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***If we are required by the FDA to obtain approval of a companion diagnostic in connection with approval of a candidate therapeutic product, and we do not obtain or there are delays in obtaining FDA approval of a diagnostic device, we will not be able to commercialize the product candidate and our ability to generate revenue will be materially impaired.***

In August 2014, the FDA issued final guidance clarifying the requirements that will apply to approval of therapeutic products and in vitro companion diagnostics. According to the guidance, if the FDA determines that a companion diagnostic device is essential to the safe and effective use of a novel therapeutic product or indication, the FDA generally will not approve the therapeutic product or new therapeutic product indication if the companion diagnostic is not also approved or cleared for that indication. Under the Federal Food, Drug, and Cosmetic Act, companion diagnostics are regulated as medical devices, and the FDA has generally required companion diagnostics intended to select the patients who will respond to cancer treatment to obtain Premarket Approval, or a PMA, for the diagnostic. The PMA process, including the gathering of clinical and preclinical data and the submission to and review by the FDA, involves a rigorous premarket review during which the applicant must prepare and provide the FDA with reasonable assurance of the device's safety and effectiveness and information about the device and its components regarding, among other things, device design, manufacturing and labeling. PMA approval is not guaranteed and may take considerable time, and the FDA may ultimately respond to a PMA submission with a not approvable determination based on deficiencies in the application and require additional clinical trial or other data that may be expensive and time-consuming to generate and that can substantially delay approval. As a result, if we are required by the FDA to obtain approval of a companion diagnostic for a candidate therapeutic product, and we do not obtain or there are delays in obtaining FDA approval of a diagnostic device, we may not be able to commercialize the product candidate on a timely basis or at all and our ability to generate revenue will be materially impaired.

***Any product candidate for which we obtain marketing approval could be subject to post-marketing restrictions or withdrawal from the market and we may be subject to substantial penalties if we fail to comply with regulatory requirements or if we experience unanticipated problems with our products, when and if any of them are approved.***

Any product candidate for which we obtain marketing approval, along with the manufacturing processes, post-approval clinical data, labeling, advertising and promotional activities for such product, will be subject to continual requirements of and review by the FDA and other regulatory authorities. These requirements include submissions of safety and other post-marketing information and reports, registration and listing requirements, cGMP requirements relating to manufacturing, quality control, quality assurance and corresponding maintenance of records and documents, requirements regarding the distribution of samples to physicians and recordkeeping. Even if marketing approval of a product candidate is granted, the approval may be subject to limitations on the indicated uses for which the product may be marketed or to the conditions of approval, including the requirement to implement a risk evaluation and mitigation strategy. New cancer drugs frequently are indicated only for patient populations that have not responded to an existing therapy or have relapsed. If any of our product candidates receives marketing approval, the accompanying label may limit the approved use of our drug in this way, which could limit sales of the product.

The FDA may also impose requirements for costly post-marketing studies or clinical trials and surveillance to monitor the safety or efficacy of the product. The FDA and other agencies, including the Department of Justice, or the DOJ, closely regulate and monitor the post-approval marketing and promotion of drugs to ensure they are marketed and distributed only for the approved indications and in accordance with the provisions of the approved labeling. The FDA and DOJ impose stringent restrictions on manufacturers' communications regarding off-label use, and if we do not market our products for their approved indications, we may be subject to enforcement action for off-label marketing. Violations of the Federal Food, Drug, and Cosmetic Act and other statutes, including the False Claims Act, relating to the promotion and advertising of prescription drugs may lead to investigations and enforcement actions alleging violations of federal and state health care fraud and abuse laws, as well as state consumer protection laws.

In addition, later discovery of previously unknown adverse events or other problems with our products, manufacturers or manufacturing processes, or failure to comply with regulatory requirements, may yield various results, including:

restrictions on such products, manufacturers or manufacturing processes;

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restrictions on the labeling or marketing of a product;

restrictions on product distribution or use;

requirements to conduct post-marketing studies or clinical trials;

warning letters or untitled letters;

withdrawal of the products from the market;

refusal to approve pending applications or supplements to approved applications that we submit;

recall of products;

fines, restitution or disgorgement of profits or revenues;

suspension or withdrawal of marketing approvals;

damage to relationships with any potential collaborators;

unfavorable press coverage and damage to our reputation;

refusal to permit the import or export of our products;

product seizure;

injunctions or the imposition of civil or criminal penalties; or

litigation involving patients using our products.

Non-compliance with European Union requirements regarding safety monitoring or pharmacovigilance, and with requirements related to the development of products for the pediatric population, can also result in significant financial penalties. Similarly, failure to comply with the European Union's requirements regarding the protection of personal information can also lead to significant penalties and sanctions.

***Our relationships with healthcare providers, physicians and third party payors will be subject to applicable anti-kickback, fraud and abuse and other healthcare laws and regulations, which, in the event of a violation, could expose us to criminal sanctions, civil penalties, contractual damages, reputational harm and diminished profits and future earnings.***

Healthcare providers, physicians and third party payors will play a primary role in the recommendation and prescription of any product candidates for which we obtain marketing approval. Our future arrangements with healthcare providers, physicians and third party payors may expose us to broadly applicable fraud and abuse and other healthcare laws and regulations that may constrain the business or financial arrangements and relationships through which we market, sell and distribute any products for which we obtain marketing approval. Restrictions under applicable federal and state healthcare laws and regulations include the following:

the federal Anti-Kickback Statute prohibits, among other things, persons from knowingly and willfully soliciting, offering, receiving or providing remuneration, directly or indirectly, in cash or in kind, to induce or reward, or in return for, either the referral of an individual for, or the purchase, order or recommendation or arranging of, any good or service, for which payment may be made under a federal healthcare program such as Medicare and Medicaid;

the federal False Claims Act imposes criminal and civil penalties, including through civil whistleblower or *qui tam* actions, against individuals or entities for, among other things, knowingly presenting, or causing to be presented, false or fraudulent claims for payment by a federal healthcare program or making a false statement or record material to payment of a false claim or avoiding, decreasing or concealing an obligation to pay money to the federal government, with potential liability including mandatory treble damages and significant per-claim penalties, currently set at \$5,500 to \$11,000 per false claim;

the federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, imposes criminal and civil liability for executing a scheme to defraud any healthcare benefit program or making false statements relating to healthcare matters;

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HIPAA, as amended by the Health Information Technology for Economic and Clinical Health Act and its implementing regulations, also imposes obligations, including mandatory contractual terms, with respect to safeguarding the privacy, security and transmission of individually identifiable health information;

the federal Physician Payments Sunshine Act requires applicable manufacturers of covered drugs to report payments and other transfers of value to physicians and teaching hospitals; and

analogous state and foreign laws and regulations, such as state anti-kickback and false claims laws and transparency statutes, may apply to sales or marketing arrangements and claims involving healthcare items or services reimbursed by non-governmental third party payors, including private insurers.

Some state laws require pharmaceutical companies to comply with the pharmaceutical industry's voluntary compliance guidelines and the relevant compliance guidance promulgated by the federal government and may require drug manufacturers to report information related to payments and other transfers of value to physicians and other healthcare providers or marketing expenditures. State and foreign laws also govern the privacy and security of health information in some circumstances, many of which differ from each other in significant ways and often are not preempted by HIPAA, thus complicating compliance efforts.

Efforts to ensure that our business arrangements with third parties will comply with applicable healthcare laws and regulations will involve substantial costs. It is possible that governmental authorities will conclude that our business practices may not comply with current or future statutes, regulations or case law involving applicable fraud and abuse or other healthcare laws and regulations. If our operations are found to be in violation of any of these laws or any other governmental regulations that may apply to us, we may be subject to significant civil, criminal and administrative penalties, damages, fines, imprisonment, exclusion of products from government funded healthcare programs, such as Medicare and Medicaid, and the curtailment or restructuring of our operations. If any of the physicians or other healthcare providers or entities with whom we expect to do business is found to be not in compliance with applicable laws, they may be subject to criminal, civil or administrative sanctions, including exclusions from government funded healthcare programs.

***Recently enacted and future legislation may increase the difficulty and cost for us to obtain marketing approval of and commercialize our product candidates and affect the prices we may obtain.***

In the United States and some foreign jurisdictions, there have been a number of legislative and regulatory changes and proposed changes regarding the healthcare system that could prevent or delay marketing approval of our product candidates, restrict or regulate post-approval activities and affect our ability to profitably sell any product candidates for which we obtain marketing approval. In the United States, the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, or the MMA, changed the way Medicare covers and pays for pharmaceutical products. The legislation expanded Medicare coverage for drug purchases by the elderly and introduced a new reimbursement methodology based on average sales prices for physician-administered drugs. In addition, this legislation provided authority for limiting the number of drugs that will be covered in any therapeutic class. Cost reduction initiatives and other provisions of this legislation could decrease the coverage and price that we receive for any approved products. 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 reimbursement rates. Therefore, any reduction in reimbursement that results from the MMA may result in a similar reduction in payments from private payors.

In March 2010, President Obama signed into law the Patient Protection and Affordable Care Act,