

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(MARK ONE)

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

For the quarterly period ended March 31, 2014

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 001-35238

**HORIZON PHARMA, INC.**

(Exact name of registrant as specified in its charter)

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

**27-2179987**  
(I.R.S. Employer  
Identification No.)

**520 Lake Cook Road, Suite 520**  
**Deerfield, Illinois**  
(Address of principal executive offices)

**60015**  
(Zip Code)

**(224) 383-3000**  
(Registrant's telephone number, including area code)

**Not applicable**  
(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

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

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

Number of shares of registrant's common stock, par value \$0.0001, outstanding as of May 6, 2014: 73,464,786.

**HORIZON PHARMA, INC.**

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

**HORIZON PHARMA, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED)**  
**(In thousands, except share data)**

	March 31, 2014	December 31, 2013
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 103,374	\$ 80,480
Restricted cash	738	738
Accounts receivable, net	40,100	15,958
Inventories, net	9,432	8,701
Prepaid expenses and other current assets	9,105	4,888
Total current assets	<u>162,749</u>	<u>110,765</u>
Property and equipment, net	3,897	3,780
Intangible assets, net	125,992	131,094
Other assets	6,496	6,957
<b>TOTAL ASSETS</b>	<u>\$ 299,134</u>	<u>\$ 252,596</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 10,271	\$ 9,921
Accrued expenses	44,712	24,049
Accrued royalties	11,416	8,010
Deferred revenues—current portion	3,102	1,330
Total current liabilities	<u>69,501</u>	<u>43,310</u>
<b>LONG-TERM LIABILITIES:</b>		
Convertible debt, net	112,774	110,762
Derivative liability	313,440	109,410
Accrued royalties	21,576	24,982
Deferred revenues, net of current	8,017	9,686
Deferred tax liabilities, net	2,903	3,362
Other long term liabilities	166	166
Total long-term liabilities	<u>458,876</u>	<u>258,368</u>
<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>STOCKHOLDERS' EQUITY:</b>		
Common stock, \$0.0001 par value; 200,000,000 shares authorized; 71,413,573 and 66,097,417 shares issued and outstanding at March 31, 2014 and December 31, 2013, respectively	7	7
Additional paid-in capital	436,513	410,430
Accumulated other comprehensive loss	(2,398)	(2,403)
Accumulated deficit	(663,365)	(457,116)
Total stockholders' deficit	<u>(229,243)</u>	<u>(49,082)</u>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<u>\$ 299,134</u>	<u>\$ 252,596</u>

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

**HORIZON PHARMA, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**  
**(UNAUDITED)**  
**(In thousands, except share and per share data)**

	Three Months Ended March 31,	
	2014	2013
<b>REVENUES:</b>		
Gross sales	\$ 92,248	\$ 10,698
Sales discounts and allowances	(40,322)	(2,005)
Net sales	51,926	8,693
Cost of goods sold	7,619	3,769
Gross profit	44,307	4,924
<b>OPERATING EXPENSES:</b>		
Research and development	2,833	2,198
Sales and marketing	28,695	16,328
General and administrative	11,192	4,942
Total operating expenses	42,720	23,468
Operating income (loss)	1,587	(18,544)
<b>OTHER (EXPENSE) INCOME, NET:</b>		
Interest expense, net	(4,207)	(3,603)
Foreign exchange loss	(38)	(905)
Loss on derivative fair value	(204,030)	—
Other, net	(667)	—
Total other expense, net	(208,942)	(4,508)
Loss before benefit for income taxes	(207,355)	(23,052)
<b>BENEFIT FOR INCOME TAXES</b>	(1,105)	(881)
<b>NET LOSS</b>	<b>\$ (206,250)</b>	<b>\$ (22,171)</b>
<b>NET LOSS PER COMMON SHARE - Basic and diluted</b>	<b>\$ (3.07)</b>	<b>\$ (0.36)</b>
<b>WEIGHTED AVERAGE COMMON SHARES OUTSTANDING - Basic and diluted</b>	<b>67,138,463</b>	<b>61,939,822</b>
<b>OTHER COMPREHENSIVE INCOME (LOSS), NET OF TAX</b>		
Foreign currency translation adjustments	5	(797)
Other comprehensive income (loss)	5	(797)
<b>COMPREHENSIVE LOSS</b>	<b>\$ (206,245)</b>	<b>\$ (22,968)</b>

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

**HORIZON PHARMA, INC.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**  
**(In thousands)**

	Three Months Ended March 31,	
	2014	2013
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (206,250)	\$ (22,171)
<b>Adjustments to reconcile net loss to net cash used in operating activities:</b>		
Depreciation and intangible amortization expense	5,403	1,922
Stock-based compensation	1,927	1,079
Loss on derivative revaluation	204,030	—
Amortization of debt discount and deferred financing costs	2,333	910
Paid in kind interest expense	—	783
Foreign exchange loss	38	905
Changes in operating assets and liabilities:		
Accounts receivable	(24,142)	(4,300)
Inventories	(729)	866
Prepaid expenses and other current assets	(4,218)	379
Accounts payable	352	(1,026)
Accrued expenses	20,702	(1,682)
Deferred revenues	112	349
Deferred tax liabilities	(454)	(864)
Other non-current assets and liabilities	139	81
Net cash used in operating activities	<u>(757)</u>	<u>(22,769)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(494)	(225)
Net cash used in investing activities	<u>(494)</u>	<u>(225)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from the issuance of common stock	24,156	—
Net cash provided by financing activities	<u>24,156</u>	<u>—</u>
Effect of foreign exchange rate changes on cash	(11)	(17)
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>22,894</b>	<b>(23,011)</b>
<b>CASH AND CASH EQUIVALENTS, beginning of the year</b>	<b>80,480</b>	<b>104,087</b>
<b>CASH AND CASH EQUIVALENTS, end of the period</b>	<b><u>\$ 103,374</u></b>	<b><u>\$ 81,076</u></b>
<b>Supplemental cash flow information:</b>		
Cash paid for interest	\$ —	\$ 1,876
Cash paid for income taxes	10	17
Fee paid for debt commitment	5,000	—

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

**HORIZON PHARMA, INC.**  
**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(In thousands, except share and per share data)**

**NOTE 1 – BASIS OF PRESENTATION**

The unaudited condensed consolidated financial statements presented herein have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the financial statements do not include all of the information and notes required by GAAP for complete financial statements. In the opinion of management, all adjustments, including normal recurring adjustments, considered necessary for a fair statement of the financial statements have been included. Operating results for the three months ended March 31, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. The December 31, 2013 condensed consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by GAAP.

The unaudited condensed consolidated financial statements presented herein include the accounts of Horizon Pharma, Inc. (the “Company”) and its wholly-owned subsidiaries. All inter-company transactions and balances have been eliminated. Additionally, certain reclassifications have been made to prior period financial statements to conform to the current period presentation.

During the fourth quarter of 2013, the Company determined that there had been a misclassification of certain fees in its financial statements for the previously reported periods. Those financial statements classified wholesaler service fees as cost of goods sold. The Company determined that these fees should be classified as sales discounts and allowances, which are a reduction in revenue instead of an increase in cost of goods sold and has revised all identified prior period misclassifications in the periods in which they originated. The revision had no impact on the Company’s reported gross profit, net loss or cash flows and was immaterial individually or in the aggregate, to any of the prior reporting periods. Amounts included within this Quarterly Report on Form 10-Q for the period ended March 31, 2013 have been revised to reflect this adjustment of \$478 from cost of goods sold to sales discounts and allowances. The revision increased sales discounts and allowances and reduced both net sales and cost of goods sold by this amount.

Additionally, as previously disclosed in the Company’s Quarterly Report on Form 10-Q for the period ended June 30, 2013, the Company made a \$258 reclassification of certain departmental expenses from general and administrative expenses to selling and marketing expenses in the Company’s condensed consolidated statements of comprehensive loss for the three months ended March 31, 2013.

During the first quarter of 2014, the Company recorded an out of period adjustment of \$1,578 resulting in a reduction to its wholesaler fees. This adjustment to wholesaler fees was recorded as a reduction of sales discounts and allowances within the Company’s condensed consolidated statements of comprehensive loss for the three months ended March 31, 2014. The Company has evaluated the impact of the reduction in wholesaler fees to prior reporting periods and has determined it was immaterial.

**Business Overview**

The Company was incorporated in Delaware on March 23, 2010. On April 1, 2010, the Company became a holding company that operates primarily through its two wholly-owned subsidiaries, Horizon Pharma USA, Inc., a Delaware corporation, and Horizon Pharma AG, a company organized under the laws of Switzerland which was acquired by the Company on April 1, 2010 in exchange for newly-issued shares of Horizon Pharma, Inc. Horizon Pharma AG owns all of the outstanding share capital of its wholly-owned subsidiary, Horizon Pharma GmbH, a company organized under the laws of Germany, through which Horizon Pharma AG conducts most of its European operations. Unless the context indicates otherwise, the “Company” refers to Horizon Pharma, Inc. and its subsidiaries taken as a whole.

The Company is a specialty pharmaceutical company commercializing DUEXIS®, VIMOVO® and RAYOS®/LODOTRA®, each of which targets unmet therapeutic needs in arthritis, pain and inflammatory diseases. The Company developed DUEXIS and RAYOS/LODOTRA, and it acquired the U.S. rights to VIMOVO from AstraZeneca AB (“AstraZeneca”) in November 2013. The Company markets its products in the United States through its field sales force of approximately 290 representatives. The Company’s strategy is to develop, acquire or in-license additional innovative medicines or acquire companies, such as the Company’s proposed transaction with Vidara Therapeutics International Ltd. (“Vidara”), where the Company can execute a targeted commercial approach among specific target physicians, such as primary care physicians, orthopedic surgeons and rheumatologists, while taking advantage of its commercial strengths and the infrastructure that has been put in place.

On April 23, 2011, the U.S. Food and Drug Administration (“FDA”) approved DUEXIS, a proprietary tablet formulation containing a fixed-dose combination of ibuprofen and famotidine in a single pill. DUEXIS is indicated for the relief of signs and symptoms of rheumatoid arthritis (“RA”), osteoarthritis (“OA”) and to decrease the risk of developing upper gastrointestinal ulcers in patients who are taking ibuprofen for these indications. The Company began detailing DUEXIS to physicians in December 2011. In June 2012, the Company licensed DUEXIS rights in Latin America to Grünenthal S.A., a private company focused on the promotion of pain products.

The Company’s second approved product in the United States, RAYOS, known as LODOTRA outside the United States, is a proprietary delayed-release formulation of low-dose prednisone for the treatment of moderate to severe, active RA in adults, particularly when accompanied by morning stiffness. On July 26, 2012, the FDA approved RAYOS for the treatment of RA, polymyalgia rheumatica (“PMR”), psoriatic arthritis, ankylosing spondylitis (“AS”), asthma and chronic obstructive pulmonary disease and a number of other conditions. The Company is focusing its promotion of RAYOS in the United States on rheumatology indications, including RA and PMR. The Company began detailing RAYOS to a subset of U.S. rheumatologists in December 2012 and began the full launch in late January 2013 to the majority of U.S. rheumatologists and key primary care physicians. LODOTRA is currently marketed outside the United States by the Company’s distribution partner, Mundipharma International Corporation Limited (“Mundipharma”).

On November 18, 2013, the Company entered into agreements with AstraZeneca pursuant to which the Company acquired from AstraZeneca and its affiliates certain intellectual property and other assets, and assumed from AstraZeneca and its affiliates certain liabilities, each with respect to VIMOVO, and obtained rights to develop other pharmaceutical products that contain gastroprotective agents in a single fixed combination oral solid dosage form with non-steroidal anti-inflammatory drugs (“NSAIDs”) in the United States. VIMOVO (naproxen/esomeprazole magnesium) is a proprietary fixed-dose multi-layer delayed-release tablet combining an enteric-coated naproxen, an NSAID, core and an immediate-release esomeprazole, a proton pump inhibitor, layer surrounding the core. VIMOVO was originally developed by Pozen Inc. (“Pozen”) together with AstraZeneca pursuant to an exclusive global collaboration and license agreement under which AstraZeneca and Pozen agreed to co-develop VIMOVO and AstraZeneca obtained exclusive rights to commercialize VIMOVO worldwide. On April 30, 2010, the FDA approved VIMOVO for the relief of the signs and symptoms of OA, RA, and AS and to decrease the risk of developing gastric ulcers in patients at risk of developing NSAID associated gastric ulcers.



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Under the asset purchase agreement with AstraZeneca, the Company acquired certain existing assets and rights necessary to commercialize VIMOVO in the United States including, among other things, the investigational new drug application (“IND”) and new drug application (“NDA”) for VIMOVO in the United States, AstraZeneca’s interest in certain patents covering VIMOVO in the United States and certain promotional materials and records related to VIMOVO in the United States. In addition, AstraZeneca assigned to the Company its amended and restated collaboration and license agreement for the United States with Pozen, pursuant to which AstraZeneca has in-licensed from Pozen certain patents and know-how of Pozen covering VIMOVO in the United States. For accounting purposes, the acquisition of the U.S. rights to VIMOVO was treated as a business combination. Collectively, these transactions are referred to as the “VIMOVO Acquisition.”

In December 2013, as a result of its acquisition of the U.S. rights to VIMOVO, the Company recognized revenues under the transition agreement with AstraZeneca. The Company announced the availability of Horizon-labeled VIMOVO on January 2, 2014, at which time it also began promotion with its primary care sales force and began direct recording of VIMOVO revenue under the transition agreement.

On March 18, 2014, the Company, Vidara Therapeutics Holdings LLC, a Delaware limited liability company (“Holdings”), Vidara, an Irish private limited company, Hamilton Holdings (USA), Inc., a Delaware corporation and an indirect wholly-owned subsidiary of Vidara (“U.S. HoldCo”), and Hamilton Merger Sub, Inc., a Delaware corporation and a wholly-owned subsidiary of U.S. HoldCo (“Merger Sub”), entered into a Transaction Agreement and Plan of Merger (the “Merger Agreement”). The Merger Agreement provides that, upon the terms and subject to the conditions set forth in the Merger Agreement, Merger Sub will merge with and into the Company, with the Company continuing as the surviving corporation and as a wholly-owned, indirect subsidiary of Vidara (the “Merger”), with Vidara converting to a public limited company and changing its name to Horizon Pharma plc (“New Horizon”). New Horizon will be organized under the laws of Ireland. Upon consummation of the Merger (the “Closing”), the security holders of the Company (excluding the holders of the convertible notes) will own approximately 74% of New Horizon and Holdings will own approximately 26% of New Horizon. At the Closing, Holdings will receive a cash payment of \$200,000, plus the cash of Vidara and its subsidiaries as of Closing, less the indebtedness of Vidara and its subsidiaries and transaction expenses of Vidara and its subsidiaries paid by New Horizon at or following the Closing, subject to certain adjustments.

Vidara is a privately-held specialty pharmaceutical company with operations in Dublin, Ireland and the United States. Vidara markets ACTIMMUNE®, a bioengineered form of interferon gamma-1b, a protein that acts as a biologic response modifier, in the United States. ACTIMMUNE is approved by the FDA for use in children and adults with chronic granulomatous disease (“CGD”) and severe, malignant osteopetrosis (“SMO”). ACTIMMUNE is indicated for reducing the frequency and severity of serious infections associated with CGD and for delaying time to disease progression in patients with SMO.

The New Horizon ordinary shares to be issued to the stockholders of the Company will be registered with the Securities and Exchange Commission (“SEC”) and are expected to be listed on NASDAQ. The Company has secured a \$250,000 bridge loan commitment from Deerfield Management Company, L.P., pending potential execution of its final financing plans.

The Merger, which has been approved by the boards of directors of the parties, is subject to approval by the stockholders of the Company and the satisfaction of customary closing conditions. The Merger is expected to close mid-year 2014.

The financial statements are prepared on a going concern basis, which contemplates the realization of assets and discharge of liabilities in the normal course of business. As of March 31, 2014, the Company had cash and cash equivalents totaling \$103,374. The Company believes that it has sufficient liquidity and capital resources to reach cash flow positive operations based on the Company’s current expectations of continued revenue growth. However, the Company is highly dependent in the near term on the commercial success of DUEXIS, VIMOVO and RAYOS in the U.S. market. Additionally, the Company has convertible debt which may be required to be settled in cash up to the principal amount upon certain circumstances outside the control of the Company, prior to obtaining stockholder approval to issue enough shares to cover the conversion option in shares of its common stock. The Company has incurred net operating losses and negative cash flows from operations since its inception. In order to continue its operations, the Company must generate sufficient revenue and achieve profitable operations. If that does not occur, the Company’s plan is to obtain additional debt or equity financing. There can be no assurance, however, that such financing will be available or on terms acceptable to the Company. These uncertainties and lack of commercial operating history raise substantial doubt about the Company’s ability to continue as a going concern.

## **NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

### *Segment Information*

The Company operates as one segment. Management uses one measure of profitability and does not segment its business for internal reporting.

### *Use of Estimates*

The preparation of the accompanying condensed consolidated financial statements in conformity with GAAP requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.



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### *Foreign Currency Translation and Transactions*

The reporting currency of the Company and its subsidiaries is the U.S. dollar.

The U.S. dollar is the functional currency for the Company's U.S. based businesses and the Euro is the functional currency for its subsidiaries in Switzerland and Germany. Foreign currency-denominated assets and liabilities of these subsidiaries are translated into U.S. dollars based on exchange rates prevailing at the end of the period, revenues and expenses are translated at average exchange rates prevailing during the corresponding period, and stockholders' equity (deficit) accounts are translated at historical exchange rates as of the date of any equity transaction. The effects of foreign exchange gains and losses arising from the translation of assets and liabilities of those entities where the functional currency is not the U.S. dollar are included as a component of accumulated other comprehensive income (loss).

Gains and losses resulting from foreign currency translations are reflected within the Company's results of operations. During the three months ended March 31, 2014 and 2013, the Company recorded a loss from foreign currency translations of \$38 and \$905, respectively. The Company does not currently utilize and has not in the past utilized any foreign currency hedging strategies to mitigate the effect of its foreign currency exposure.

### *Revenue Recognition*

Revenue is recognized when all of the following criteria are met: persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; the price is fixed or determinable; and collectability is reasonably assured. Some of the Company's agreements contain multiple elements and in accordance with these agreements, the Company may be eligible for upfront license fees, marketing or commercial milestones and payment for product deliveries.

#### *Revenue from upfront license fees*

The Company recognizes revenues from the receipt of non-refundable, upfront license fees. In situations where the licensee is able to obtain stand-alone value from the license and no further performance obligations exist on the Company's part, revenues are recognized on the earlier of when payments are received or collection is reasonably assured. Where continuing involvement by the Company is required in the form of technology transfer, product manufacturing or technical support, revenues are deferred and recognized over the term of the agreement.

#### *Revenue from milestone receipts*

Milestone payments are recognized as revenue based on achievement of the associated milestones, as defined in the relevant agreements. Revenue from a milestone achievement is recognized when earned, as evidenced by acknowledgment from the Company's partner, provided that (1) the milestone event is substantive and its achievability was not reasonably assured at the inception of the agreement, (2) the milestone represents the culmination of an earnings process and (3) the milestone payment is non-refundable. If all of these criteria are not met, revenue from the milestone achievement is recognized over the remaining minimum period of the Company's performance obligations under the agreement.

#### *Revenue from product deliveries*

The Company recognizes revenue from the delivery of its products when delivery has occurred, title has transferred, the selling price is fixed or determinable, collectability is reasonably assured and the Company has no further performance obligations. In addition, revenue is only recognized when the right of return no longer exists (which is the earlier of the product being dispensed through patient prescriptions or the expiration of the right of return) or when product returns can be reasonably estimated. Due to the Company's ability to reasonably estimate and determine allowances for product returns, rebates and discounts, the Company recognizes DUEXIS and RAYOS revenue at the point of sale to wholesale pharmaceutical distributors and retail chains. The Company also recognizes VIMOVO revenue at the point of sale, consistent with its revenue recognition of DUEXIS and RAYOS, given the availability of prior VIMOVO product return data.

The Company anticipates revenues will continue to result from distribution, marketing, manufacturing and supply agreements with third parties in Europe and certain Asian, Latin American and other countries with respect to LODOTRA.

Under the manufacturing and supply agreements with Mundipharma Medical Company ("Mundipharma Medical"), Mundipharma Medical agreed to purchase LODOTRA exclusively from the Company at a price based on a specified percentage of the average net selling price ("ANSP") for sales in a given country, subject to a minimum price. Mundipharma Medical has a nine-month period from purchase date to request an ANSP adjustment. If the ANSP is lower than the actual purchase price, then Mundipharma Medical would receive a price adjustment. Products sold to Mundipharma Medical are recognized upon delivery at the minimum price, as no contractual right of return exists. The difference between the actual selling price and the minimum price is recorded as deferred revenue until such time as adjustments for product returns, rebates and discounts can be reliably estimated or the nine-month ANSP adjustment period passes, at which time any previously deferred revenue would be recognized as revenue. As of March 31, 2014 and December 31, 2013, deferred revenues related to the sale of LODOTRA were \$956 and \$615, respectively. Additionally, as of March 31, 2014 and December 31, 2013, deferred revenues related to milestone and upfront payments received under existing agreements were \$8,513 and \$8,682, respectively.

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### *Product Sales Discounts and Allowances*

The Company makes allowances for product returns, rebates and discounts at the time of sale to wholesale pharmaceutical distributors and national and regional retail chains. The Company is required to make significant judgments and estimates in determining some of these allowances. If actual results differ from its estimates, the Company will be required to make adjustments to these allowances in the future.

### *Customer Discounts and Rebates*

#### *Product Launch Discounts*

The Company has offered additional discounts to wholesale distributors for product purchased at the time of product launch. The Company has recorded these discounts as an allowance against accounts receivable and a reduction of revenue when orders were placed.

#### *Customer Rebates*

The Company participates in certain commercial rebate programs. Under these rebate programs, the Company pays a rebate to the commercial entity or third-party administrator of the program. The Company accrues estimated rebates based on contract prices, estimated percentages of product sold to qualified patients and estimated levels of inventory in the distribution channel and records the rebate as a reduction of revenue.

#### *Distribution Service Fees*

The Company includes distribution service fees paid to its wholesalers for distribution and inventory management services as a reduction to revenue. The estimates are based on contractually determined fees, typically as a percentage of revenue.

### *Government Rebates and Chargebacks*

#### *Government Rebates*

The Company participates in certain federal government rebate programs, such as Medicare and Medicaid. The Company accrues estimated rebates based on percentages of product sold to qualified patients, estimated rebate percentages and estimated levels of inventory in the distribution channel that will be sold to qualified patients and records the rebate as a reduction of revenue.

#### *Government Chargebacks*

The Company provides discounts to federal government qualified entities with whom the Company has contracted. These federal entities purchase products from the wholesale pharmaceutical distributors at a discounted price, and the wholesale pharmaceutical distributors then charge back to the Company the difference between the current retail price and the contracted price that the federal entities paid for the products. The Company accrues estimated chargebacks based on contract prices and sell-through sales data obtained from third party information and records the chargeback as a reduction of revenue.

### *Co-Pay Assistance*

The Company offers discount card programs to patients under which the patient receives a discount on his or her prescription. The Company reimburses pharmacies for this discount through a third-party vendor. The Company records the total amount of estimated discounts for sales recorded in the period as a reduction of revenue based on a combination of actual invoices received and an estimate of discounts to be paid for product in the sales channel based on historical information.

### *Returns and Prompt Pay Allowances*

#### *Sales Returns*

Consistent with industry practice, the Company maintains a return policy that allows customers to return product within a specified period prior to and subsequent to the product expiration date. Generally, product may be returned for a period beginning six months prior to its expiration date and up to one year after its expiration date. The right of return expires on the earlier of one year after the product expiration date or the time that the product is dispensed to the patient. The majority of product returns result from product dating, which falls within the range set by the Company's policy, and are settled through the issuance of a credit to the customer. The estimate of the provision for returns is based upon the Company's historical experience with actual returns, which is applied to the level of sales for the period that corresponds to the period during which the customer may return product. This period is known to the Company based on the shelf life of products at the time of shipment. The Company records sales returns as an allowance against accounts receivable and a reduction of revenue.

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### *Prompt Pay Discounts*

As an incentive for prompt payment, the Company offers a 2% cash discount to customers. The Company expects that all customers will comply with the contractual terms to earn the discount. The Company records the discount as an allowance against accounts receivable and a reduction of revenue.

### *Bad Debt Expense*

The Company's products are sold to wholesale distributors and retail chains through manufacturing and supply agreements. For the three months ended March 31, 2014 and for the years ended December 31, 2013, 2012 and 2011, the Company did not record a bad debt expense related to its accounts receivable balances. Accordingly, the Company has not established a reserve for bad debt expense. The Company will continue to monitor its accounts receivable balances to determine the impact, if any, of such factors as changes in customer concentration, credit risk and the realizability of its accounts receivable would require a bad debt reserve allowance in subsequent periods.

### *Cost of Goods Sold*

The Company recognizes cost of goods sold in connection with its sale of DUEXIS, VIMOVO and RAYOS/LODOTRA.

Cost of goods sold of DUEXIS includes all costs directly related to the acquisition of product from the Company's third party manufacturers, including freight charges and costs of distribution.

Cost of goods sold of RAYOS includes all costs directly related to the acquisition of product from the Company's third party manufacturers, including freight charges and costs of distribution, amortization of developed technology, royalty payments to third parties for the use of certain licensed patents and applicable taxes.

Cost of goods sold of LODOTRA includes raw material costs, costs associated with third parties who manufacture LODOTRA for the Company, supply chain costs, manufacturing overhead costs, amortization of developed technology, royalty payments to third parties for the use of certain licensed patents and applicable taxes.

Cost of goods sold for VIMOVO in the fourth quarter of 2013, following the acquisition in November 2013 of certain assets and rights necessary to commercialize VIMOVO in the United States, included only intangible amortization expense. In connection with the Company's commercialization of VIMOVO in the United States beginning in January 2014, cost of goods sold for VIMOVO now includes all costs directly related to the acquisition of product from AstraZeneca and/or a third-party manufacturer and intangible amortization expense. At the time of the VIMOVO Acquisition, the Company estimated the fair value of contingent royalties payable to Pozen using an income approach under the discounted cash flow method, which included revenue projections and other assumptions made by the Company to determine the fair value. If the Company were to significantly overperform or underperform against its original revenue projections or it became necessary to make changes to its assumptions, the Company would be required to reassess the fair value of the contingent royalties payable to Pozen. Any adjustments to fair value would be recorded in the period such adjustment was made as either a charge or credit to royalties payable, which is part of cost of goods sold in accordance with the Company's established accounting policies, and could impact the reported operating results in the period the adjustment was made.

### *Inventories*

Inventories are stated at the lower of cost or market value. Inventories consist of raw materials, work-in-process and finished goods. The Company has entered into manufacturing and supply agreements for the manufacture or purchase of raw materials and production supplies. The Company's inventories include the direct purchase cost of materials and supplies and manufacturing overhead costs. As of March 31, 2014 and December 31, 2013, the Company had inventories of \$9,432 and \$8,701, respectively.

Inventories exclude product sample inventory, which is included in other current assets and is expensed as a component of sales and marketing expense when provided to physicians or healthcare providers. As of March 31, 2014 and December 31, 2013, the Company had product sample inventory of \$1,588 and \$1,323, respectively.

### *Preclinical Studies and Clinical Trial Accruals*

The Company's preclinical studies and clinical trials have historically been conducted by third-party contract research organizations and other vendors. Preclinical study and clinical trial expenses are based on the services received from these contract research organizations and vendors. Payments depend on factors such as the milestones accomplished, successful enrollment of certain numbers of patients and site initiation. 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 the estimate, the Company adjusts the accrual accordingly. To date, the Company has had no significant adjustments to accrued clinical expenses.

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### *Net Loss Per Share*

Basic net loss per share is computed by dividing net loss by the weighted-average number of shares of common stock outstanding during the period. For the periods presented, the Company's potential dilutive shares, which include shares issuable upon the exercise of outstanding stock options, unvested restricted stock units and warrants to purchase common stock, have not been included in the computation of diluted net loss per share for the periods presented in which there is a net loss as the result would be anti-dilutive. Such potentially dilutive shares are excluded when the effect would be to reduce net loss per share.

### *Cash and Cash Equivalents*

Cash and cash equivalents primarily consist of cash balances and money market funds. Cash and cash equivalents were \$103,374 and \$80,480 as of March 31, 2014 and December 31, 2013, respectively. The Company's policy is to invest excess cash in money market funds, which are generally of a short-term duration based upon operating requirements.

### *Restricted Cash*

Restricted cash consists of balances included in interest-bearing money market accounts required by a vendor for the Company's sponsored employee credit card program and by the lessor for the Company's corporate office. As of both March 31, 2014 and December 31, 2013, the Company had restricted cash in the amount of \$738.

### *Fair Value of Financial Instruments*

The carrying amounts of the Company's financial instruments, including cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses, approximate their fair values due to their short maturities. The estimated fair value of the Company's derivative liability related to the convertible portion of its 5.00% Convertible Senior Notes due 2018 (the "Convertible Senior Notes") was derived utilizing the binomial lattice approach for the valuation of convertible instruments. Assumptions used in the calculation included, among others, determining the appropriate credit spread using benchmarking analysis and solving for the implied credit spread, calculating the fair value of the stock component using a discounted risk free rate and borrowing cost and calculating the fair value of the note component using a discounted credit adjusted discount rate. Based on the assumptions used to determine the fair value of the derivative liability associated with the Convertible Senior Notes, the Company concluded that these inputs were Level 3 inputs. The Company will continue to derive the fair value of the derivative liability using the binomial lattice approach and these assumptions in all future reporting periods.

### *Business Combinations*

The Company accounts for business combinations in accordance with the pronouncement guidance in ASC 805, *Business Combinations*, in which acquired assets and liabilities are measured at their respective estimated fair values as of the acquisition date. The Company may be required, as in the case of intangible assets or contingent royalties, to determine the fair value associated with these amounts by estimating the fair value using an income approach under the discounted cash flow method, which may include revenue projections and other assumptions made by the Company to determine the fair value.

### *Property and Equipment, Net*

Property and equipment are stated at cost less accumulated depreciation. Depreciation is recognized using the straight-line method over the estimated useful lives of the related assets for financial reporting purposes and an accelerated method for income tax reporting purposes. Upon retirement or sale of an asset, the cost and related accumulated depreciation and amortization are removed from the balance sheet and the resulting gain or loss is reflected in operations. Repair and maintenance costs are charged to expenses as incurred and improvements are capitalized.

Leasehold improvements are amortized on a straight-line basis over the term of the applicable lease, or the useful life of the assets, whichever is shorter.

Depreciation and amortization periods for the Company's property and equipment are as follows:

Machinery and equipment	5-7 years
Furniture and fixtures	3-5 years
Computer equipment	3 years
Software	3 years
Trade show equipment	3 years

Software includes internal-use software acquired and modified to meet the Company's internal requirements. Amortization commences when the software is ready for its intended use.

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### *Intangible Assets*

The Company's intangible assets consist of developed technology related to three of its approved products: LODOTRA outside the United States, RAYOS in the United States and intellectual property rights related to the Company's acquisition of the U.S. rights to VIMOVO. The Company amortizes the LODOTRA and RAYOS intangible assets over twelve years, which is the estimated useful life of the underlying patents, and amortizes the U.S. intellectual property rights of the VIMOVO intangible asset over an estimated useful life of 61.5 months, or through the end of 2018. The Company reviews its intangible assets when events or circumstances may indicate that the carrying value of these assets exceeds their fair value. The Company measures fair value based on the estimated future discounted cash flows associated with these assets in addition to other assumptions and projections that the Company deems to be reasonable and supportable.

### *Research and Development Expenses*

Research and development expenses include, but are not limited to, payroll and other personnel expenses, consultant expenses, expenses incurred under agreements with contract research organizations to conduct clinical trials and expenses incurred to manufacture clinical trial materials.

### *Sales and Marketing Expenses*

Sales and marketing expenses consist principally of payroll of sales representatives and marketing and support staff, travel and other personnel-related expenses, marketing materials and distributed sample inventories. In addition, sales and marketing expenses include the Company's medical affairs expenses, which consist of expenses related to scientific publications, health outcomes, biostatistics, medical education and information, and medical communications.

### *Concentration of Credit Risk and Other Risks and Uncertainties*

Financial instruments that may potentially subject the Company to significant concentrations of credit risk consist of cash and cash equivalents. The Company's cash and cash equivalents are invested in deposits with various banks in the United States, Switzerland and Germany that management believes are creditworthy. At times, deposits in these banks may exceed the amount of insurance provided on such deposits. To date, the Company has not experienced any losses on its deposits of cash and cash equivalents.

The Company's LODOTRA sales contracts are principally denominated in Euros and, therefore, its revenues are subject to significant foreign currency risk.

To achieve profitable operations, the Company must successfully develop, obtain regulatory approval for, manufacture and market its products and product candidates, and/or acquire or in-license products from third parties. There can be no assurance that any additional products can be developed, will be approved for marketing by the regulatory authorities, or can be manufactured at an acceptable cost and with appropriate performance characteristics or that any new or existing products can be successfully marketed, acquired or in-licensed by the Company. These factors could have a material adverse effect on the Company's operations.

The Company relies on third parties to manufacture its commercial supplies of DUEXIS, VIMOVO and RAYOS/LODOTRA. The commercialization of any of its products or product candidates could be stopped, delayed or made less profitable if those third parties fail to provide the Company with sufficient quantities of product or fail to do so at acceptable quality levels or prices.

The Company is required to maintain compliance with applicable Swiss laws with respect to its Swiss subsidiary, Horizon Pharma AG, including laws requiring maintenance of equity in the subsidiary to avoid overindebtedness, which requires Horizon Pharma AG to maintain assets in excess of its liabilities. The Company reviews on a regular basis whether its Swiss subsidiary is overindebted. As of March 31, 2014 and December 31, 2013, the Company's Swiss subsidiary was overindebted, primarily as a result of operating losses at the subsidiary. The Company will continue to monitor and review steps to address any overindebtedness until such time as its Swiss subsidiary may generate positive income at a statutory level, which could require the Company to have cash at its Swiss subsidiary in excess of its near term operating needs and could affect the Company's ability to have sufficient cash at its U.S. subsidiary to meet its near term operating needs. As of March 31, 2014 and December 31, 2013, Horizon Pharma AG had cash and cash equivalents of \$2,558 and \$3,476, respectively. Based upon the cash and cash equivalents held by Horizon Pharma AG as of March 31, 2014 and December 31, 2013 and Horizon Pharma AG's level of overindebtedness at such time, the Company does not expect that its financial position or results of operations will be materially affected by any need to address overindebtedness at its Swiss subsidiary. To date, the overindebtedness of the Company's Swiss subsidiary has not resulted in the need to divert material cash resources from its U.S. subsidiary.

Historically, the Company's accounts receivable balances have been highly concentrated with a select number of customers, consisting primarily of large wholesale pharmaceutical distributors who, in turn, sell the products to pharmacies, hospitals and other customers. For the three months ended March 31, 2014, the Company's top three customers, AmerisourceBergen, McKesson Corporation and Cardinal Health, Inc., accounted for approximately 85% of total consolidated gross sales. For the year ended December 31, 2013, the Company's top five customers, AmerisourceBergen, McKesson Corporation, Cardinal Health, Inc., Mundipharma and Rochester Drug Company, accounted for approximately 89% of total consolidated gross sales.

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In addition, three customers, McKesson Corporation, AmerisourceBergen and Cardinal Health, Inc., accounted for approximately 85% of the Company's total outstanding accounts receivable balances at March 31, 2014. As of December 31, 2013, four customers, McKesson Corporation, AmerisourceBergen, Rochester Drug Company and Cardinal Health, Inc., accounted for approximately 85% of the Company's total outstanding accounts receivable balances. Historically, the Company has not experienced any losses related to its accounts receivable balances.

### *Comprehensive Income (Loss)*

Comprehensive income (loss) is comprised of net income (loss) and other comprehensive income (loss) ("OCI"). OCI includes certain changes in stockholders' equity that are excluded from net income (loss), which consist of foreign currency translation adjustments. In February 2013, the Company adopted on a prospective basis FASB Accounting Standards Update 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* ("ASU 2013-02"). ASU 2013-02 requires an entity to report the effect of significant reclassifications out of accumulated OCI on the respective line items in net income if the amount being reclassified is required under GAAP to be reclassified in its entirety to net income. For other amounts that are not required under GAAP to be reclassified in their entirety to net income in the same reporting period, an entity is required to cross-reference other disclosures required under GAAP that provide additional detail about those amounts. As of March 31, 2014 and December 31, 2013, accumulated other comprehensive loss was \$2,398 and \$2,403, respectively.

### **NOTE 3 – EARNINGS PER SHARE**

The following table presents basic and diluted earnings (loss) per share for the three months ended March 31, 2014 and 2013:

	<u>Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
<b>Basic and diluted earnings per share calculation:</b>		
Net loss	\$ (206,250)	\$ (22,171)
Weighted average of common shares outstanding	67,138,463	61,939,822
Basic and diluted net loss per share	<u>\$ (3.07)</u>	<u>\$ (0.36)</u>

The following dilutive securities were excluded from the computation of diluted earnings per share for the three months ended March 31, 2014 and 2013 due to the anti-dilutive effects resulting from the Company's net loss for the periods presented:

- Outstanding stock options to purchase an aggregate of 5,704,679 and 4,008,164 shares of common stock at March 31, 2014 and 2013, respectively; outstanding and unvested restricted stock units covering an aggregate of 1,437,526 and 915,158 shares of common stock at March 31, 2014 and 2013, respectively; and 244,079 vested restricted stock units outstanding at March 31, 2014.
- Outstanding common stock warrants to purchase an aggregate of 10,918,973 and 17,480,243 shares of common stock at March 31, 2014 and 2013, respectively.
- 13,164,951 shares of the Company's common stock associated with the potential conversion of the Convertible Senior Notes as the conversion is subject to such share limitation under applicable NASDAQ rules until such time as the Company receives stockholder approval to issue all shares required to cover the conversion option.

### **NOTE 4 – BUSINESS ACQUISITIONS**

#### *Vidara acquisition*

On March 18, 2014, the Company, Holdings, Vidara, U.S. HoldCo and Merger Sub, entered into the Merger Agreement. The Merger Agreement provides that, upon the terms and subject to the conditions set forth in the Merger Agreement, Merger Sub will merge with and into the Company, with the Company continuing as the surviving corporation and as a wholly-owned, indirect subsidiary of Vidara, with Vidara converting to a public limited company and changing its name to Horizon Pharma plc.

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At the effective time of the Merger (the “Effective Time”), (i) each share of the Company’s common stock issued and outstanding will be converted into one ordinary share of New Horizon; (ii) each equity plan of the Company will be assumed by New Horizon and each outstanding option under the Company’s equity plans will be converted into an option to acquire the number of ordinary shares of New Horizon equal to the number of shares of common stock underlying such option immediately prior to the Effective Time at the same exercise price per share as such option of the Company, and each other stock award that is outstanding under the Company’s equity plans will be converted into a right to receive, on substantially the same terms and conditions as were applicable to such equity award before the Effective Time, the number of ordinary shares of New Horizon equal to the number of shares of common stock of the Company subject to such stock award immediately prior to the Effective Time; (iii) each warrant to acquire the Company’s common stock outstanding immediately prior to the Effective Time and not terminated as of the Effective Time will be converted into a warrant to acquire, on substantially the same terms and conditions as were applicable under such warrant before the Effective Time, the number of ordinary shares of New Horizon equal to the number of shares of common stock underlying such warrant immediately prior to the Effective Time; and (iv) the Convertible Senior Notes will remain outstanding and, pursuant to a supplemental indenture to be entered into effective as of the Effective Time, will become convertible into the same number of ordinary shares of New Horizon at the same conversion rate in effect immediately prior to the Effective Time. Holdings will also retain ownership of 31,350,000 ordinary shares of New Horizon at the Effective Time. Upon consummation of the Merger (the “Closing”), the security holders of the Company (excluding the holders of the Convertible Senior Notes) will own approximately 74% of New Horizon and Holdings will own approximately 26% of New Horizon. At the Closing, Holdings will receive a cash payment of \$200,000, plus the cash of Vidara and its subsidiaries as of Closing, less the indebtedness of Vidara and its subsidiaries and transaction expenses of Vidara and its subsidiaries paid by New Horizon at or following the Closing, plus or minus an adjustment to the extent that Vidara’s working capital (exclusive of cash) as of the Closing exceeds or is less than target working capital of \$123.

In connection with the Merger Agreement, the Company entered into a commitment letter (the “Commitment Letter”) with Deerfield Management Company, L.P. (“Deerfield”) and certain funds managed by Deerfield (the “Deerfield Funds”), pursuant to which the Deerfield Funds have committed to provide up to \$250,000 of senior secured loans to finance the Merger (the “Facility”). The commitment to provide the Facility is subject to certain conditions, including the negotiation of definitive documentation and other customary closing conditions consistent with the Merger Agreement. The receipt of funding under the Facility is not a condition to the obligations of the Company under the terms of the Merger Agreement.

The obligation of each party to consummate the Merger is subject to certain conditions, including the receipt of the requisite approval by the stockholders of the Company as well as other customary closing conditions.

If the Merger Agreement is terminated by Holdings following a change of the recommendation of the Company’s board of directors, the Company would be obligated to pay Holdings a termination fee of \$23,000 and may be obligated to pay such termination fee in other circumstances specified in the Merger Agreement. If the Merger Agreement is terminated because the stockholders of the Company do not approve the adoption of the Merger Agreement and the Merger, then the Company would be obligated to pay Holdings an expense reimbursement fee of \$13,500. If the Merger Agreement is terminated because the Company fails to close the transaction after satisfaction of all of the conditions to Closing and Holdings is ready to close the Merger, then the Company would be obligated to pay Holdings a termination fee of \$44,000.

### ***VIMOVO acquisition***

On November 18, 2013, the Company entered into agreements with AstraZeneca pursuant to which the Company acquired from AstraZeneca and its affiliates certain intellectual property and other assets, and assumed from AstraZeneca and its affiliates certain liabilities, each with respect to VIMOVO, and obtained rights to develop other pharmaceutical products that contain gastroprotective agents in a single fixed combination oral solid dosage form with NSAIDs, in the United States. VIMOVO (naproxen/esomeprazole magnesium), a proprietary fixed-dose multi-layer delayed-release tablet combining an enteric-coated naproxen, an NSAID, core and an immediate-release esomeprazole, a proton pump inhibitor, layer surrounding the core, was approved by the FDA in 2010 for the relief of the signs and symptoms of OA, RA and AS, and to decrease the risk of developing gastric ulcers in patients at risk of developing NSAID-associated gastric ulcers.

Pursuant to the transactions contemplated by the asset purchase agreement, the Company acquired certain existing assets and rights necessary to commercialize VIMOVO in the United States including, among other things, the IND and NDA for VIMOVO in the United States, AstraZeneca’s interest in certain patents covering VIMOVO in the United States and certain promotional materials and records related to VIMOVO in the United States. The Company will also be entitled to the benefit of a covenant not to sue granted by Merck Sharp & Dohme Corp. and certain of its affiliates (collectively, “Merck”) to AstraZeneca, with respect to certain patents owned by AstraZeneca but exclusively licensed to Merck, that cover the manufacture and commercialization of VIMOVO in the United States. In addition, AstraZeneca assigned to the Company its amended and restated collaboration and license agreement for the United States with Pozen pursuant to which AstraZeneca has in-licensed from Pozen certain patents and know-how of Pozen covering VIMOVO in the United States. The terms of the amended and restated collaboration and license agreement for the United States with Pozen (the “Pozen license agreement”) are described below.

In November 2013, in connection with the closing of the transactions contemplated by the asset purchase agreement, the Company also entered into a license agreement with AstraZeneca, a supply agreement with AstraZeneca’s affiliate, AstraZeneca LP, and certain other agreements that are described below. The Company also executed a transition agreement with AstraZeneca pursuant to which AstraZeneca transitioned to the Company regulatory and commercial responsibility for VIMOVO in the United States. From the closing of the transaction until December 31, 2013, AstraZeneca continued to commercialize VIMOVO in the United States under AstraZeneca’s existing pricing and paid to the Company the net profits recognized on sales of VIMOVO in the United States. Beginning January 2, 2014, the Company commenced commercialization of VIMOVO in the United States on its own behalf and under new pricing for VIMOVO. In consideration for the U.S. rights to VIMOVO, the Company paid to AstraZeneca a one-time upfront cash payment of \$35,000.

The Company is responsible for and controls matters relating to VIMOVO in the United States, including responsibility for commercialization of VIMOVO in the United States, responsibility for ongoing developmental and regulatory activities with respect to VIMOVO in the United States and responsibility for the current VIMOVO litigation with respect to the patents the Company purchased under the asset purchase agreement and the patents the Company licensed from Pozen under the Pozen license agreement. AstraZeneca will be responsible for and will retain control of VIMOVO outside the United States.

Additionally, in connection with the closing of the transactions contemplated by the asset purchase agreement, the Company entered into a license agreement with AstraZeneca (the “AstraZeneca license agreement”), pursuant to which AstraZeneca granted the Company an exclusive license under certain intellectual property (including patents, know-how, trademarks, copyrights and domain names) of AstraZeneca and its affiliates to develop, manufacture and commercialize VIMOVO in the United States. AstraZeneca also granted the Company a non-exclusive license under certain intellectual property of AstraZeneca and its affiliates to manufacture, import, export and perform research and development activities with respect to VIMOVO outside the United States but solely for purposes of commercializing VIMOVO in the United States. In addition, AstraZeneca granted the Company a non-exclusive right of

reference and use under certain regulatory documentation controlled by AstraZeneca and its affiliates to develop, manufacture and commercialize VIMOVO in the United States and to manufacture, import, export and perform research and development activities with respect to VIMOVO outside the United States but solely for purposes of commercializing VIMOVO in the United States.

Under the AstraZeneca license agreement, the Company granted AstraZeneca a non-exclusive sublicense under such licensed intellectual property and a non-exclusive right of reference under certain regulatory documentation controlled by the Company to manufacture, import, export and perform research and development activities with respect to VIMOVO in the United States but solely for purposes of commercializing VIMOVO outside the United States.

Under the AstraZeneca license agreement, the Company and its affiliates are subject to certain limitations and restrictions on its ability to develop, commercialize and seek regulatory approval with respect to VIMOVO or other products that contain gastroprotective agents in a single fixed combination oral solid dosage form with NSAIDs (excluding DUEXIS). These limitations and restrictions include, among other things, restrictions on indications for which the Company may commercialize VIMOVO or any such other products, restrictions on the Company's ability to develop or seek regulatory approval with respect to such other products that contain esomeprazole, restrictions on the Company's ability to develop or seek regulatory approval for VIMOVO for any indications other than the indications for which NSAIDs are indicated, and restrictions on the Company's marketing activities with respect to VIMOVO and any such other products.

Under the Pozen license agreement, Pozen granted to the Company an exclusive, royalty-bearing license under certain of Pozen's intellectual property in the United States to manufacture, develop and commercialize VIMOVO and other products controlled by the Company that contain gastroprotective agents in a single fixed combination oral solid dosage form with NSAIDs, excluding DUEXIS, in the United States.

Under the Pozen license agreement, the Company is required to pay Pozen a flat 10% royalty on net sales of VIMOVO and such other products sold by the Company, its affiliates or sublicensees during the royalty term, subject to minimum annual royalty obligations of \$5,000 in 2014 and \$7,500 each year thereafter, which minimum royalty obligations will continue for each year during which one of Pozen's patents covers such products in the United States and there are no competing products in the United States. The royalty rate may be reduced to a mid-single digit royalty rate as a result of loss of market share to competing products. The Company's obligation to pay royalties to Pozen will expire upon the later of (a) expiration of the last-to-expire of certain patents covering such products in the United States, and (b) ten years after the first commercial sale of such products in the United States. In addition, the Company is obligated to reimburse Pozen for costs, including attorneys' fees, incurred by Pozen in connection with VIMOVO patent litigation moving forward, subject to agreed caps.

The Company is responsible for and is required to use diligent and reasonable efforts to commercialize VIMOVO or another qualified product in the United States. The Company also owns and maintains all regulatory filings and marketing approvals in the United States for any such products, including all INDs and NDAs for VIMOVO. Pozen has covenanted that it will not at any time prior to the expiration of the royalty term, and will ensure that its affiliates do not, directly or indirectly, develop or commercialize or license any third party to develop or commercialize certain competing products in the United States.

The Pozen license agreement, unless earlier terminated, will expire upon expiration of the royalty term for all such products in the United States. Either party has the right to terminate the agreement upon any uncured material breach by the other party or upon the bankruptcy or similar proceeding of the other party. The Company also has the right to terminate the Pozen license agreement for cause upon certain defined product failures.

In November 2013, in connection with the asset purchase agreement and the Pozen license agreement, the Company, AstraZeneca and Pozen entered into a letter agreement in which Pozen consented to AstraZeneca's assignment of the Pozen license agreement to the Company and that addresses the rights and responsibilities of the parties in relation to the Pozen license agreement and the amended and restated collaboration and license agreement between Pozen and AstraZeneca for territories outside the United States (the "Pozen-AstraZeneca license agreement"). Under the letter agreement, the Company and AstraZeneca agreed to pay Pozen milestone payments upon the achievement by the Company and AstraZeneca, collectively, of certain annual aggregate global sales thresholds ranging from \$550,000 to \$1,250,000 with respect to products licensed by Pozen to the Company under the Pozen license agreement and to AstraZeneca under the Pozen-AstraZeneca license agreement. The aggregate milestone payment amount that may be owed by AstraZeneca and the Company, collectively, under the letter agreement is \$260,000, with the amount payable by each of the Company and AstraZeneca with respect to each milestone to be based upon the proportional sales achieved by each of the Company and AstraZeneca, respectively, in the applicable year.

The letter agreement will terminate with respect to Pozen and the Company upon the termination of the Pozen license agreement and will terminate with respect to Pozen and AstraZeneca upon the termination of the Pozen-AstraZeneca license agreement.

In November 2013, in connection with the asset purchase agreement, the Company entered into a supply agreement with AstraZeneca pursuant to which AstraZeneca agreed to supply VIMOVO to the Company for commercialization in the United States through December 31, 2014. Under the supply agreement, AstraZeneca will supply the quantity of VIMOVO that the Company orders, both for the Company's own use and for use by the Company's sublicensees, on a transitional basis through December 31, 2014. The Company agreed to pay a set transfer price agreed to by the Company and AstraZeneca for quantities of VIMOVO supplied by AstraZeneca under the supply agreement.

The supply agreement will expire on December 31, 2014, unless terminated earlier as described herein. The supply agreement may be terminated earlier by either party for any uncured material breach by the other party of its obligations under the supply agreement or upon the bankruptcy or similar proceeding of the other party. Additionally, the Company has the right to terminate the supply agreement at any time upon 120 days prior written notice to AstraZeneca or immediately upon written notice if the existing regulatory approval of VIMOVO is suspended for any reason or if any regulatory authority provides a warning letter or other official documentation expressing major and significant concerns from a regulatory perspective with AstraZeneca's or its affiliates' or third party manufacturer's manufacturing of VIMOVO. Additionally, the supply agreement will automatically terminate upon any termination of the AstraZeneca license agreement.

Pursuant to ASC Topic 805, *Business Combinations*, the Company accounted for the acquisition of the U.S. rights to VIMOVO under the acquisition method of accounting, in which the Company recognized and accounted for the acquisition of the U.S. rights to VIMOVO as a business combination. Net tangible and intangible assets acquired and contingent royalty liabilities, based upon their respective estimated fair values as of the acquisition date (November 22, 2013). The following table shows the fair values assigned to the assets acquired and liabilities assumed by the Company as part of the asset purchase agreement:

	<u>Allocation</u>
Samples inventory	\$ 287
VIMOVO intellectual property	67,705
Contingent royalty liabilities	<u>(32,992)</u>
Total cash consideration paid	<u>\$ 35,000</u>



The valuation of the intellectual property acquired, an identifiable intangible asset, was based on management's estimates, information and reasonable and supportable assumptions. The allocation was generally based on the Company's estimated fair value of the rights to payments with respect to U.S. revenue associated with VIMOVO which were acquired in the transaction. This estimated fair value was determined using the income approach under the discounted cash flow method. Significant assumptions used in valuing the intellectual property intangible asset included revenue projections through 2030 based on assumptions relating to pricing and reimbursement rates and market size and market penetration rates, cost of goods sold based on current manufacturing experience, general and administrative expenses, sales and marketing expenses, and research and development expenses for clinical and regulatory support. The calculated value of the VIMOVO intellectual property intangible asset is amortized using the straight-line method over an estimated useful life of 61.5 months.

Additionally, the Company assigned a fair value to its liability for contingent royalties. The contingent royalty liability was based on anticipated revenue streams utilizing the income approach under the discounted cash flow method. As a result, the Company recorded \$33,000 of fair value royalty payments due to Pozen, of which \$24,500 was guaranteed during the years 2014 through 2018 and \$8,500 was contingent on meeting certain revenue targets.

**NOTE 5 – INVENTORIES**

Inventories are stated at the lower of cost or market value. Inventories consist of raw materials, work-in-process and finished goods. The Company has entered into manufacturing and supply agreements for the manufacture or purchase of raw materials and production supplies. The Company's inventories include the direct purchase cost of materials and supplies and manufacturing overhead costs. Inventories exclude product sample inventory, which is included in other current assets and is expensed as a component of sales and marketing expense when provided to physicians or healthcare providers.

The components of inventories as of March 31, 2014 and December 31, 2013, are summarized as follows:

	March 31, 2014	December 31, 2013
Raw materials	\$ 135	\$ 91
Work-in-process	839	522
Finished goods	8,458	8,088
Net inventories	<u>\$ 9,432</u>	<u>\$ 8,701</u>

**NOTE 6 – PREPAID EXPENSES AND OTHER CURRENT ASSETS**

Prepaid expenses and other current assets as of March 31, 2014 and December 31, 2013, consisted of the following:

	March 31, 2014	December 31, 2013
Prepaid debt commitment fee	\$ 4,333	\$ —
Product samples inventory	1,588	1,323
Prepaid software license fees	828	855
Prepaid clinical trial studies	630	688
Prepaid co-pay expenses	523	621
Prepaid marketing expenses	38	381
Prepaid insurance	250	379
Prepaid FDA product and manufacturing fees	429	312
Other prepaid expenses	486	329
Total prepaid and other current assets	<u>\$ 9,105</u>	<u>\$ 4,888</u>

**NOTE 7 – PROPERTY AND EQUIPMENT**

Property and equipment as of March 31, 2014 and December 31, 2013, consisted of the following:

	March 31, 2014	December 31, 2013
Machinery and equipment	\$ 2,367	\$ 2,367
Furniture and fixtures	113	113
Computer equipment	2,245	2,160
Software	1,092	775
Trade show equipment	228	228
Leasehold improvement	873	783
	6,918	6,426
Less-accumulated depreciation	(3,021)	(2,646)
Total property and equipment	<u>\$ 3,897</u>	<u>\$ 3,780</u>

Depreciation expense was \$376 and \$259 for the three months ended March 31, 2014 and 2013, respectively.

**NOTE 8 – INTANGIBLE ASSETS**

The Company's intangible assets consist of developed technology related to the Company's approved products LODOTRA in Europe and RAYOS in the United States and VIMOVO intellectual property rights in the United States.

On November 18, 2013, the Company entered into an asset purchase agreement with AstraZeneca, pursuant to which the Company acquired from AstraZeneca and its affiliates certain intellectual property with respect to VIMOVO and obtained the rights to develop other pharmaceutical products that contain gastroprotective agents in a single fixed combination oral solid dosage form with NSAIDs in the United States. In connection with the Company's acquisition of the U.S. rights to VIMOVO, the Company capitalized \$67,705 for the U.S. intellectual property rights of VIMOVO to intangible assets.

The Company tests its intangible assets for impairment when events or circumstances may indicate that the carrying value of these assets exceeds their fair value. The Company does not believe there have been any circumstances or events that would indicate that the carrying value of any of its intangible assets have been impaired at March 31, 2014 or December 31, 2013.

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As of March 31, 2014 and December 31, 2013, intangible assets consisted of the following:

	March 31, 2014				December 31, 2013			
	Cost Basis	Accumulated Amortization	Currency Translation	Net Book Value	Cost Basis	Accumulated Amortization	Currency Translation	Net Book Value
Developed technology	\$ 84,779	\$ (19,547)	\$ (2,211)	\$ 63,021	\$ 84,779	\$ (17,823)	\$ (2,136)	\$ 64,820
VIMOVO intellectual property	67,705	(4,734)	—	62,971	67,705	(1,431)	—	66,274
Total intangible assets	<u>\$152,484</u>	<u>\$ (24,281)</u>	<u>\$ (2,211)</u>	<u>\$125,992</u>	<u>\$152,484</u>	<u>\$ (19,254)</u>	<u>\$ (2,136)</u>	<u>\$131,094</u>

Amortization expense was \$5,027 and \$1,656 for the three months ended March 31, 2014 and 2013, respectively. As of March 31, 2014, estimated future amortization expense was as follows:

2014 (remainder of the year)	\$ 15,088
2015	20,118
2016	20,118
2017	20,118
2018 and thereafter	50,550
Total	<u>\$125,992</u>

### NOTE 9 – ACCRUED LIABILITIES

Accrued liabilities as of March 31, 2014 and December 31, 2013, consisted of the following:

	March 31, 2014	December 31, 2013
Accrued trade discounts and rebates	\$ 25,264	\$ 8,463
Payroll related expenses	9,160	9,491
Accrued interest	2,685	810
Professional services	2,676	350
Sales and marketing expenses	2,208	1,761
Deferred rent	928	755
Clinical and regulatory expenses	556	488
Consulting services	546	283
Contract manufacturing expenses	161	301
Accrued other	528	1,347
Total accrued liabilities	<u>\$ 44,712</u>	<u>\$ 24,049</u>

### NOTE 10 – FAIR VALUE MEASUREMENTS

The following tables set forth the Company's financial instruments that are measured at fair value on a recurring basis within the fair value hierarchy. Assets and liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The Company's assessment of the significance of a particular input to the fair value measurement in its entirety requires management to make judgments and consider factors specific to the asset or liability. The standard describes three levels of inputs that may be used to measure fair value:

Level 1—Observable inputs such as quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company utilizes the market approach to measure fair value for its money market funds. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

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*Assets and liabilities measured at fair value on a recurring basis*

The following table sets forth the Company's financial assets and liabilities at fair value on a recurring basis as of March 31, 2014 and December 31, 2013:

	As of March 31, 2014			
	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Money market funds	\$86,585	\$ —	\$ —	\$ 86,585
<b>Total assets at fair value</b>	<b>\$86,585</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 86,585</b>
<b>Liabilities:</b>				
Derivative liability	\$ —	\$ —	\$313,440	\$313,440
<b>Total liabilities at fair value</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$313,440</b>	<b>\$313,440</b>
	As of December 31, 2013			
	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Money market funds	\$66,817	\$ —	\$ —	\$ 66,817
<b>Total assets at fair value</b>	<b>\$66,817</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$ 66,817</b>
<b>Liabilities:</b>				
Derivative liability	\$ —	\$ —	\$109,410	\$109,410
<b>Total liabilities at fair value</b>	<b>\$ —</b>	<b>\$ —</b>	<b>\$109,410</b>	<b>\$109,410</b>

In accordance with the pronouncement guidance in ASC 815 "Derivatives and Hedging", the conversion option included within the Convertible Senior Notes was deemed to include an embedded derivative, which required the Company to bifurcate and separately account for the embedded derivative as a separate liability on its condensed consolidated balance sheets. The estimated fair value was derived utilizing the binomial lattice approach for the valuation of convertible instruments. Assumptions used in the calculation included, among others, determining the appropriate credit spread using benchmarking analysis and solving for the implied credit spread, calculating the fair value of the stock component using a discounted risk free rate and borrowing cost and calculating the fair value of the note component using a discounted credit adjusted discount rate. Based on the assumptions used to determine the fair value of the derivative liability associated with the Convertible Senior Notes, the Company concluded that these inputs were Level 3 inputs.

The following table presents the assumptions used by the Company to determine the fair value as of March 31, 2014 and December 31, 2013 of the conversion option embedded in the Convertible Senior Notes:

	March 31, 2014	December 31, 2013
Stock price	\$15.12	\$7.62
Risk free rate	1.59%	1.69%
Borrowing cost	3.5%	5.0% and 3.5%
Weights	Equal weight	Equal weight
Credit spread (in basis points)	1,110	930 and 1,170
Volatility	40.00%	40.00%
Initial conversion price	\$5.36	\$5.36
Remaining time to maturity (in years)	4.6	4.9

At March 31, 2014, the Company conducted a fair value assessment to reflect the market value adjustments for the embedded derivative due to the increase in the Company's common stock value and for changes in the fair value assumptions. During the three months ended March 31, 2014, the Company recorded a \$204,030 loss in its results of operations to properly reflect the fair value of the embedded derivative of \$313,440.

## NOTE 11 – COMMITMENTS AND CONTINGENCIES

### *Lease Obligations*

In September 2011, the Company entered into an office lease agreement for 21,182 square feet of office space in Deerfield, Illinois, which was effective August 31, 2011. The initial term of the lease commenced on December 1, 2011, and expires on June 30, 2018. The minimum net rent was initially approximately \$30 per month during the first year and increases each year during the initial term, up to approximately \$35 per month after the sixth year. The Company has the option to extend the lease for an additional five-year term, which would commence upon the expiration of the initial term. In August 2012, the Company entered into an amendment to the lease agreement to expand the office space available to it by an additional 4,926 square feet in the same Deerfield, Illinois facility as its existing office space. The initial rent on the additional lease is \$7 per month and will increase up to a maximum of \$8 per month after the sixth year. In December 2013, the Company entered into a second amendment to the lease agreement to expand the office space available to it by an additional 8,352 square feet. The two amendments to the lease term coincide with the original lease and run through June 30, 2018. The initial rent on the second amendment is \$12 per month and will increase up to a maximum of \$14 per month after the fifth year.

The Company also leases its offices in Reinach, Switzerland and in Mannheim, Germany. The Reinach office lease rate is \$7 (6 CHF) per month, expiring on May 31, 2015. The Mannheim office lease rate is approximately \$7 (5 Euros) per month, expiring on December 31, 2014.

### *Commitments*

If the proposed Merger between the Company and Vidara is consummated, the Company will be required to pay its investment bankers a fee of \$8,000. An additional \$1,000 non-refundable fee has already been paid to the investment bankers in connection with the delivery of the fairness opinion. The Company also paid Deerfield a commitment fee of \$5,000 upon execution of the Commitment Letter. The Commitment Letter expires on June 30, 2014 unless by June 30, 2014 the Company has provided notice to Deerfield that it commits to borrow at least \$225,000 under the Facility, in which case the Commitment Letter will expire on the earlier of September 30, 2014, or the Closing and the entry into definitive documentation for the Facility with the Deerfield Funds. In the event the commitments under the Commitment Letter are extended to September 30, 2014 and the Company fails to consummate the Merger, the Company will be required to pay an additional fee of \$3,750 to Deerfield. The Company has also agreed to pay customary fees and expenses in connection with obtaining the Facility and has agreed to indemnify Deerfield and the Deerfield Funds if certain losses are incurred by Deerfield and the Deerfield Funds in connection therewith.

### *Annual Purchase Commitments*

In August 2007, the Company entered into a manufacturing and supply agreement with Jagotec AG (“Jagotec”). Under the agreement, Jagotec or its affiliates are required to manufacture and supply RAYOS/LODOTRA exclusively to the Company in bulk. The Company committed to a minimum purchase of RAYOS/LODOTRA tablets from Jagotec for five years from the date of first launch of RAYOS/LODOTRA in a major country, as defined in the agreement, which was in April 2009. At March 31, 2014, the minimum remaining purchase commitment based on tablet pricing in effect under the agreement was \$3,481. The agreement automatically renews on a yearly basis until either party provides two years advance written notice of termination. In April 2013, the agreement automatically renewed, and, therefore, the earliest the current agreement can expire according to this advance notice procedure is April 15, 2016.

In May 2011, the Company entered into a manufacturing and supply agreement with sanofi-aventis U.S., and amended the agreement effective as of September 25, 2013. Pursuant to the agreement, as amended, sanofi-aventis U.S. is obligated to manufacture and supply DUEXIS to the Company in final, packaged form, and the Company is obligated to purchase DUEXIS exclusively from sanofi-aventis U.S. for the commercial requirements of DUEXIS in North America, South America and certain countries and territories in Europe, including the European Union member states and Scandinavia. At March 31, 2014, the Company had a binding purchase commitment to sanofi-aventis U.S. for DUEXIS of \$8,818, which is to be delivered during 2014.

In November 2013, the Company and AstraZeneca entered in a supply agreement pursuant to which AstraZeneca agreed to supply VIMOVO to the Company for commercialization in the United States through December 31, 2014. As of December 5, 2013, the Company has been providing AstraZeneca with a forecast of its supply requirements, including any forecasts for its sublicensees. The first four months of each forecast is a binding purchase commitment and may not be changed without AstraZeneca’s written consent. As of March 31, 2014, the minimum binding purchase commitment to AstraZeneca was \$3,408 and is to be delivered through the fourth quarter of 2014.

### *Royalty Agreements*

In connection with the August 2004 development and license agreement with SkyePharma AG (“SkyePharma”) and Jagotec, a wholly-owned subsidiary of SkyePharma, regarding certain proprietary technology and know-how owned by SkyePharma, Jagotec is entitled to receive a single digit percentage royalty on net sales of RAYOS/LODOTRA and on any sub-licensing income, which includes any payments not calculated based on the net sales of RAYOS/LODOTRA, such as license fees, lump sum and milestone payments. Royalty expense recognized in cost of goods sold for the three months ended March 31, 2014 and 2013 was \$331 and \$169, respectively.

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Under the Pozen license agreement, the Company is required to pay Pozen a flat 10% royalty on net sales of VIMOVO and such other products sold by the Company, its affiliates or sublicensees during the royalty term, subject to minimum annual royalty obligations of \$5,000 in 2014 and \$7,500 each year thereafter, which minimum royalty obligations will continue for each year during which one of Pozen's patents covers such products in the United States and there are no competing products in the United States. The royalty rate may be reduced to a mid-single digit royalty rate as a result of loss of market share to competing products. The Company's obligation to pay royalties to Pozen will expire upon the later of (a) expiration of the last-to-expire of certain patents covering such products in the United States, and (b) ten years after the first commercial sale of such products in the United States.

### *Contingencies*

The Company is subject to claims and assessments from time to time in the ordinary course of business. The Company's management does not believe that any such matters, individually or in the aggregate, will have a material adverse effect on the Company's business, financial condition, results of operations or cash flows.

### *Indemnification*

In the normal course of business, the Company enters into contracts and agreements that contain a variety of representations and warranties and provide for general indemnifications. The Company's exposure under these agreements is unknown because it involves claims that may be made against the Company in the future, but have not yet been made. To date, the Company has not paid any claims or been required to defend any action related to its indemnification obligations. However, the Company may record charges in the future as a result of these indemnification obligations.

In accordance with its amended and restated certificate of incorporation and amended and restated bylaws, the Company has indemnification obligations to its officers and directors for certain events or occurrences, subject to certain limits, while they are serving at the Company's request in such capacity. Additionally, the Company has entered, and intends to continue to enter, into separate indemnification agreements with its directors and executive officers. These agreements, among other things, require the Company to indemnify its directors and executive officers for certain expenses, including attorneys' fees, judgments, fines and settlement amounts incurred by a director or executive officer in any action or proceeding arising out of their services as one of the Company's directors or executive officers, or any of the Company's subsidiaries or any other company or enterprise to which the person provides services at the Company's request. There have been no claims to date and the Company has a director and officer insurance policy that enables it to recover a portion of any amounts paid for future potential claims.

## **NOTE 12 – LEGAL PROCEEDINGS**

On February 15, 2012, the Company received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an Abbreviated New Drug Application ("ANDA") with the FDA for a generic version of DUEXIS, containing 800 mg of ibuprofen and 26.6 mg of famotidine. In March 2012, the Company filed a patent infringement lawsuit in the United States District Court for the District of Delaware against Par Pharmaceutical, Inc. and Par Pharmaceutical Companies, Inc. (collectively, "Par") for filing an ANDA against DUEXIS and seeking an injunction to prevent the approval of Par's ANDA and/or prevent Par from selling a generic version of DUEXIS. In January 2013, the Company filed a second suit against Par in the United States District Court for the District of Delaware claiming patent infringement of additional patents that have been issued for DUEXIS and seeking an injunction to prevent the approval of Par's ANDA and/or prevent Par from selling a generic version of DUEXIS.

On August 21, 2013, the Company entered into a settlement agreement ("Par settlement agreement"), and license agreement ("Par license agreement") with Par relating to its patent infringement litigation. The Par settlement agreement provides for a full settlement and release by both the Company and Par of all claims that were or could have been asserted in the litigation and that arise out of the specific patent issues that were the subject of the litigation, including all resulting damages or other remedies.

Under the Par license agreement, the Company granted Par a non-exclusive license (that is only royalty-bearing in some circumstances) to manufacture and commercialize Par's generic version of DUEXIS in the United States after the generic entry date and to take steps necessary to develop inventory of, and obtain regulatory approval for, but not commercialize, Par's generic version of DUEXIS prior to the generic entry date (collectively, the "License"). The License covers all patents owned or controlled by us during the term of the Par license agreement that would, absent the License, be infringed by the manufacture, use, sale, offer for sale, or importation of Par's generic version of DUEXIS in the United States. Unless terminated sooner pursuant to the terms of the Par license agreement, the License will continue until the last to expire of the licensed patents and/or applicable periods of regulatory exclusivity.

Under the Par license agreement, the generic entry date is January 1, 2023; however, Par may be able to enter the market earlier in certain circumstances. Such events relate to the resolution of potential future third party DUEXIS patent litigation, the entry of other third party generic versions of DUEXIS or certain specific changes in DUEXIS market conditions. Only in the event that Par enters the DUEXIS market due to the specified changes in DUEXIS market conditions will the License become royalty-bearing, with the royalty obligations ceasing upon the occurrence of one of the other events that would have allowed Par to enter the DUEXIS market.

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Under the Par license agreement, the Company also agreed not to sue or assert any claim against Par for infringement of any patent or patent application owned or controlled by the Company during the term of the Par license agreement based on the manufacture, use, sale, offer for sale, or importation of Par's generic version of DUEXIS in the United States.

The Par license agreement may be terminated by the Company if Par commits a material breach of the agreement that is not cured or curable within 30 days after the Company provides notice of the breach. The Company may also terminate the Par license agreement immediately if Par or any of its affiliates initiate certain challenges to the validity or enforceability of any of the licensed patents or their foreign equivalents. In addition, the Par license agreement will terminate automatically upon termination of the Par settlement agreement.

On March 13, 2013, the Company received purported Notice Letters that a Paragraph IV Patent Certification had been filed by Alvogen Pine Brook, Inc. ("Alvogen") advising that Alvogen had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. In the Notice Letters, Alvogen noted that as of March 13, 2013, the FDA had not accepted the ANDA for review. Alvogen has agreed that their Notice Letters do not constitute Notice as described in 21 U.S.C. 355(j)(2)(B).

On July 15, 2013, the Company received a Paragraph IV Patent Certification from Watson Laboratories, Inc.—Florida ("Watson") advising that Watson had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Watson has not advised the Company as to the timing or status of the FDA's review of its filing. On August 26, 2013, the Company, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against Watson, Actavis Pharma, Inc., Andrx Corp., and Actavis, Inc., (collectively "WLF") seeking an injunction to prevent the approval of the ANDA. The lawsuit alleges that WLF has infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124, and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS containing 1 mg, 2 mg, and 5 mg of prednisone prior to the expiration of the patents. The subject patents are listed in the FDA's Approved Drug Products with Therapeutic Equivalence Evaluations, commonly known as the Orange Book. The commencement of the patent infringement lawsuit stays, or bars, FDA approval of WLF's ANDA for 30 months or until an earlier district court decision that the subject patents are not infringed or invalid.

On or about August 12, 2013, the Company received a Notice of Opposition to a European patent covering LODOTRA, EP 2049123, filed by Laboratorios Liconsa, S.A. In the European Union, the grant of a patent may be opposed by one or more private parties.

On September 12, 2013, the Company received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. On October 22, 2013, the Company, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against Par seeking an injunction to prevent the approval of the ANDA. The lawsuit alleged that Par had infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124 and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS prior to the expiration of the patents. The subject patents are listed in the FDA's Orange Book. On November 20, 2013, the Company was notified by counsel for Par that Par Pharmaceutical, Inc. had elected to withdraw its ANDA with the FDA for a generic version of RAYOS containing 2 mg and 5 mg of prednisone. On December 5, 2013, the Company entered into a Stipulation of Dismissal with Par Pharmaceutical, Inc. whereby Par Pharmaceutical, Inc. agreed to withdraw its application to market a generic version of RAYOS.

Currently, patent litigation is pending against five generic companies intending to market VIMOVO before the expiration of patents listed in the Orange Book. These cases are in the District of New Jersey and are grouped in three sets: (i) Dr. Reddy's Laboratories, Inc. ("Dr. Reddy's"); Lupin Pharmaceuticals Inc. ("Lupin"); Anchen Pharmaceuticals Inc. ("Anchen") (collectively, the "DRL cases"); (ii) Mylan Laboratories Limited (collectively the "Mylan cases"); and (iii) Watson Pharma, Inc. (collectively, the "Watson cases"). The Company understands that Dr. Reddy's has entered into a settlement with AstraZeneca with respect to patent rights directed to Nexium for the commercialization of VIMOVO, and that according to the settlement agreement, Dr. Reddy's will not be able to commercialize VIMOVO under AstraZeneca's Nexium patent rights until May 28, 2014. As part of the Company's acquisition of the U.S. rights to VIMOVO, the Company has taken over and is responsible for the patent litigations that include the Pozen patents licensed to the Company under the Pozen license agreement.

The DRL cases were filed on April 21, 2011, July 25, 2011, October 28, 2011, and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. The Company understands the cases arise from Paragraph IV Notice Letters providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The Company understands the Dr. Reddy's notice letters were dated March 11, 2011 and November 12, 2012; the Lupin notice letter was dated June 10, 2011; and the Anchen notice letter was dated September 16, 2011. The court has issued a claims construction order. The DRL cases do not have pretrial deadlines or a trial date set. The Company understands Anchen has recertified under Paragraph III and has filed a motion to dismiss on that basis.

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The Watson cases were filed on May 10, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. The Company understands the cases arise from a March 29, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Watson cases.

The Mylan cases were filed on June 28, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. The Company understands the cases arise from a May 16, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Mylan cases.

### **NOTE 13 – DEBT AGREEMENT**

The Company's outstanding debt balances as of March 31, 2014 and December 31, 2013, consisted of the following:

	March 31, 2014	December 31, 2013
Convertible Senior Notes	\$150,000	\$ 150,000
Debt discount	(37,226)	(39,238)
Long-term debt, net of current maturities	<u>\$112,774</u>	<u>\$ 110,762</u>

#### ***Convertible Senior Notes***

On November 18, 2013, the Company entered into note purchase agreements with investors to issue \$150,000 aggregate principal amount of Convertible Senior Notes. The note purchase agreements contain customary representations, warranties, covenants and closing conditions. The Convertible Senior Notes were issued on November 22, 2013. The Company received net proceeds of \$143,598 from the sale of the Convertible Senior Notes, after deducting fees and expenses of \$6,402. The Convertible Senior Notes are governed by an Indenture, dated as of November 22, 2013, between the Company and U.S. Bank National Association, as trustee. The Convertible Senior Notes bear interest at a rate of 5.00% per year, payable in arrears on May 15 and November 15 of each year, beginning on May 15, 2014. The Convertible Senior Notes will mature on November 15, 2018, unless earlier repurchased or converted.

The Company used a portion of the proceeds from the Convertible Senior Notes to purchase \$18,675 related to a capped call transaction. The capped call transaction is comprised of a net settled purchased call option and a net settled written call option. The Company purchased the call option with an initial strike price of \$5.364, which was equal to the initial conversion price, and sold a call option with a strike price of \$6.705, which is equal to the cap price. The number of options underlying the capped call is 150,000 or the equivalent to the number of \$1,000 Convertible Senior Notes initially issued by the Company.

The Convertible Senior Notes were sold at a price equal to 100% of the principal amount thereof and are convertible at the option of the holders at any time prior to the close of business on the business day immediately preceding August 15, 2018 only under certain conditions. Prior to August 15, 2018, the Convertible Senior Notes will be convertible, at the option of the holders thereof, only under the following circumstances:

- Conversion upon Satisfaction of Sale Price Condition:* During any fiscal quarter beginning after June 30, 2014, if the closing price of the Company's common stock for at least 20 trading days during the period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price on each applicable trading day.
- Conversion upon Satisfaction of Trading Price Condition:* The Convertible Senior Notes can be surrendered for conversion during the five business day period after any five consecutive trading day period in which the trading price per \$1,000 principal amount of Convertible Senior Notes was less than 98% of the product of the last reported sale price of the Company's common stock and the applicable conversion rate on such date.
- Conversion upon Specified Distributions:* If the Company elects to:
  - issue to all or substantially all holders of the Company's common stock any rights, options or warrants (other than in connection with a stockholder rights plan) entitling them, for a period of not more than 45 calendar days after the declaration date for such issuance, to subscribe for or purchase shares of the Company's common stock at a price per share that is less than the average of the last reported sale prices of the Company's common stock for the 10 consecutive trading day period ending on, and including, the trading day immediately preceding the declaration date for such issuance; or



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- ii. distribute to all or substantially all holders of the Company's common stock our assets, securities or rights to purchase our securities, which distribution has a per share value, as reasonably determined by the Company's board of directors or a committee thereof, exceeding 10% of the last reported sale price of the Company's common stock on the trading day preceding the date of announcement for such distribution.
- 4. *Conversion upon Specified Corporate Events:* If (i) a transaction or event that constitutes a fundamental change or a make-whole fundamental change occurs or (ii) the Company is party to a consolidation, merger, binding share exchange, or transfer or lease of all or substantially all of its consolidated assets pursuant to which the Company's common stock would be converted into cash, securities or other assets.

On or after August 15, 2018 until the close of business on the second scheduled trading day immediately preceding the maturity date for the Convertible Senior Notes, holders will be able to convert their Convertible Senior Notes at their option at the conversion rate then in effect at any time, regardless of these conditions.

Subject to certain limitations, the Company may settle conversions of the Convertible Senior Notes by paying or delivering, as the case may be, cash, shares of common stock or a combination of cash and shares of the Company's common stock, at the Company's election. If the Company undergoes a fundamental change prior to the maturity date of the Convertible Senior Notes, the holders may require the Company to repurchase for cash all or any portion of their Convertible Senior Notes at a price equal to 100% of the principal amount of the Convertible Senior Notes to be repurchased, plus accrued and unpaid interest.

The conversion rate for the Convertible Senior Notes will initially be 186.4280 shares of common stock per \$1,000 principal amount of Convertible Senior Notes (equivalent to an initial conversion price of approximately \$5.36 per share of common stock); provided that unless and until the Company obtains stockholder approval to issue more than 13,164,951 shares of its common stock, which is 19.99% of the Company's common stock outstanding on November 18, 2013, upon conversion of the Convertible Senior Notes in accordance with the listing standards of The NASDAQ Global Market, the number of shares of common stock deliverable upon conversion will be subject to a "conversion share cap." Unless and until such stockholder approval is obtained, the Company is required to settle conversions of the Convertible Senior Notes in cash up to their principal amount, shares for any conversion spread, and, if the number of shares deliverable for the conversion spread exceeds the conversion share cap, cash in lieu of shares that would otherwise be deliverable. The conversion rate of the Convertible Senior Notes, and the corresponding conversion price, is subject to adjustment for certain events, but will not be adjusted for accrued and unpaid interest. As of March 31, 2014, the carrying value of the Convertible Senior Notes approximated their fair value.

Pursuant to a number of factors outlined in ASC Topic 815, *Derivative and Hedging*, the conversion option in the Convertible Senior Notes was deemed to include an embedded derivative that required bifurcation and separate accounting. As such, the Company ascertained the value of the conversion option as if separate from the convertible issuance and appropriately recorded that value as a derivative liability. On November 22, 2013, a derivative liability and a corresponding debt discount in the amount of \$40,110 were recorded. The debt discount is being charged to interest expense ratably over the life of the convertible debt. The effective interest rate computed on the Convertible Senior Notes was 11.22%.

The derivative liability is subject to revaluation on a quarterly basis to reflect the market value change of the embedded conversion option. At December 31, 2013, the Company conducted a fair value assessment of the embedded derivative due primarily to changes in the Company's common stock value. As a result of the fair value assessment, the Company recorded a \$69,300 expense in its results of operations for the three and twelve months ended December 31, 2013 to properly reflect the fair value of the embedded derivative of \$109,410 as of December 31, 2013. At March 31, 2014, the Company conducted a subsequent fair value assessment to reflect the market value adjustments for the embedded derivative due to the increase in the Company's common stock value and for changes in the fair value assumptions. During the three months ended March 31, 2014, the Company recorded a \$204,030 loss in its results of operations to properly reflect the fair value of the embedded derivative of \$313,440.

Upon receiving stockholder approval, the derivative liability will be re-measured on such date of approval to determine the fair value. Any gains or losses as a result of the re-measurement of the derivative liability will be recorded in the Company's results of operations during that period and the entire fair value of the derivative liability will be recorded to the Company's additional paid-in capital upon conversion.

### ***Commitment Letter***

On March 18, 2014, the Company entered into the Commitment Letter with Deerfield and certain Deerfield Funds pursuant to which the Deerfield Funds have committed to provide up to \$250,000 of senior secured loans to finance the Merger. The commitment to provide the Facility is subject to certain conditions, including the negotiation of definitive documentation and other customary closing conditions consistent with the Merger Agreement. The receipt of funding under the Facility is not a condition to the obligations we have under the terms of the Merger Agreement.

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The Company also paid Deerfield a commitment fee of \$5,000 upon execution of the Commitment Letter. The \$5,000 commitment fee paid to Deerfield was capitalized as a prepaid expense and is being amortized to expense through June 30, 2014. The Commitment Letter expires on June 30, 2014 unless by June 30, 2014 the Company has provided notice to Deerfield that it commits to borrow at least \$225,000 under the Facility, in which case the Commitment Letter will expire on the earlier of September 30, 2014, or the Closing and the entry into definitive documentation for the Facility with the Deerfield Funds. In the event the commitments under the Commitment Letter are extended to September 30, 2014 and the Company fails to consummate the Merger, the Company will be required to pay an additional fee of \$3,750 to Deerfield. The Company has also agreed to pay customary fees and expenses in connection with obtaining the Facility and has agreed to indemnify Deerfield and the Deerfield Funds if certain losses are incurred by Deerfield and the Deerfield Funds in connection therewith.

**NOTE 14 – RELATED PARTY TRANSACTIONS**

The Company has entered into a consulting agreement with a former stockholder who previously served as a director of Horizon Pharma USA. In addition, the Company's wholly-owned subsidiary, Horizon Pharma AG, has entered into a consulting agreement with a former owner and majority shareholder of Nitec. For the three months ended March 31, 2014 and 2013, the Company paid \$122 and \$197, respectively, in consulting fees to the related parties.

**NOTE 15 – INCOME TAXES**

The Company accounts for income taxes based upon an asset and liability approach. Deferred tax assets and liabilities represent the future tax consequences of the differences between the financial statement carrying amounts of assets and liabilities versus the tax basis of assets and liabilities. Under this method, deferred tax assets are recognized for deductible temporary differences, and operating loss and tax credit carryforwards. Deferred tax liabilities are recognized for taxable temporary differences. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The impact of tax rate changes on deferred tax assets and liabilities is recognized in the year that the change is enacted.

The following table presents the benefit for income taxes for the three months ended March 31, 2014 and 2013:

	For the Three Months Ended March 31,	
	2014	2013
Net loss before benefit for income taxes	\$ (207,355)	\$ (23,052)
Benefit for income taxes	(1,105)	(881)
Net loss	<u>\$ (206,250)</u>	<u>\$ (22,171)</u>

During the three months ended March 31, 2014 and 2013, benefit for incomes taxes was \$1,105 and \$881, respectively. The increase in benefit for income taxes during the first quarter of 2014 was primarily due to a higher net loss compared to the prior year period. Additionally, during the three months ended March 31, 2013, the Company recorded an additional benefit for income taxes of \$831 associated with a reduction in the Company's deferred tax valuation allowance resulting from a determination that a portion of deferred tax assets associated with deferred revenues from milestone payments would be realized in future years.

At March 31, 2014, the Company had a net deferred tax liability of \$2,903 primarily related to temporary differences associated with its intangible assets. During the three months ended March 31, 2014, the Company recorded a \$204,030 loss on the derivative revaluation in connection with the increase in the fair value of the embedded derivative associated with the Convertible Senior Notes. The loss on derivative revaluation was a permanent tax difference and is not deductible for income tax reporting purposes.

**NOTE 16 – STOCKHOLDERS' EQUITY**

During the three months ended March 31, 2014, the Company issued an aggregate of 5,154,142 shares of common stock upon the cash exercise of warrants and the Company received proceeds of \$23,544 representing the aggregate exercise price for such warrants. In addition, warrants to purchase an aggregate of 41,631 shares of the Company's common stock were exercised in cashless exercises, resulting in the issuance of 34,774 shares of common stock.

## NOTE 17 – EQUITY INCENTIVE PLANS

### Employee Stock Purchase Plan

In July 2010, the Company's board of directors adopted the 2011 Employee Stock Purchase Plan (the "2011 ESPP"). In June 2011, the Company's stockholders approved the 2011 ESPP, and it became effective upon the signing of the underwriting agreement related to the Company's initial public offering in July 2011. The Company reserved a total of 463,352 shares of common stock for issuance under the 2011 ESPP. The 2011 ESPP provides that an additional number of shares will automatically be added to the shares authorized for issuance under the 2011 ESPP each year on January 1, until 2021. The number of shares added each year will be equal to the least of: (a) 4% of the total number of shares of common stock outstanding on December 31 of the preceding calendar year; (b) 1,053,074 shares of common stock; or (c) a number of shares of common stock that may be determined each year by the Company's board of directors that is less than (a) and (b). Subject to certain limitations, the Company's employees may elect to have 1% to 15% of their compensation withheld through payroll deductions to purchase shares of common stock under the 2011 ESPP. Employees purchase shares of common stock at a price per share equal to 85% of the lower of the fair market value at the start or end of the six-month offering period.

On December 5, 2013, pursuant to the terms of the 2011 ESPP, the Company's board of directors approved an increase in the number of shares available for issuance under the 2011 ESPP of 1,053,074 shares, effective January 1, 2014. As of March 31, 2014, 350,547 shares have been issued and an aggregate of 1,465,879 shares of common stock were authorized and available for future grants under the 2011 ESPP.

### Stock-Based Compensation Plans

In October 2005, the Company adopted the 2005 Stock Plan (the "2005 Plan"). The 2005 Plan provides for the granting of stock options to employees and consultants of the Company. Options granted under the 2005 Plan may be either incentive stock options or nonqualified stock options. Upon the signing of the underwriting agreement related to the Company's initial public offering, on July 28, 2011, no further option grants were made under the 2005 Plan. As of July 28, 2011, the 460,842 shares of common stock reserved for future issuance and the 1,304,713 shares of common stock reserved for future issuance upon the exercise of options outstanding under the 2005 Plan were transferred to the 2011 Equity Incentive Plan (the "2011 EIP"), as described below. All stock options granted under the 2005 Plan prior to the offering continue to be governed by the terms of the 2005 Plan.

In July 2010, the Company's board of directors adopted the 2011 EIP. In June 2011, the Company's stockholders approved the 2011 EIP, and it became effective upon the signing of the underwriting agreement related to the Company's initial public offering on July 28, 2011. The 2011 EIP had an initial reserve of 3,366,228 shares of common stock, including 460,842 shares of common stock previously reserved for future issuance under the 2005 Plan, 1,304,713 shares of common stock reserved for future issuance upon the exercise of options outstanding under the 2005 Plan as of the 2011 EIP's effective date and 1,600,673 new shares of common stock reserved. The 2011 EIP provides that an additional number of shares will automatically be added to the shares authorized for issuance each year on January 1, until 2021. The number of shares added each year will be equal to the least of: (a) 5% of the total number of shares of common stock outstanding on December 31 of the preceding calendar year; (b) 1,474,304 shares of common stock; or (c) a number of shares of common stock that may be determined each year by the Company's board of directors that is less than (a) and (b). On December 5, 2013, pursuant to the terms of the Company's 2011 EIP, the Company's board of directors approved an increase in the number of shares available for issuance under the 2011 EIP of 1,474,304 shares, effective January 1, 2014. As of March 31, 2014, there were 344,275 shares available for future grants under the 2011 EIP, not including the additional shares available for grant pursuant to Rule 5635(c)(4) of the NASDAQ Listing Rules ("Rule 5635(c)(4)") described below.

On November 7, 2013, November 16, 2013 and March 3, 2014, the Company's board of directors approved amendments to the Company's 2011 EIP to reserve an additional 200,000 shares, 800,000 shares and 730,000 shares of the Company's common stock to be used exclusively for grants of awards to individuals who were not previously employees or directors of the Company (or following a bona fide period of non-employment with the Company), as an inducement material to the individual's entry into employment with the Company within the meaning of Rule 5635(c)(4). On January 10, 2014, the Company's board of directors approved an amendment to the 2011 EIP to increase the number of shares available for issuance under the 2011 EIP by 703,400 shares (the "January 2014 amendment"), with such increase to the number of shares available for issuance under the 2011 EIP subject to stockholder approval of the January 2014 amendment. As of March 31, 2014, there were 438,400 shares available for future grants under the 2011 EIP pursuant to Rule 5635(c)(4).

Under the 2011 EIP, the board of directors, or a committee of the board of directors, may grant incentive and nonqualified stock options, stock appreciation rights, restricted stock units, or restricted stock awards to employees, directors and consultants to the Company or any subsidiary of the Company. Under the terms of the 2011 EIP, the exercise price of stock options may not be less than 100% of the fair market value on the date of grant and their term may not exceed ten years.

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**Stock Option Plans**

The following table summarizes stock option activity during the three months ended March 31, 2014:

	<b>Options</b>	<b>Weighted Average Exercise Price</b>
Outstanding as of December 31, 2013	4,411,080	\$ 6.47
Granted	1,500,900	\$ 9.55
Exercised	(114,925)	\$ 5.79
Forfeited	(92,376)	\$ 5.28
Outstanding as of March 31, 2014	<u>5,704,679</u>	\$ 7.31
Exercisable as of March 31, 2014	<u>2,210,466</u>	\$ 9.22

The fair value of each stock option award is estimated on the date of grant using the Black-Scholes option pricing model. The determination of the fair value of each stock option is affected by the Company's stock price on the date of grant, as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the Company's expected stock price volatility over the expected life of the awards and actual and projected stock option exercise behavior. The weighted average fair value per share of stock option awards granted during the three months ended March 31, 2014 and 2013, and assumptions used to value stock options, are as follows:

	<b>For the Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
Dividend yield	—	—
Risk-free interest rate	2.0%	1.0%
Weighted average volatility	83.0%	88.3%
Expected life (in years)	6.0	6.0
Weighted average grant date fair value per share of options granted	\$ 6.75	\$ 1.74

*Dividend yields*

The Company has never paid dividends and does not anticipate paying any dividends in the near future.

*Risk-Free Interest Rate*

The Company determined the risk-free interest rate by using a weighted average assumption equivalent to the expected term based on the U.S. Treasury constant maturity rate as of the date of grant.

*Volatility*

The Company used an average historical stock price volatility of comparable companies to be representative of future stock price volatility, as the Company did not have sufficient trading history for its common stock.

*Expected Term*

Given the Company's limited historical exercise behavior, the expected term of options granted was determined using the "simplified" method since the Company does not have sufficient historical exercise data to provide a reasonable basis upon which to estimate the expected term. Under this approach, the expected term is presumed to be the average of the vesting term and the contractual life of the option.

During the three months ended March 31, 2013, the Company utilized a forfeiture rate of 5% for estimating the forfeitures of stock options granted. During the three months ended March 31, 2014, the Company reassessed its forfeiture rate based on actual historical experience and subsequently utilized a forfeiture rate that ranges from 5% to 15% based on the stratification of various employee grant categories.

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[Table of Contents](#)**Restricted Stock Units**

The following table summarizes restricted stock unit activity during the three months ended March 31, 2014:

	<u>Number of Units</u>	<u>Weighted Average Grant-Date Fair Value Per Units</u>
Outstanding as of December 31, 2013	833,001	\$ 2.86
Granted	766,300	\$ 8.85
Vested	<u>(161,775)</u>	\$ 2.40
Outstanding as of March 31, 2014	<u>1,437,526</u>	\$ 6.10

The following table summarizes stock-based compensation expense included in the Company's condensed consolidated statements of operations for the three months ended March 31, 2014 and 2013:

	<u>For the Three Months Ended March 31,</u>	
	<u>2014</u>	<u>2013</u>
<b>Stock-based compensation expense:</b>		
Research and development	\$ 300	\$ 282
Sales and marketing	584	280
General and administrative	<u>1,043</u>	<u>517</u>
Net effect of stock-based compensation expense on net loss	<u>\$ 1,927</u>	<u>\$ 1,079</u>

The Company estimates that, as of March 31, 2014, pre-tax compensation expense was \$20,829 for all unvested stock-based awards, including both stock options and restricted stock units that will be recognized through the second quarter of 2017. The Company expects to satisfy the exercise of stock options and future distribution of shares of restricted stock by issuing new shares of its common stock which have been reserved under the 2011 Plan.

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

*The following discussion and analysis should be read in conjunction with our condensed consolidated financial statements and the related notes that appear elsewhere in this report. This discussion contains forward-looking statements reflecting our current expectations that involve risks and uncertainties which are subject to safe harbors under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, or the Exchange Act. These forward-looking statements include, but are not limited to, statements concerning our strategy and other aspects of our future operations, future financial position, future revenues, projected costs, expectations regarding demand and acceptance for our products, growth opportunities and trends in the market in which we operate, prospects, plans and objectives of management and statements related to the anticipated completion of the proposed merger with Vidara Therapeutics International Ltd. The words "anticipates", "believes", "estimates", "expects", "intends", "may", "plans", "projects", "will", "would" and similar expressions are intended to identify forward-looking statements, although not all forward-looking statements contain these identifying words. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. These forward-looking statements involve risks and uncertainties that could cause our actual results to differ materially from those in the forward-looking statements, including, without limitation, the risks set forth in Part II, Item 1A, "Risk Factors" in this report and in our other filings with the Securities and Exchange Commission, or SEC. We do not assume any obligation to update any forward-looking statements.*

*(Dollars are presented in thousands except share data or unless otherwise stated)*

### OUR BUSINESS

We are a specialty pharmaceutical company commercializing DUEXIS®, VIMOVO® and RAYOS®/LODOTRA®, each of which targets unmet therapeutic needs in arthritis, pain and inflammatory diseases. We developed DUEXIS and RAYOS/LODOTRA, and acquired the U.S. rights to VIMOVO from AstraZeneca AB, or AstraZeneca, in November 2013. We market our products in the United States through our field sales force of approximately 290 representatives. Our strategy is to develop, acquire or in-license additional innovative medicines or acquire companies where we can execute a targeted commercial approach among specific target physicians, such as primary care physicians, orthopedic surgeons and rheumatologists, while taking advantage of our commercial strengths and the infrastructure that has been put in place.

On April 23, 2011, the U.S. Food and Drug Administration, or FDA, approved DUEXIS, a proprietary tablet formulation containing a fixed-dose combination of ibuprofen and famotidine in a single pill. DUEXIS is indicated for the relief of signs and symptoms of rheumatoid arthritis, or RA, osteoarthritis, or OA, and to decrease the risk of developing upper gastrointestinal ulcers in patients who are taking ibuprofen for these indications. We began detailing DUEXIS to physicians in December 2011. In June 2012, we licensed DUEXIS rights in Latin America to Grünenthal S.A., a private company focused on the promotion of pain products.

Our second approved product in the United States, RAYOS, known as LODOTRA outside the United States, is a proprietary delayed-release formulation of low-dose prednisone for the treatment of moderate to severe, active RA in adults, particularly when accompanied by morning stiffness. On July 26, 2012, the FDA approved RAYOS for the treatment of RA, polymyalgia rheumatica, or PMR, psoriatic arthritis, ankylosing spondylitis, or AS, asthma and chronic obstructive pulmonary disease and a number of other conditions. We are focusing our promotion of RAYOS in the United States on rheumatology indications, including RA and PMR. We began detailing RAYOS to a subset of U.S. rheumatologists in December 2012 and began the full launch in late January 2013 to the majority of U.S. rheumatologists and key primary care physicians. LODOTRA is currently marketed outside the United States by our distribution partner, Mundipharma International Corporation Limited, or Mundipharma.

On November 18, 2013, we entered into agreements with AstraZeneca pursuant to which we acquired from AstraZeneca and its affiliates certain intellectual property and other assets, and assumed from AstraZeneca and its affiliates certain liabilities, each with respect to VIMOVO, and obtained rights to develop other pharmaceutical products that contain gastroprotective agents in a single fixed combination oral solid dosage form with non-steroidal anti-inflammatory drugs, or NSAIDs, in the United States. VIMOVO (naproxen/esomeprazole magnesium) is a proprietary fixed-dose multi-layer delayed-release tablet combining an enteric-coated naproxen, an NSAID, core and an immediate-release esomeprazole, a proton pump inhibitor, layer surrounding the core. VIMOVO was originally developed by Pozen Inc., or Pozen, together with AstraZeneca pursuant to an exclusive global collaboration and license agreement under which AstraZeneca and Pozen agreed to co-develop VIMOVO and AstraZeneca obtained exclusive rights to commercialize VIMOVO worldwide. On April 30, 2010, the FDA approved VIMOVO for the relief of the signs and symptoms of OA, RA, and AS and to decrease the risk of developing gastric ulcers in patients at risk of developing NSAID associated gastric ulcers.

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Under the asset purchase agreement with AstraZeneca, we acquired certain existing assets and rights necessary to commercialize VIMOVO in the United States including, among other things, the investigational new drug application and new drug application for VIMOVO in the United States, AstraZeneca's interest in certain patents covering VIMOVO in the United States and certain promotional materials and records related to VIMOVO in the United States. In addition, AstraZeneca assigned to us its amended and restated collaboration and license agreement for the United States with Pozen, pursuant to which AstraZeneca has in-licensed from Pozen certain patents and know-how of Pozen covering VIMOVO in the United States.

In December 2013, as a result of the acquisition of the U.S. rights to VIMOVO, we recognized revenues under our transition agreement with AstraZeneca. We announced the availability of Horizon-labeled VIMOVO on January 2, 2014, at which time we also began promotion with our primary care sales force.

On March 18, 2014, we, Vidara Therapeutics Holdings LLC, a Delaware limited liability company, or Holdings, Vidara Therapeutics International Ltd., an Irish private limited company, or Vidara, Hamilton Holdings (USA), Inc., a Delaware corporation and an indirect wholly-owned subsidiary of Vidara, or U.S. HoldCo, and Hamilton Merger Sub, Inc., a Delaware corporation and a wholly-owned subsidiary of U.S. HoldCo, or Merger Sub, entered into a Transaction Agreement and Plan of Merger, or the Merger Agreement. The Merger Agreement provides that, upon the terms and subject to the conditions set forth in the Merger Agreement, Merger Sub will merge with and into Horizon Pharma, Inc., with Horizon Pharma, Inc. continuing as the surviving corporation and as a wholly-owned, indirect subsidiary of Vidara, or the Merger, with Vidara converting to a public limited company and changing its name to Horizon Pharma plc, or New Horizon. New Horizon will be organized under the laws of Ireland. Upon consummation of the Merger, or the Closing, our security holders (excluding the holders of the convertible notes) will own approximately 74% of New Horizon and Holdings will own approximately 26% of New Horizon. At the Closing, Holdings will receive a cash payment of \$200,000, plus the cash of Vidara and its subsidiaries as of Closing, less the indebtedness of Vidara and its subsidiaries and transaction expenses of Vidara and its subsidiaries paid by New Horizon at or following the Closing, subject to certain adjustments.

Vidara is a privately-held specialty pharmaceutical company with operations in Dublin, Ireland and the United States. Vidara markets ACTIMMUNE®, a bioengineered form of interferon gamma-1b, a protein that acts as a biologic response modifier, in the United States. ACTIMMUNE is approved by the FDA for use in children and adults with chronic granulomatous disease, or CGD, and severe, malignant osteopetrosis, or SMO. ACTIMMUNE is indicated for reducing the frequency and severity of serious infections associated with CGD and for delaying time to disease progression in patients with SMO.

The New Horizon ordinary shares to be issued to our stockholders will be registered with the SEC and are expected to be listed on NASDAQ. We have secured a \$250,000 bridge loan commitment from Deerfield Management Company, L.P., pending potential execution of our final financing plans.

The Merger, which has been approved by the boards of directors of the parties, is subject to approval by our stockholders and the satisfaction of customary closing conditions. The Merger is expected to close mid-year 2014.

**RESULTS OF OPERATIONS****Comparison of Three Months Ended March 31, 2014 and 2013**

The summary of selected financial data table below should be referenced in connection with a review of the following discussion of our results of operations for the three months ended March 31, 2014, compared to the three months ended March 31, 2013.

	Three Months Ended		Increase / (Decrease)
	March 31,		
	2014	2013	
Gross sales	\$ 92,248	\$ 10,698	\$ 81,550
Sales discounts and allowances	(40,322)	(2,005)	38,317
Net sales	51,926	8,693	43,233
Cost of good sold	7,619	3,769	3,850
Gross profit	44,307	4,924	39,383
Operating expenses			
Research and development	2,833	2,198	635
Sales and marketing	28,695	16,328	12,367
General and administrative	11,192	4,942	6,250
Total operating expenses	42,720	23,468	19,252
Operating income (loss)	1,587	(18,544)	20,131
Other (expense) income			
Interest expense, net	(4,207)	(3,603)	604
Foreign exchange loss	(38)	(905)	(867)
Loss on derivative fair value	(204,030)	—	204,030
Other expense	(667)	—	667
Total other expense, net	(208,942)	(4,508)	204,434
Loss before benefit for income taxes	(207,355)	(23,052)	184,303
Benefit for income taxes	(1,105)	(881)	224
Net loss	<u>\$(206,250)</u>	<u>\$(22,171)</u>	<u>\$184,079</u>

*Sales.* During the three months ended March 31, 2014, gross and net sales were \$92,248 and \$51,926, respectively, compared to \$10,698 and \$8,693, respectively, during the three months ended March 31, 2013.

DUEXIS gross and net sales during the three months ended March 31, 2014 were \$36,471 and \$13,923, respectively, after deducting sales discounts and allowances of \$22,548, including co-pay assistance costs of \$11,268, compared to gross and net sales of \$6,726 and \$4,894, respectively, during the three months ended March 31, 2013. The increase in DUEXIS sales during the three months ended March 31, 2014 compared to the prior year period was primarily the result of prescription volume growth driven by expansion of the field sales organization and product price increases implemented during the course of 2013 and in January 2014. DUEXIS sales discounts and allowances increased from the prior year period and from the fourth quarter of 2013 primarily due to higher co-pay costs as a result of our strategy of keeping patients in spite of higher deductibles and managed care plan changes at the beginning of the calendar year, and higher managed care rebates in the quarter driven by channel mix. We expect a moderating of DUEXIS sales discounts and allowances in the coming quarters as patients meet their plan deductibles and co-pay costs are reduced.

VIMOVO gross and net sales during the three months ended March 31, 2014 were \$50,010 and \$34,007, respectively, after deducting sales discounts and allowances of \$16,003, including co-pay assistance costs of \$4,587. We began promotion of VIMOVO with our rheumatology sales force on November 26, 2013 and began commercialization through our primary care sales force on January 2, 2014 as the installed base of prior VIMOVO prescribers were very responsive to active promotion for the first time in years and the commercial business outgrew the decline of the government and cash business.

RAYOS gross and net sales were \$5,082 and \$3,307, respectively, during the three months ended March 31, 2014 after deducting sales discounts and allowances of \$1,775, including co-pay assistance costs of \$850, compared to gross and net sales of \$418 and \$348, respectively, during the three months ended March 31, 2013. The increase in RAYOS sales during the three months ended March 31, 2014 compared to the prior year period was primarily attributable to increased volume driven by the expansion of our sales force focused on RAYOS and product price increases implemented during the course of 2013 and in January 2014.

LODOTRA gross and net sales during the three months ended March 31, 2014 were \$685 and \$689, respectively, with net sales including the effect of a favorable trade allowance adjustment of \$5, compared to gross and net sales of \$3,554 and \$3,452, respectively, during the three months ended March 31, 2013. The decrease in LODOTRA sales during the three months ended March 31, 2014 compared to the prior year period was the result of timing of product shipments to our European distribution partner, Mundipharma. LODOTRA sales to Mundipharma occur at the time we ship product based on Mundipharma's estimated requirements. Accordingly, LODOTRA sales are not linear or directly tied to Mundipharma sales to the market and can therefore fluctuate from quarter to quarter.



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*Sales discounts and allowances.* During the three months ended March 31, 2014, sales discounts and allowances were \$40,322 compared to \$2,005 during the three months ended March 31, 2013. As a percentage of gross product sales, sales discounts and allowances increased to 44% during the three months ended March 31, 2014 from 19% during the three months ended March 31, 2013. The increase in sales discounts and allowances was attributable to product price increases implemented during the course of 2013 and a significant increase in product sales during the three months ended March 31, 2014, which resulted in a corresponding increase in customer discounts and rebates, including distribution service fees and prompt pay allowances. Co-pay assistance costs increased \$15,846 during the three months ended March 31, 2014 compared to the prior year period as a result of a larger number of prescriptions being filled by patients and product price increases implemented during the course of 2013, which resulted in us increasing the amount of co-pay assistance we would provide to a patient. Additionally, customer discounts and rebates increased \$14,178 during the three months ended March 31, 2014 compared to the prior year period as a result of increased sales volumes, channel mix and product price increases implemented during 2013, offset by distribution service fee rebates earned as a result of gains earned by wholesalers for inventories held at the time of wholesaler price increases. The following table presents our sales discounts and allowances for the three months ended March 31, 2014 and 2013:

	For the Three Months Ended March 31,	
	2014	2013
Gross product sales	\$ 92,248	\$ 10,698
Customer discounts and rebates	14,899	721
Co-pay assistance	16,705	859
Government rebates and chargebacks	5,048	283
Product returns and prompt pay allowances	3,670	142
Sales discounts and allowances	40,322	2,005
Product sales, net	\$ 51,926	\$ 8,693
Sales discounts and allowances, as a percent of gross product sales	44%	19%

*Cost of Goods Sold.* Cost of goods sold increased \$3,850 to \$7,619 during the three months ended March 31, 2014, from \$3,769 during the three months ended March 31, 2013. The increase in cost of goods sold was primarily due to an increase in DUEXIS product shipments, cost of goods sold associated with our launch of VIMOVO in the United States in the first quarter of 2014, and \$3,303 in higher intangible amortization expense during the first quarter of 2014. The increase in intangible amortization expense was related to our acquisition of the U.S. rights to VIMOVO from AstraZeneca in the fourth quarter of 2013, which resulted in us capitalizing \$67,705 in intangible assets related to VIMOVO intellectual property rights. For the three months ended March 31, 2014 and 2013, intangible amortization expense accounted for 66% and 44%, respectively, of total cost of goods sold. At the time of our acquisition of the U.S. rights to VIMOVO, we estimated the fair value of contingent royalties payable to Pozen using an income approach under the discounted cash flow method, which included revenue projections and other assumptions we made to determine the fair value. If we were to significantly overperform or underperform against our original revenue projections or it became necessary to make changes to our assumptions, we would be required to reassess the fair value of the contingent royalties payable to Pozen. Any adjustments to fair value would be recorded in the period such adjustment was made as either a charge or credit to royalties payable, which is part of cost of goods sold, in accordance with our established accounting policies, and could impact the reported operating results in the period the adjustment was made.

*Research and Development Expenses.* Research and development expenses increased \$635 to \$2,833 during the three months ended March 31, 2014, from \$2,198 during the three months ended March 31, 2013. The increase in research and development expenses during the first quarter of 2014 was primarily associated with \$226 in higher consulting fees and \$349 in increased clinical expenses.

*Sales and Marketing Expenses.* Sales and marketing expenses increased \$12,367 to \$28,695 during the three months ended March 31, 2014, from \$16,328 during the three months ended March 31, 2013. The increase in sales and marketing expenses was primarily attributable to an increase of \$8,659 in salaries and benefits expenses associated with increased staffing of our field sales force, \$2,467 in higher marketing and commercialization expenses, a \$847 increase in consulting costs and \$581 in higher facility expenses.

*General and Administrative Expenses.* General and administrative expenses increased \$6,250 to \$11,192 during the three months ended March 31, 2014, from \$4,942 during the three months ended March 31, 2013. The increase in general and administrative expenses was primarily due to \$5,222 in higher consulting and professional fees, of which \$4,049 was incurred in connection with investment advisory and professional service fees related to our pending merger with Vidara and \$1,020 related to higher salaries and benefits expense during the three months ended March 31, 2014 as a result of increased staffing.

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*Interest Expense, Net.* Interest expense, net increased \$604 to \$4,207 during the three months ended March 31, 2014, from \$3,603 during the three months ended March 31, 2013. The increase in interest expense, net was primarily attributable to higher debt discount expenses of \$1,420, partially offset by \$816 in lower interest expense as a result of lower borrowing costs under our 5.00% Convertible Senior Notes due 2018, or the Convertible Senior Notes, during the three months ended March 31, 2014 compared to our borrowing costs during the three months ended March 31, 2013 under our prior senior secured loan facility which we retired in November 2013.

*Foreign Exchange Loss.* During the three months ended March 31, 2014 and 2013, we reported a foreign exchange loss of \$38 and \$905, respectively. The decrease in foreign exchange loss during the first quarter of 2014 was primarily due to a decrease in U.S. dollar denominated transactions for our Horizon Pharma AG subsidiary, whose functional currency is the Euro.

*Loss on Derivative Revaluation.* During the three months ended March 31, 2014, we recorded a \$204,030 non-cash charge related to the increase in the fair value of the embedded derivative associated with our Convertible Senior Notes. The increase in loss on the derivative revaluation was primarily due to an increase in the market value of our common stock during the three months ended March 31, 2014. The loss on derivative revaluation was a permanent tax difference and was not deductible for income tax reporting purposes.

*Income Tax Benefit.* Income tax benefit increased \$224 to \$1,105 during the three months ended March 31, 2014, from \$881 during the three months ended March 31, 2013. The increase in benefit for income taxes during the first quarter of 2014 was primarily due to a higher net loss compared to the three months ended March 31, 2013. Additionally, during the three months ended March 31, 2013, we recorded an additional benefit for income taxes of \$831 associated with a reduction in our deferred tax valuation allowance resulting from a determination that a portion of deferred tax assets associated with deferred revenues from milestone payments would be realized in future years.

*Net Loss.* Net loss increased \$184,079 to \$206,250 during the three months ended March 31, 2014, from \$22,171 during the three months ended March 31, 2013, primarily as a result of the loss on derivative revaluation, which was partially offset by an increase in gross profit related to higher product sales in the three months ended March 31, 2014.

### **Summary of Critical Accounting Policies**

The methods, estimates and judgments that we use in applying our critical accounting policies have a significant impact on the results that we report in our financial statements. Some of our accounting policies require us to make difficult and subjective judgments, often as a result of the need to make estimates regarding matters that are inherently uncertain.

We have identified the accounting policies and estimates listed below as those that we believe require management's most subjective and complex judgments in estimating the effect of inherent uncertainties. This section should also be read in conjunction with Note 2, "Summary of Significant Accounting Policies," in the notes to our condensed consolidated financial statements included in this report, which includes a discussion of these and other significant accounting policies.

#### *Revenue Recognition*

Revenue is recognized when all of the following criteria are met: persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; the price is fixed or determinable; and collectability is reasonably assured. Some of our agreements contain multiple elements and in accordance with these agreements, we may be eligible for upfront license fees, marketing or commercial milestones and payment for product deliveries.

#### *Revenue from product deliveries*

We recognize revenue from the delivery of our products when delivery has occurred, title has transferred, the selling price is fixed or determinable, the right of return no longer exists (which is the earlier of product being dispensed through patient prescriptions or the expiration of the right of return) or product returns can be reasonably estimated, collectability is reasonably assured and we have no further performance obligations. Due to our ability to reasonably estimate and determine allowances for product returns, rebates and discounts, we recognize DUEXIS and RAYOS revenue at the point of sale to the wholesale pharmaceutical distributors and retail chains. We also recognize VIMOVO revenue at the point of sale, consistent with our revenue recognition of DUEXIS and RAYOS, given the availability of prior VIMOVO product return data.

#### *Revenue from upfront license fees*

We recognize revenues from the receipt of non-refundable, upfront license fees. In situations where the licensee is able to obtain stand-alone value from the license and no further performance obligations exist on our part, revenues are recognized on the earlier of when payments are received or collection is assured. Where continuing involvement by us is required in the form of technology transfer, product manufacturing or technical support, revenues are deferred and recognized over the term of the agreement.

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### *Revenue from milestone receipts*

Milestone payments are recognized as revenue based on achievement of the associated milestones, as defined in the relevant agreements. Revenue from a milestone achievement is recognized when earned, as evidenced by acknowledgment from our partner, provided that (1) the milestone event is substantive and its achievability was not reasonably assured at the inception of the agreement, (2) the milestone represents the culmination of an earnings process and (3) the milestone payment is non-refundable. If all of these criteria are not met, revenue from the milestone achievement is recognized over the remaining minimum period of our performance obligations under the agreement.

### *Customer-Related Accruals and Allowances*

#### *DUEXIS, VIMOVO and RAYOS Product Sales Discounts and Allowances*

We make allowances for product returns, rebates and discounts at the time of sale to wholesale pharmaceutical distributors and national and regional retail chains. We are also required to make significant judgments and estimates in determining some of these allowances. If actual results differ from our estimates, we will be required to make adjustments to these allowances in the future.

### *Customer Discounts and Rebates*

#### *Product Launch Discounts*

We have offered additional discounts to wholesale distributors for product purchased at the time of product launch. We have recorded these discounts as an allowance against accounts receivable and a reduction of revenue when orders were placed.

#### *Customer Rebates*

We participate in certain commercial rebate programs. Under these rebate programs, we pay a rebate to the commercial entity or third-party administrator of the program. We accrue estimated rebates based on contract prices, estimated percentages of product sold to qualified patients and estimated levels of inventory in the distribution channel and record the rebate as a reduction of revenue.

#### *Distribution Service Fees*

We include distribution service fees paid to our wholesalers for distribution and inventory management services as a reduction to revenue. The estimates are based on contractually determined fees, typically as a percentage of revenue.

### *Government Rebates and Chargebacks*

#### *Government Rebates*

We participate in certain federal government rebate programs, such as Medicare and Medicaid. We accrue estimated rebates based on estimated percentages of product sold to qualified patients, estimated rebate percentages and estimated levels of inventory in the distribution channel that will be sold to qualified patients and record the rebate as a reduction of revenue.

#### *Government Chargebacks*

We provide discounts to federal government qualified entities with whom we have contracted. These federal entities purchase products from the wholesale pharmaceutical distributors at a discounted price, and the wholesale pharmaceutical distributors then charge back to us the difference between the current retail price and the contracted price that the federal entities paid for the product. We accrue estimated chargebacks based on contract prices and sell-through sales data obtained from third party information and record the chargeback as a reduction of revenue.

#### *Co-Pay Assistance*

We offer discount card programs to patients under which the patient receives a discount on his or her prescription. We reimburse pharmacies for this discount through a third-party vendor. We record the total amount of estimated discounts for sales recorded in the period as a reduction of revenue based on a combination of actual invoices received and an estimate of discounts to be paid for product in the sales channel based on historical information.

### *Returns and Prompt Pay Allowances*

#### *Sales Returns*

Consistent with industry practice, we maintain a return policy that allows customers to return product within a specified period prior to and subsequent to the product expiration date. Generally, product may be returned for a period beginning six months prior to its expiration date and up to one year after its expiration date. The right of return expires on the earlier of one year after the product expiration date or the time that the product is dispensed to the patient. The majority of our product returns are the result of product dating, which falls within the range set by our policy, and are settled through the issuance of a credit to the customer. Our estimate of the provision for returns is based upon our historical experience with actual returns, which is applied to the level of sales for the period that corresponds to the period during which our customer may return product. This period is known to us based on the shelf lives of our products at the time of shipment. We record sales returns as an allowance against accounts receivable and a reduction of revenue.

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### *Prompt Pay Discounts*

As an incentive for prompt payment, we offer a 2% cash discount to customers. We expect that all customers will comply with the contractual terms to earn the discount. We record the discount as an allowance against accounts receivable and a reduction of revenue.

The following table summarizes our customer-related accruals and allowances as of March 31, 2014:

	<u>Customer Discounts and Rebates</u>	<u>Co-Pay Assistance</u>	<u>Government Rebates and Chargebacks</u>	<u>Returns and Prompt Pay Allowances</u>	<u>Total</u>
Balance at December 31, 2013	\$ 4,459	\$ 2,258	\$ 1,407	\$ 431	\$ 8,555
Current provisions relating to sales in current year	16,475	16,899	5,048	3,670	42,092
Adjustments relating to prior year sales	(1,576)	(194)	—	—	(1,770)
Payments/returns relating to sales in current year	(4,730)	(10,169)	(1,735)	(2,485)	(19,119)
Payments/returns relating to sales in prior years	(926)	(1,078)	(871)	—	(2,875)
Balance at March 31, 2014	<u>\$ 13,702</u>	<u>\$ 7,716</u>	<u>\$ 3,849</u>	<u>\$ 1,616</u>	<u>\$ 26,883</u>

### *Cost of Goods Sold*

We recognize cost of goods sold in connection with our sales of DUEXIS, VIMOVO and RAYOS/LODOTRA.

Cost of goods sold of DUEXIS includes all costs directly related to the acquisition of product from our third party manufacturers, including freight charges and costs of distribution.

Cost of goods sold of RAYOS includes all costs directly related to the acquisition of product from our third party manufacturers, including freight charges and costs of distribution, amortization of developed technology, royalty payments to third parties for the use of certain licensed patents and applicable taxes.

Cost of goods sold of LODOTRA includes raw material costs, costs associated with third parties who manufacture LODOTRA for us, supply chain costs, manufacturing overhead costs, amortization of developed technology, royalty payments to third parties for the use of certain licensed patents and applicable taxes.

Cost of goods sold for VIMOVO in the fourth quarter of 2013, following our acquisition in November 2013 of certain assets and rights necessary to commercialize VIMOVO in the United States, included only intangible amortization expense. Beginning in the first quarter of 2014, in connection with our marketing of VIMOVO in the United States, cost of goods sold for VIMOVO includes all costs directly related to the acquisition of product from AstraZeneca and/or a third-party manufacturer. At the time of our acquisition of the U.S. rights to VIMOVO, we estimated the fair value of contingent royalties payable to Pozen using an income approach under the discounted cash flow method, which included revenue projections and other assumptions we made to determine the fair value. If we were to significantly overperform or underperform against our original revenue projections or it became necessary to make changes to our assumptions, we would be required to reassess the fair value of the contingent royalties payable to Pozen. Any adjustments to fair value would be recorded in the period such adjustment was made as either a charge or credit to royalties payable, which is part of cost of goods sold, in accordance with our established accounting policies, and could impact the reported operating results in the period the adjustment was made.

### *Inventories*

Inventories are stated at the lower of cost or market value. Inventories consist of raw materials, work-in-process and finished goods. We have entered into manufacturing and supply agreements for the manufacture or purchase of raw materials and production supplies. Inventories include the direct purchase cost of materials and supplies and manufacturing overhead costs. Inventories exclude product sample inventory, which are included in other current assets and are expensed as a component of sales and marketing expense when provided to physicians or healthcare providers.

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### *Intangible Assets*

Our intangible assets consist of developed technology related to three of our approved products: LODOTRA outside the United States, RAYOS in the United States and intellectual property rights related to our acquisition of the U.S. rights to VIMOVO. We amortize LODOTRA and RAYOS intangible assets over 12 years, which is the estimated useful life of the underlying patents, and we amortize the U.S. intellectual property rights of the VIMOVO intangible asset over 61.5 months, or through the end of 2018. We review our intangible assets when events or circumstances may indicate that the carrying value of these assets exceeds their fair value. We measure fair value based on the estimated future discounted cash flows associated with our assets in addition to other assumptions and projections that we deem to be reasonable and supportable.

### *Fair Value of Financial Instruments*

The carrying amounts of our financial instruments, including cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses, approximate their fair values due to their short maturities. The estimated fair value of our derivative liability related to the convertible portion of our Convertible Senior Notes was derived utilizing the binomial lattice approach for the valuation of convertible instruments. Assumptions used in the calculation included, among others, determining the appropriate credit spread using benchmarking analysis and solving for the implied credit spread, calculating the fair value of the stock component using a discounted risk free rate and borrowing cost and calculating the fair value of the note component using a discounted credit adjusted discount rate. Based on the assumptions used to determine the fair value of the derivative liability associated with the Convertible Senior Notes, we concluded that these inputs were Level 3 inputs. We will continue to derive the fair value of the derivative liability using the binomial lattice approach and these assumptions in all future reporting periods.

### *Business Combinations*

We account for business combinations in accordance with the pronouncement guidance in ASC 805, *Business Combinations*, in which acquired assets and liabilities are measured at their respective estimated fair values as of the acquisition date. We may be required, as in the case of intangible assets or contingent royalties, to determine the fair value associated with these amounts by estimating the fair value using an income approach under the discounted cash flow method, which may include revenue projections and other assumptions made by us to determine the fair value.

### *Provision for Income Taxes*

We account for income taxes based upon an asset and liability approach. Deferred tax assets and liabilities represent the future tax consequences of the differences between the financial statement carrying amounts of assets and liabilities versus the tax basis of assets and liabilities. Under this method, deferred tax assets are recognized for deductible temporary differences, and operating loss and tax credit carryforwards. Deferred tax liabilities are recognized for taxable temporary differences. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The impact of tax rate changes on deferred tax assets and liabilities is recognized in the year that the change is enacted. We also account for the uncertainty in income taxes by utilizing a comprehensive model for the recognition, measurement, presentation and disclosure in financial statements of any uncertain tax positions that have been taken or are expected to be taken on an income tax return.

### *Stock-Based Compensation*

We account for employee stock-based compensation by measuring and recognizing compensation expense for all stock-based payments based on estimated grant date fair values. We use the straight-line method to allocate compensation cost to reporting periods over each optionee's requisite service period, which is generally the vesting period. We estimate the fair value of our stock-based awards to employees using the Black-Scholes option pricing model. The Black-Scholes model requires the input of subjective assumptions, including the expected stock price, volatility, risk-free interest rate, the calculation of expected term and the fair value of the underlying common stock on the date of grant, among other inputs.

We also account for stock options issued to non-employees based on the stock options' estimated fair value determined using the Black-Scholes option pricing model. The fair value of equity awards granted to non-employees are re-measured at each reporting date, and the resulting change in the fair value associated with awards, if any, is recognized as a corresponding increase or reduction to stock-based compensation during the period.

## **LIQUIDITY, FINANCIAL POSITION AND CAPITAL RESOURCES**

We have incurred losses since our inception in June 2005 and, as of March 31, 2014, we had an accumulated deficit of \$663,365. We anticipate that we will continue to incur net losses until such time as the revenues we generate from DUEXIS, VIMOVO and RAYOS/LODOTRA or any products we may acquire or in-license are sufficient to cover our operating expenses. We expect that our sales and marketing expenses will continue to increase as a result of our commercialization of DUEXIS, VIMOVO and RAYOS/LODOTRA. As a result, we will need to generate significant net product sales, and royalty and other revenues to achieve profitability.

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We have financed our operations to date through equity financings, debt financings and the issuance of convertible notes. As of March 31, 2014, we had \$103,374 in cash and cash equivalents.

On November 18, 2013, we entered into note purchase agreements with investors to issue \$150,000 aggregate principal amount of Convertible Senior Notes. The note purchase agreements contain customary representations, warranties, covenants and closing conditions. The Convertible Senior Notes were issued on November 22, 2013. We received net proceeds of \$124,923 from the sale of the Convertible Senior Notes, after deducting fees and expenses of \$6,402 and \$18,675 related to a capped call transaction. The Convertible Senior Notes are governed by an Indenture, dated as of November 22, 2013, between us and U.S. Bank National Association, as trustee. The Convertible Senior Notes bear interest at a rate of 5.00% per year, payable in arrears on May 15 and November 15 of each year, beginning on May 15, 2014. The Convertible Senior Notes will mature on November 15, 2018, unless earlier repurchased or converted. The Convertible Senior Notes were sold at a price equal to 100% of the principal amount thereof and are convertible at the option of the holders at any time prior to the close of business on the business day immediately preceding August 15, 2018 only under certain conditions. On or after August 15, 2018 until the close of business on the second scheduled trading day immediately preceding the maturity date for the Convertible Senior Notes, holders will be able to convert their Convertible Senior Notes at their option at the conversion rate then in effect at any time, regardless of these conditions. Subject to certain limitations, we may settle conversions of the Convertible Senior Notes by paying or delivering, as the case may be, cash, shares of common stock or a combination of cash and shares of our common stock, at our election. If we undergo a fundamental change prior to the maturity date of the Convertible Senior Notes, the holders may require us to repurchase for cash all or any portion of their Convertible Senior Notes at a price equal to 100% of the principal amount of the Convertible Senior Notes to be repurchased, plus accrued and unpaid interest.

The conversion rate for the Convertible Senior Notes will initially be 186.4280 shares of common stock per \$1,000 principal amount of Convertible Senior Notes (equivalent to an initial conversion price of approximately \$5.36 per share of common stock); provided that unless and until we obtain stockholder approval to issue more than 13,164,951 shares of our common stock, which is 19.99% of our common stock outstanding on November 18, 2013, upon conversion of the Convertible Senior Notes in accordance with the listing standards of The NASDAQ Global Market, the number of shares of common stock deliverable upon conversion will be subject to a "conversion share cap." Unless and until such stockholder approval is obtained, we are required to settle conversions of the Convertible Senior Notes in cash up to their principal amount, shares for any conversion spread, and, if the number of shares deliverable for the conversion spread exceeds the conversion share cap, cash in lieu of shares that would otherwise be deliverable. The conversion rate of the Convertible Senior Notes, and the corresponding conversion price, is subject to adjustment for certain events, but will not be adjusted for accrued and unpaid interest.

On March 18, 2014, we, Holdings, Vidara, U.S. HoldCo and Merger Sub entered into the Merger Agreement under which Merger Sub will merge with and into Horizon Pharma, Inc., with Horizon Pharma, Inc. continuing as the surviving corporation and as a wholly-owned, indirect subsidiary of Vidara, with Vidara converting to a public limited company and changing its name to Horizon Pharma plc. New Horizon will be organized under the laws of Ireland with a portfolio of four products marketed primarily in the United States. Upon the Closing, our security holders (excluding the holders of the Convertible Senior Notes) will own approximately 74% of New Horizon and Holdings will own approximately 26% of New Horizon. At the Closing, Holdings will receive a cash payment of \$200,000, plus the cash of Vidara and its subsidiaries as of Closing, less the indebtedness of Vidara and its subsidiaries and transaction expenses of Vidara and its subsidiaries paid by New Horizon at or following the Closing, subject to certain adjustments.

In connection with the Merger, our stockholders will receive one ordinary share of New Horizon in exchange for each share of our common stock they own at Closing. Additionally, we entered into a commitment letter, or the Commitment Letter, with Deerfield Management Company, L.P., or Deerfield, and certain funds managed by Deerfield, or the Deerfield Funds, pursuant to which the Deerfield Funds have committed to provide up to \$250,000 of senior secured loans to finance the Merger, or the Facility. The commitment to provide the Facility is subject to certain conditions, including the negotiation of definitive documentation and other customary closing conditions consistent with the Merger Agreement. The receipt of funding under the Facility is not a condition to the obligations of we have under the terms of the Merger Agreement.

During the three months ended March 31, 2014, we received proceeds of \$23,544 in connection with our issuance of an aggregate of 5,188,916 shares of our common stock upon the exercise of common stock warrants. Additionally, we received \$612 in proceeds in connection with our issuance of an aggregate of 108,600 shares of our common stock upon the exercise of stock options.

We are required to maintain compliance with applicable Swiss laws with respect to our Swiss subsidiary, Horizon Pharma AG, including laws requiring maintenance of equity in the subsidiary to avoid overindebtedness, which requires Horizon Pharma AG to maintain assets in excess of its liabilities. We review on a regular basis whether our Swiss subsidiary is overindebted. As of March 31, 2014 and December 31, 2013, our Swiss subsidiary was overindebted, primarily as a result of operating losses at the subsidiary. We will continue to monitor and review steps to address any overindebtedness until such time as our Swiss subsidiary may generate positive income at a statutory level, which could require us to have cash at our Swiss subsidiary in excess of its near term operating needs and could affect our ability to have sufficient cash to meet our near term operating needs. As of March 31, 2014 and December 31, 2013, Horizon Pharma AG had cash and cash equivalents of \$2,558 and \$3,476, respectively. Based upon the cash and cash equivalents held by Horizon Pharma AG as of March 31, 2014 and December 31, 2013 and Horizon Pharma AG's level of overindebtedness at such times, we do not expect that our financial position or results of operations will be materially affected by any need to address overindebtedness at our Swiss subsidiary. To date, the overindebtedness of our Swiss subsidiary has not resulted in the need to divert material cash resources from our U.S. subsidiary.

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The following table provides a summary of our cash flows for the three months ended March 31, 2014 and 2013:

	Three Months Ended March 31,	
	2014	2013
Cash and cash equivalents	\$103,374	\$ 81,076
Cash (used in) provided by :		
Operating activities	(757)	(22,769)
Investing activities	(494)	(225)
Financing activities	24,156	—

### **Sources and Uses of Cash**

#### ***Operating Cash Flows***

During the three months ended March 31, 2014 and 2013, net cash used in operating activities was \$757 and \$22,769, respectively. The decrease in net cash used in operating activities during the quarter ended March 31, 2014 was primarily attributable to higher cash collections from accounts receivable balances as a result of an increase in product sales, partially offset by higher cash outlays for trade payables and transaction related costs in the current year.

#### ***Investing Cash Flows***

During the three months ended March 31, 2014 and 2013, net cash flows used in investing activities was \$494 and \$225, respectively. The increase in net cash used in investing activities during the three months ended March 31, 2014 was associated with capital expenditures related to purchases of computers and related equipment in connection with the expansion of our field sales force.

#### ***Financing Cash Flows***

During the three months ended March 31, 2014 and 2013, net cash provided by financing activities was \$24,156 and \$0, respectively. The increase in net cash provided by financing activities during the three months ended March 31, 2014 was primarily attributable to proceeds received from the exercise of common stock warrants. During the three months ended March 31, 2014, we received proceeds of \$23,544 in connection with the exercise of warrants to purchase 5,188,916 shares of our common stock. Additionally, we received \$612 in proceeds related to the exercise of stock options to purchase 108,600 shares of our common stock.

### **Contractual Obligations**

During the three months ended March 31, 2014, there were no material changes outside of the ordinary course of business to our contractual obligations as previously disclosed in Part II, Item 7 of our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, except for our entry into the following commitments described below.

On March 18, 2014, we entered into the Commitment Letter with Deerfield and certain Deerfield Funds pursuant to which the Deerfield Funds have committed to provide up to \$250,000 of senior secured loans to finance the Merger. The commitment to provide the Facility is subject to certain conditions, including the negotiation of definitive documentation and other customary closing conditions consistent with the Merger Agreement. The receipt of funding under the Facility is not a condition to the obligations we have under the terms of the Merger Agreement.

We also paid Deerfield a commitment fee of \$5,000 upon execution of the Commitment Letter. The \$5,000 commitment fee paid to Deerfield was capitalized as a prepaid expense and is being amortized to expense through June 30, 2014. The Commitment Letter expires on June 30, 2014 unless by June 30, 2014 we have provided notice to Deerfield that we commit to borrow at least \$225,000 under the Facility, in which case the Commitment Letter will expire on the earlier of September 30, 2014, or the Closing and the entry into definitive documentation for the Facility with the Deerfield Funds. In the event the commitments under the Commitment Letter are extended to September 30, 2014 and we fail to consummate the Merger, we will be required to pay an additional fee of \$3,750 to Deerfield. We have also agreed to pay customary fees and expenses in connection with obtaining the Facility and have agreed to indemnify Deerfield and the Deerfield Funds if certain losses are incurred by Deerfield and the Deerfield Funds in connection therewith.

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If the proposed Merger between us and Vidara is consummated, we will be required to pay our investment bankers a fee of \$8,000. An additional \$1,000 non-refundable fee has already been paid to the investment bankers in connection with the delivery of the fairness opinion.

### **Off-Balance Sheet Arrangements**

Since our inception, we have not engaged in any off-balance sheet arrangements, including the use of structured finance, special purpose entities or variable interest entities, other than the indemnification agreements discussed in Note 11, "Commitments and Contingencies" in the notes to our condensed consolidated financial statements included in this report.

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

We are exposed to various market risks, which include potential losses arising from adverse changes in market rates and prices, such as interest rates and foreign exchange fluctuations. We do not enter into derivatives or other financial instruments for trading or speculative purposes.

*Interest Rate Risk.* We are subject to interest rate fluctuation exposure through our investment in money market accounts which bear a variable interest rate. The goals of our investment policy are associated with the preservation of capital, fulfillment of liquidity needs and fiduciary control of cash. To achieve our goal of maximizing income without assuming significant market risk, we maintain our excess cash and cash equivalents in money market funds. Because of the short-term maturities of our cash equivalents, we do not believe that a decrease in interest rates would have any material negative impact on the fair value of our cash equivalents.

*Foreign Currency Risk.* Our sales contracts relating to LODOTRA are principally denominated in Euros and are subject to significant foreign currency risk. We also incur certain operating expenses in currencies other than the U.S. dollar in relation to Horizon Pharma AG; therefore, we are subject to volatility in cash flows due to fluctuations in foreign currency exchange rates, particularly changes in the Euro. To date, we have not entered into any hedging contracts since exchange rate fluctuations have had minimal impact on our results of operations and cash flows.

*Inflation Risk.* We do not believe that inflation has had a material impact on our business or results of operations during the periods for which the condensed consolidated financial statements are presented in this report.

*Credit Risk.* Historically, our accounts receivable balances have been highly concentrated with a select number of customers, consisting primarily of large wholesale pharmaceutical distributors who, in turn, sell the products to pharmacies, hospitals and other customers. For the three months ended March 31, 2014, our top three customers, AmerisourceBergen, McKesson Corporation and Cardinal Health, Inc., accounted for approximately 85% of total consolidated gross sales. For the year ended December 31, 2013, our top five customers, AmerisourceBergen, McKesson Corporation, Cardinal Health, Inc., Mundipharma and Rochester Drug Company, accounted for approximately 89% of total consolidated gross sales.

In addition, three customers, McKesson Corporation, AmerisourceBergen and Cardinal Health, Inc., accounted for approximately 85% of our total outstanding accounts receivable balances at March 31, 2014. As of December 31, 2013, four customers, McKesson Corporation, AmerisourceBergen, Rochester Drug Company and Cardinal Health, Inc., accounted for approximately 85% of our total outstanding accounts receivable balances. Historically, we have not experienced any losses related to our accounts receivable balances.

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

*Evaluation of Disclosure Controls and Procedures.* As required by paragraph (b) of Rules 13a-15 and 15d-15 promulgated under the Exchange Act, our management, including our Chief Executive Officer and Chief Financial Officer, conducted an evaluation as of the end of the period covered by this report, of the effectiveness of our disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e) and 15d-15(e). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of March 31, 2014, the end of the period covered by this report.

*Changes in Internal Control Over Financial Reporting.* There were no changes in our internal control over financial reporting during the period covered by this report that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

On February 15, 2012, we received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an Abbreviated New Drug Application, or ANDA, with the U.S. Food and Drug Administration, or FDA, for a generic version of DUEXIS, containing 800 mg of ibuprofen and 26.6 mg of famotidine. In March 2012, we filed a patent infringement lawsuit in the United States District Court for the District of Delaware against Par Pharmaceutical, Inc. and Par Pharmaceutical Companies, Inc., or collectively Par, for filing an ANDA against DUEXIS and seeking an injunction to prevent the approval of Par's ANDA and/or prevent Par from selling a generic version of DUEXIS. In January 2013, we filed a second suit against Par in the United States District Court for the District of Delaware claiming patent infringement of additional patents that have been issued for DUEXIS and seeking an injunction to prevent the approval of Par's ANDA and/or prevent Par from selling a generic version of DUEXIS.

On August 21, 2013, we entered into a settlement agreement, or Par settlement agreement, and license agreement, or Par license agreement, with Par relating to our patent infringement litigation. The Par settlement agreement provides for a full settlement and release by both us and Par of all claims that were or could have been asserted in the litigation and that arise out of the specific patent issues that were the subject of the litigation, including all resulting damages or other remedies.

Under the Par license agreement, we granted Par a non-exclusive license (that is only royalty-bearing in some circumstances) to manufacture and commercialize Par's generic version of DUEXIS in the United States after the generic entry date (as defined below) and to take steps necessary to develop inventory of, and obtain regulatory approval for, but not commercialize, Par's generic version of DUEXIS prior to the generic entry date, or collectively the license. The license covers all patents owned or controlled by us during the term of the Par license agreement that would, absent the license, be infringed by the manufacture, use, sale, offer for sale, or importation of Par's generic version of DUEXIS in the United States. Unless terminated sooner pursuant to the terms of the Par license agreement, the license will continue until the last to expire of the licensed patents and/or applicable periods of regulatory exclusivity.

Under the Par license agreement, the generic entry date is January 1, 2023; however, Par may be able to enter the market earlier in certain circumstances. Such events relate to the resolution of potential future third party DUEXIS patent litigation, the entry of other third party generic versions of DUEXIS or certain specific changes in DUEXIS market conditions. Only in the event that Par enters the DUEXIS market due to the specified changes in DUEXIS market conditions will the license become royalty-bearing, with the royalty obligations ceasing upon the occurrence of one of the other events that would have allowed Par to enter the DUEXIS market.

Under the Par license agreement, we also agreed not to sue or assert any claim against Par for infringement of any patent or patent application owned or controlled by us during the term of the Par license agreement based on the manufacture, use, sale, offer for sale, or importation of Par's generic version of DUEXIS in the United States.

The Par license agreement may be terminated by us if Par commits a material breach of the agreement that is not cured or curable within 30 days after we provide notice of the breach. We may also terminate the Par license agreement immediately if Par or any of its affiliates initiate certain challenges to the validity or enforceability of any of the licensed patents or their foreign equivalents. In addition, the Par license agreement will terminate automatically upon termination of the Par settlement agreement.

On March 13, 2013, we received purported Notice Letters that a Paragraph IV Patent Certification had been filed by Alvogen Pine Brook, Inc., or Alvogen, advising that Alvogen had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. In the Notice Letters, Alvogen noted that as of March 13, 2013, the FDA had not accepted the ANDA for review. Alvogen has agreed that their Notice Letters do not constitute Notice as described in 21 U.S.C. 355(j)(2)(B).

On July 15, 2013, we received a Paragraph IV Patent Certification from Watson Laboratories, Inc.—Florida, or Watson, advising that Watson had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Watson has not advised us as to the timing or status of the FDA's review of its filing. On August 26, 2013, we, together with Jagotec AG, or Jagotec, filed suit in the United States District Court for the District of New Jersey against Watson, Actavis Pharma, Inc., Andrx Corp., and Actavis, Inc., or collectively WLF, seeking an injunction to prevent the approval of the ANDA. The lawsuit alleges that WLF has infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124, and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS containing 1 mg, 2 mg, and 5 mg of prednisone prior to the expiration of the patents. The subject patents are listed in the FDA's Approved Drug Products with Therapeutic Equivalence Evaluations, commonly known as the Orange Book. The commencement of the patent infringement lawsuit stays, or bars, FDA approval of WLF's ANDA for 30 months or until an earlier district court decision that the subject patents are not infringed or invalid.

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On or about August 12, 2013, we received a Notice of Opposition to a European patent covering LODOTRA, EP 2049123, filed by Laboratorios Liconsa, S.A. In the European Union, the grant of a patent may be opposed by one or more private parties.

On September 12, 2013, we received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Par Pharmaceutical, Inc. has not advised us as to the timing or status of the FDA's review of its filing. On October 22, 2013, we, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against Par seeking an injunction to prevent the approval of the ANDA. The lawsuit alleged that Par had infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124 and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS prior to the expiration of the patents. The subject patents are listed in the FDA's Orange Book. On November 20, 2013, we were notified by counsel for Par that Par Pharmaceutical, Inc. had elected to withdraw its ANDA with the FDA for a generic version of RAYOS containing 2 mg and 5 mg of prednisone. On December 5, 2013, we entered into a Stipulation of Dismissal with Par Pharmaceutical, Inc. whereby Par Pharmaceutical, Inc. agreed to withdraw its application to market a generic version of RAYOS.

Currently there are patent litigations pending against five generic companies intending to market VIMOVO before the expiration of patents listed in the Orange Book. These cases are in the District of New Jersey and are grouped in three sets: (i) Dr. Reddy's Laboratories, Inc., or Dr. Reddy's; Lupin Pharmaceuticals Inc., or Lupin; Anchen Pharmaceuticals Inc., or Anchen, or collectively, the DRL cases; (ii) Mylan Laboratories Limited, or collectively, the Mylan cases; and (iii) Watson Pharma, Inc., or collectively, the Watson cases. These cases seek an injunction preventing any infringing activity until the expiration of the patents. We understand that Dr. Reddy's has entered into a settlement with AstraZeneca AB, or AstraZeneca, with respect to patent rights directed to Nexium for the commercialization of VIMOVO, and that according to the settlement agreement, Dr. Reddy's will not be able to commercialize VIMOVO under AstraZeneca's Nexium patent rights until May 28, 2014. As part of our acquisition of the U.S. rights to VIMOVO, we have taken over and are responsible for the patent litigations that include the Pozen patents licensed to us under the Pozen license agreement.

The DRL cases were filed on April 21, 2011, July 25, 2011, October 28, 2011, and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from Paragraph IV Notice Letters providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. We understand the Dr. Reddy's notice letters were dated March 11, 2011 and November 12, 2012; the Lupin notice letter was dated June 10, 2011; and the Anchen notice letter was dated September 16, 2011. The court has issued a claims construction order. The DRL cases do not have pretrial deadlines or a trial date set. We understand Anchen has recertified under Paragraph III and has filed a motion to dismiss on that basis.

The Watson cases were filed on May 10, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from a March 29, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Watson cases.

The Mylan cases were filed on June 28, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from a May 16, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Mylan cases.

### **Item 1A: Risk Factors**

You should consider carefully the risks described below, together with all of the other information included in this report, and in our other filings with the Securities and Exchange Commission, or SEC, before deciding whether to invest in or continue to hold our common stock. The risks described below are all material risks currently known, expected or reasonably foreseeable by us. If any of these risks actually occurs, our business, financial condition, results of operations or cash flow could be seriously harmed. This could cause the trading price of our common stock to decline, resulting in a loss of all or part of your investment.

The risk factors set forth below with an asterisk (\*) next to the title are new risk factors or risk factors containing changes, including any material changes, from the risk factors previously disclosed in Item 1A of our annual report on Form 10-K for the year ended December 31, 2013, as filed with the SEC.

## **Risks Related to Our Business and Industry**

*Our ability to generate revenues from our products will be subject to attaining significant market acceptance among physicians, patients and healthcare payers.*

DUEXIS®, VIMOVO® and RAYOS®/LODOTRA®, and other product candidates that we may develop, acquire, or in-license, may not attain market acceptance among physicians, patients, healthcare payers or the medical community. In the U.S. market, we began selling DUEXIS in December 2011. We began commercial sales of RAYOS, which was approved by the U.S. Food and Drug Administration, or FDA, in July 2012, to a subset of rheumatologists in the fourth quarter of 2012 with the full launch to the majority of U.S. rheumatologists and key primary care physicians in late January 2013. Outside the United States, LODOTRA has been sold in a limited number of countries and sales may not grow to expected levels, in part because we depend on our distribution partner, Mundipharma International Corporation Limited, or Mundipharma, for commercialization outside the United States. With respect to DUEXIS, we have only received marketing approval in the United Kingdom, or UK, thus far, and even if it is approved in other European countries, we do not expect the opportunity in Europe to be material to our business given the current state of the market in Europe for pain products and the revenue being generated by existing branded non-steroidal anti-inflammatory drugs, or NSAIDs, in Europe. There have been no sales of DUEXIS in the UK thus far. VIMOVO was launched in the U.S. market in the fourth quarter of 2010 by AstraZeneca AB, or AstraZeneca, under its license from Pozen Inc., or Pozen. Following our acquisition of the U.S. rights to VIMOVO in November 2013, we began selling VIMOVO in the first quarter of 2014 and have completed the expansion of our sales force to approximately 250 primary care representatives and approximately 40 rheumatology sales specialists. We believe that the degree of market acceptance and our ability to generate revenues from our products will depend on a number of factors, including:

- timing of market introduction of our products as well as competitive drugs;
- efficacy and safety of our products;
- continued projected growth of the arthritis, pain and inflammation markets;
- prevalence and severity of any side effects;
- acceptance by patients, primary care specialists and key specialists, including rheumatologists, orthopedic surgeons and pain specialists;
- the performance of our distribution partners, over which we have limited control;
- potential or perceived advantages or disadvantages of our products over alternative treatments, including cost of treatment and relative convenience and ease of administration;
- strength of sales, marketing and distribution support;
- the price of our products, both in absolute terms and relative to alternative treatments;
- impact of past and future product price increases;
- our ability to maintain a continuous supply of product for commercial sale;
- the effect of current and future healthcare laws;
- availability of coverage and adequate reimbursement and pricing from government and other third-party payers; and
- product labeling or product insert requirements of the FDA or other regulatory authorities.

With respect to DUEXIS and VIMOVO, studies indicate that physicians do not commonly co-prescribe gastrointestinal, or GI, protective agents to high-risk patients taking NSAIDs. We believe this is due in part to a lack of awareness among physicians prescribing NSAIDs of the risk of NSAID-induced upper GI ulcers, in addition to the inconvenience of prescribing two separate medications and patient compliance issues associated with multiple prescriptions. If physicians remain unaware of, or do not otherwise believe in, the benefits of combining GI protective agents with NSAIDs, our market opportunity for DUEXIS and VIMOVO will be limited. Some physicians may also be reluctant to prescribe DUEXIS or VIMOVO due to the inability to vary the dose of ibuprofen and naproxen, respectively, or if they believe treatment with NSAIDs or GI protective agents other than those contained in DUEXIS and VIMOVO, including those of our competitors, would be more effective for their patients. With respect to each of DUEXIS, VIMOVO and RAYOS/LODOTRA, their higher cost compared to the generic or branded forms of their active ingredients alone may limit adoption by physicians, patients and healthcare payers. If DUEXIS, VIMOVO, RAYOS/LODOTRA or any other product that we may seek approval for, acquire or in-license fail to attain market acceptance, we may not be able to generate significant revenue to achieve or sustain profitability, which would have a material adverse effect on our business, results of operations, financial condition and prospects.

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*Our current business plan is highly dependent upon our ability to successfully execute on our sales and marketing strategy for the commercialization of DUEXIS, VIMOVO and RAYOS/LODOTRA. If we are unable to successfully execute on our sales and marketing strategy, we may not be able to generate significant product revenues or execute on our business plan.*

Our strategy is to build a fully-integrated U.S.-focused biopharmaceutical company to successfully execute the commercialization of DUEXIS, VIMOVO and RAYOS in the U.S. market. We may not be able to successfully commercialize DUEXIS, VIMOVO or RAYOS in the United States. Prior to our commercial launch of DUEXIS in the United States in December 2011, we did not have any experience commercializing pharmaceutical products on our own. LODOTRA was commercially launched in Europe by our exclusive distribution partners Merck Serono and Mundipharma. In order to commercialize any approved products, we must continue to build our sales, marketing, distribution, managerial and other non-technical capabilities. Although we have expanded our sales force to approximately 290 sales representatives in connection with our November 2013 acquisition of the U.S. rights to VIMOVO, we currently have limited resources compared to some of our competitors, and the continued development of our own commercial organization to market these products and any additional products we may acquire or in-license will be expensive and time-consuming and could delay any product launch or our success in assuming commercialization for VIMOVO in the United States. Nor can we be certain that we will be able to continue to successfully develop this capability. As a result of the evolving role of various constituents in the prescription decision making process, we adjusted the profile of the sales representatives we hire from those with traditional pharmaceutical sales experience to those with successful business to business experience. For example, we have faced challenges due to pharmacists increasingly switching a patient's intended prescription from DUEXIS to a generic or over the counter brand. We have faced similar challenges for RAYOS with respect to generic brands and expect to face similar challenges with respect to VIMOVO. While we believe the new profile of our representatives is better suited for this evolving environment, we cannot be certain that our representatives will be able to successfully protect DUEXIS, VIMOVO and RAYOS prescriptions or that we will be able to continue attracting and retaining sales representatives with our desired profile and skills. We will also have to compete with other pharmaceutical and biotechnology companies to recruit, hire, train and retain commercial personnel. To the extent we rely on additional third parties to commercialize any approved products, we may receive less revenues than if we commercialized these products ourselves. In addition, we may have little or no control over the sales efforts of any third parties involved in our commercialization efforts. In the event we are unable to successfully develop and maintain our own commercial organization or collaborate with a third-party sales and marketing organization, we would not be able to commercialize our product candidates and execute on our business plan. If we are unable to successfully implement our commercial plans and drive adoption by patients and physicians of any approved products through our sales, marketing and commercialization efforts, or if our partners fail to successfully commercialize our products, then we will not be able to generate sustainable revenues from product sales which will have a material adverse effect on our business and prospects.

*Our future prospects are highly dependent on the success of DUEXIS, VIMOVO and RAYOS/LODOTRA, and we may not be able to successfully commercialize these products. Failure to do so would adversely impact our financial condition and prospects.*

A substantial majority of our resources are focused on the commercialization of DUEXIS and RAYOS in the United States and we expect to devote significant additional resources to the commercialization of VIMOVO in the United States. Our ability to generate significant product revenues and to achieve commercial success in the near term will initially depend almost entirely on our ability to successfully commercialize DUEXIS, VIMOVO and RAYOS in the United States. DUEXIS has been approved for marketing in the UK but is not yet approved in any other countries in Europe and therefore, unless we obtain regulatory approval in other countries, DUEXIS may not be commercialized to any significant extent outside of the United States. Even if DUEXIS is approved in other European countries, we do not expect the opportunity in Europe to be material to our business given the current state of the market in Europe for pain products and the revenue being generated by existing branded NSAIDs in Europe. Following our acquisition of the U.S. rights to VIMOVO in November 2013, we began selling VIMOVO in the first quarter of 2014. Our strategy with respect to VIMOVO included bringing its pricing in-line with DUEXIS and thereby significantly increasing the value realized per prescription. While we have recently employed a similar strategy for DUEXIS, we cannot guarantee a similar result for VIMOVO, including due to the past declines in VIMOVO prescriptions and our need to re-negotiate managed care contracts for VIMOVO. Our initial strategy for RAYOS is to solely focus on the rheumatology indications approved for RAYOS where our Phase 3 clinical trial data supports our commercial plans. We initially launched RAYOS in the United States to a subset of rheumatologists in the fourth quarter of 2012, and the full launch to the majority of U.S. rheumatologists and key primary care physicians occurred in late January 2013. Although LODOTRA is approved for marketing in more than 30 countries outside the United States, to date it has only been marketed in a limited number of countries. While we anticipate that LODOTRA will be marketed in additional countries as our distribution partner, Mundipharma, formulates its reimbursement strategy, the ability to market LODOTRA in additional countries will depend on Mundipharma's ability to obtain reimbursement approvals in these countries. Even if we obtain additional marketing and reimbursement approvals, our product revenues in Europe are entirely dependent upon the marketing efforts of our exclusive distribution partner, over which we have no control. Before we can market and sell these products in a particular jurisdiction, we need to obtain necessary regulatory approvals (from the FDA in the United States and from similar foreign regulatory agencies in other jurisdictions) and in some jurisdictions, reimbursement authorization. There are no guarantees that we or our commercialization partners will obtain any additional regulatory approvals for our products. Even if we or our commercialization partners obtain additional regulatory approvals, we may never generate significant revenues from any commercial sales of our products. If we fail to successfully commercialize DUEXIS, VIMOVO or RAYOS, we may be unable to generate sufficient revenues to sustain and grow our business, and our business, financial condition and results of operations will be adversely affected.

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*We are solely dependent on Mundipharma to commercialize LODOTRA in Europe and certain Asian, Latin American, Middle Eastern, African and other countries. Failure of Mundipharma or any other third parties to successfully commercialize our products and product candidates in the applicable jurisdictions could have a material adverse effect on our business.*

We rely on Mundipharma for commercialization of LODOTRA in various European countries and certain Asian, Latin American, Middle Eastern, African and other countries. We have limited contractual rights to force Mundipharma to invest significantly in commercialization of LODOTRA in its markets. In the event that Mundipharma or any other third party with any future commercialization rights to any of our products or product candidates fails to adequately commercialize those products or product candidates because it lacks adequate financial or other resources, decides to focus on other initiatives or otherwise, our ability to successfully commercialize our products or product candidates in the applicable jurisdictions would be limited, which would adversely affect our business, financial condition, results of operations and prospects. We have had disagreements with Mundipharma under our European agreements and may continue to have disagreements, which could harm commercialization of LODOTRA in Europe or result in the termination of our agreements with Mundipharma. We also rely on Mundipharma's ability to obtain regulatory approval for LODOTRA in certain Asian, Latin American, Middle Eastern, African and other countries. In addition, our agreements with Mundipharma may be terminated by either party in the event of a bankruptcy of the other party or upon an uncured material breach by the other party. If Mundipharma terminated its agreements with us, we may not be able to secure an alternative distributor in the applicable territory on a timely basis or at all, in which case our ability to generate revenues from the sale of LODOTRA would be materially harmed.

*Our products are subject to extensive regulation, and we may not obtain additional regulatory approvals for our products.*

The clinical development, manufacturing, labeling, packaging, storage, recordkeeping, advertising, promotion, export, marketing and distribution and other possible activities relating to our product candidates are, and any resulting drugs will be, subject to extensive regulation by the FDA and other regulatory agencies. Failure to comply with FDA and other applicable regulatory requirements may, either before or after product approval, subject us to administrative or judicially imposed sanctions.

To market any drugs outside of the United States, we and current or future collaborators must comply with numerous and varying regulatory and compliance related requirements of other countries. Approval procedures vary among countries and can involve additional product testing and additional administrative review periods, including obtaining reimbursement approval in select markets. The time required to obtain approval in other countries might differ from that required to obtain FDA approval. The regulatory approval process in other countries may include all of the risks associated with FDA approval as well as additional, presently unanticipated, risks. Regulatory approval in one country does not ensure regulatory approval in another, but a failure or delay in obtaining regulatory approval in one country may negatively impact the regulatory process in others.

Applications for regulatory approval, including a marketing authorization application for marketing new drugs in Europe, must be supported by extensive clinical and preclinical data, as well as extensive information regarding chemistry, manufacturing and controls, or CMC, to demonstrate the safety and effectiveness of the applicable product candidate. The number and types of preclinical studies and clinical trials that will be required for regulatory approval varies depending on the product candidate, the disease or the condition that the product candidate is designed to target and the regulations applicable to any particular product candidate. Despite the time and expense associated with preclinical and clinical studies, failure can occur at any stage, and we could encounter problems that cause us to repeat or perform additional preclinical studies, CMC studies or clinical trials. Regulatory authorities could delay, limit or deny approval of a product candidate for many reasons, including because they:

- may not deem a product candidate to be adequately safe and effective;
- may not find the data from preclinical studies, CMC studies and clinical trials to be sufficient to support a claim of safety and efficacy;
- may interpret data from preclinical studies, CMC studies and clinical trials significantly differently than we do;
- may not approve the manufacturing processes or facilities associated with our product candidates;
- may conclude that we have not sufficiently demonstrated long-term stability of the formulation for which we are seeking marketing approval;
- may change approval policies (including with respect to our product candidates' class of drugs) or adopt new regulations; or
- may not accept a submission due to, among other reasons, the content or formatting of the submission.

Even if we believe that data collected from our preclinical studies, CMC studies and clinical trials of our product candidates are promising and that our information and procedures regarding CMC are sufficient, our data may not be sufficient to support marketing approval by regulatory authorities, or regulatory interpretation of these data and procedures may be unfavorable. Even if approved, product candidates may not be approved for all indications requested and such approval may be subject to limitations on the indicated uses for which the drug may be marketed, restricted distribution methods or other limitations. Our business and reputation may be harmed by any failure or significant delay in obtaining regulatory approval for the sale of any of our product candidates. We cannot predict when or whether regulatory approval will be obtained for any product candidate we develop.

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While we anticipate that LODOTRA will be marketed in additional countries as Mundipharma formulates its reimbursement strategy, the ability to market LODOTRA in additional countries will depend on Mundipharma's ability to obtain regulatory and reimbursement approvals in these countries. Similarly, our ability to market DUEXIS outside of the United States will depend on obtaining regulatory and reimbursement approval in any country where DUEXIS may be marketed. However, certain countries have a very difficult reimbursement environment and we may not obtain reimbursement approval in all countries where DUEXIS may be marketed, or we may obtain reimbursement approval at a level that would make marketing DUEXIS in certain countries not viable.

*Our limited history of commercial operations makes evaluating our business and future prospects difficult, and may increase the risk of any investment in our common stock.*

Following our acquisition of the U.S. rights to VIMOVO in November 2013, we have three products approved in the United States, one product with broad approval for commercial sale in Europe, and another product approved only for commercial sale in the UK thus far. RAYOS/LODOTRA has been approved in the United States and over 30 other countries, including Australia, Korea, Israel and select countries within Europe. However, we have a limited history of marketing LODOTRA through our distribution partners, and LODOTRA is not yet marketed in all of the countries where it has been approved. DUEXIS was approved in the United States on April 23, 2011, and in March 2013 we announced we were granted marketing authorization for DUEXIS in the UK, and we have generated limited revenues for DUEXIS to date. We began the commercial sale of RAYOS in the United States in the fourth quarter of 2012 and the commercial sale of VIMOVO in the United States in the first quarter of 2014. We face considerable risks and difficulties as a company with limited commercial operating history, particularly as a consolidated entity with operating subsidiaries that also have limited operating histories. If we do not successfully address these risks, our business, prospects, operating results and financial condition will be materially and adversely harmed. Our limited commercial operating history and our lack of any history commercializing VIMOVO makes it particularly difficult for us to predict our future operating results and appropriately budget for our expenses. In the event that actual results differ from our estimates or we adjust our estimates in future periods, our operating results and financial position could be materially affected. For example, we may underestimate the resources we will require to successfully commercialize VIMOVO or not realize the benefits we expect to derive from the acquisition.

*We only have U.S. rights to VIMOVO and have no control over the activities of AstraZeneca to commercialize VIMOVO outside of the United States, which could adversely impact commercialization of VIMOVO in the United States.*

AstraZeneca has retained its existing rights to VIMOVO in territories outside of the United States, including the right to use the VIMOVO name and related trademark. We have little or no control over AstraZeneca's activities with respect to VIMOVO outside of the United States, even though those activities could impact our ability to successfully commercialize VIMOVO in the United States. For example, AstraZeneca or its assignees can make statements or use promotional materials with respect to VIMOVO outside of the United States that are inconsistent with our positioning of the product in the United States, and can sell VIMOVO in foreign countries, including Canada, at prices that are dramatically lower than the prices we expect to charge in the United States. These activities and decisions, while occurring outside of the United States, could harm our commercialization strategy in the United States, in particular because AstraZeneca is continuing to market the product outside the United States under the same VIMOVO brand name that we are using in the United States. In addition, product recalls or safety issues with VIMOVO outside the United States, even if not related to the commercial product we sell in the United States, could result in serious damage to the brand in the United States and impair our ability to successfully market VIMOVO. We also rely on AstraZeneca to provide us with timely and accurate safety information regarding the use of VIMOVO outside of the United States, as we have limited access to this information ourselves.

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*We rely on third parties to manufacture commercial supplies of DUEXIS, VIMOVO and RAYOS/LODOTRA, and we intend to rely on third parties to manufacture commercial supplies of any other approved products. The commercialization of any of our products could be stopped, delayed or made less profitable if those third parties fail to provide us with sufficient quantities of product or fail to do so at acceptable quality levels or prices or fail to maintain or achieve satisfactory regulatory compliance.\**

The facilities used by our third-party manufacturers to manufacture our products and product candidates must be approved by the applicable regulatory authorities. We do not control the manufacturing processes of third-party manufacturers and are currently completely dependent on our third-party manufacturing partners sanofi-aventis U.S. LLC, or sanofi-aventis U.S., operating through Valeant Pharmaceuticals International, Inc., or Valeant, its manufacturing partner located in Laval, Canada for production of DUEXIS, and Jagotec AG, or Jagotec, a wholly-owned subsidiary of SkyePharma PLC, located in Lyon, France, for production of RAYOS/LODOTRA. In August 2011, SkyePharma leased their entire pharmaceutical manufacturing business to Aenova France SAS, or Aenova. As such, Aenova is now a subcontractor for Jagotec for the manufacture of RAYOS/LODOTRA, with our consent. Sanofi Winthrop Industrie in France has been qualified as a backup manufacturer for DUEXIS. Bayer Pharma AG in Germany has been qualified as a backup manufacturer for RAYOS/LODOTRA. In December 2011, Valeant acquired Dermik, a dermatology unit of sanofi-aventis U.S., which includes the Laval, Canada site. Although, Valeant has taken over management and operations at the Laval, Canada facility, our manufacturing agreement remains with sanofi-aventis U.S. We purchase the primary active ingredients for DUEXIS from BASF Corporation in Bishop, Texas and Dr. Reddy's in India, and the primary active ingredient for RAYOS/LODOTRA from Tianjin Tianyao Pharmaceuticals Co., Ltd. in China and Sanofi Chimie in France. With respect to VIMOVO, we rely on AstraZeneca, including through its existing third party manufacturing arrangements, to supply finished VIMOVO product through 2014. After 2014, AstraZeneca will no longer be obligated to supply VIMOVO to us and we will need to rely on our own third-party manufacturing arrangements to ensure continued supply. In connection with our acquisition of the U.S. rights to VIMOVO, we have entered into a long-term master manufacturing services and product agreement with Patheon Pharmaceuticals Inc., or Patheon, for the supply of finished VIMOVO product. We have entered into long-term supply agreements with Divis Laboratories Limited and Minakem Holding SAS for the supply of the active pharmaceutical ingredients, or APIs, of VIMOVO. In addition, we are required to obtain AstraZeneca's consent prior to engaging any third-party manufacturers for esomeprazole, one of the APIs in VIMOVO, other than the third-party manufacturer(s) currently used by AstraZeneca or its affiliates or licensees. To the extent such manufacturers are unwilling or unable to manufacture esomeprazole for us on commercially-acceptable terms, we cannot guarantee that AstraZeneca would consent to our use of alternate sources of supply. If any of our third-party manufacturers cannot successfully manufacture material that conforms to our specifications and the applicable regulatory authorities' strict regulatory requirements, or pass regulatory inspection, they will not be able to secure or maintain regulatory approval for the manufacturing facilities. In addition, we have no control over the ability of third-party manufacturers to maintain adequate quality control, quality assurance and qualified personnel. If the FDA or any other applicable regulatory authorities do not approve these facilities for the manufacture of our products or if they withdraw any such approval in the future, or if our suppliers or third-party manufacturers decide they no longer want to supply our primary active ingredients or manufacture our products, we may need to find alternative manufacturing facilities, which would significantly impact our ability to develop, obtain regulatory approval for or market our products. To the extent any third-party manufacturers that we engage with respect to VIMOVO are different than those used by AstraZeneca, the FDA will need to approve the facilities of those third-party manufacturers used in the manufacture of VIMOVO prior to our sale of any VIMOVO product using these facilities. If we cannot agree to terms with third-party manufacturers of VIMOVO APIs or the third party suppliers we engage do not have their facilities approved by the FDA with sufficient time to transition commercial supply of VIMOVO after 2014, we may experience supply shortages and our commercialization of VIMOVO would be substantially harmed.

Although we have entered into supply agreements for the manufacture of our products, our manufacturers may not perform as agreed or may terminate their agreements with us. Under our manufacturing and supply agreement with sanofi-aventis U.S., operating through Valeant, either we or sanofi-aventis U.S. may terminate the agreement upon an uncured breach by the other party or without cause upon two years prior written notice, so long as such notice is given after the third anniversary of the first commercial sale of DUEXIS. Under our master manufacturing services and product agreement with Patheon for finished VIMOVO product, either we or Patheon may terminate the agreement for uncured material breach by the other party or upon the other party's bankruptcy or insolvency, we may terminate the agreement if any regulatory authority takes any action or raises any objection that prevents us from commercializing the VIMOVO product and Patheon may terminate the agreement if we assign our rights or obligations under the agreement to a competitor of Patheon or to a party that, in the reasonable opinion of Patheon, is not a credit worthy substitute for us, or in certain other circumstances where we assign the agreement without Patheon's consent. Under our manufacturing and supply agreement with Jagotec, either we or Jagotec may terminate the agreement in the event of an insolvency, liquidation or bankruptcy of the other party or upon an uncured breach by the other party. While we have the right to receive a continuing supply of RAYOS/LODOTRA from Jagotec for a period of 24 months after termination, we would need to move our manufacturing to our alternate supplier of RAYOS/LODOTRA, Bayer Pharma AG, in such an event and we would have to qualify a new back-up manufacturer.

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In addition, we do not have the capability to package DUEXIS, VIMOVO, RAYOS/LODOTRA or any other product candidates for distribution. Consequently, we have entered into an agreement with Temmler Werke GmbH, or Temmler, for packaging of RAYOS/LODOTRA in certain European countries, Israel and in the United States, as well as any additional countries as may be agreed to by the parties. We intend to sell drug product finished and packaged by either Temmler or an alternate packager. At the end of 2012, Temmler was acquired by the Aenova Group. Valeant manufactures and supplies DUEXIS to us in final, packaged form for the United States as well as any additional countries as may be agreed to by the parties. During 2014, AstraZeneca is obligated to supply us VIMOVO in final, packaged form under a transition agreement and will work with us to transfer product packaging to Patheon. After 2014, we expect that Patheon will supply final, packaged VIMOVO product pursuant to the master manufacturing services and product agreement we executed in connection with our acquisition of the U.S. rights to VIMOVO.

The manufacture of pharmaceutical products requires significant expertise and capital investment, including the development of advanced manufacturing techniques and process controls. Manufacturers of pharmaceutical products often encounter difficulties in production, particularly in scaling up and validating initial production. These problems include difficulties with production costs and yields, quality control, including stability of the product, quality assurance testing, shortages of qualified personnel, as well as compliance with strictly enforced federal, state and foreign regulations. We cannot assure you that issues relating to the manufacture of any of our products will not occur in the future. Additionally, our manufacturers may experience manufacturing difficulties due to resource constraints or as a result of labor disputes or unstable political environments. If our manufacturers were to encounter any of these difficulties, or otherwise fail to comply with their contractual obligations, our ability to commercialize our products in the United States or provide any product candidates to patients in clinical trials would be jeopardized. Any delay or interruption in our ability to meet commercial demand for our products will result in the loss of potential revenues and could adversely affect our ability to gain market acceptance for these products. In addition, any delay or interruption in the supply of clinical trial supplies could delay the completion of clinical trials, increase the costs associated with maintaining clinical trial programs and, depending upon the period of delay, require us to commence new clinical trials at additional expense or terminate clinical trials completely.

Failures or difficulties faced at any level of our supply chain could materially adversely affect our business and delay or impede the development and commercialization of any of our products or product candidates and could have a material adverse effect on our business, results of operations, financial condition and prospects.

*We have experienced recent growth and have expanded the size of our organization substantially in connection with our acquisition of the U.S. rights to VIMOVO in November 2013, and we may experience difficulties in managing this growth.\**

As of December 31, 2010, we employed 41 full-time employees as a consolidated entity. In anticipation of the commercial launch of DUEXIS, we hired 80 sales representatives during the period from September 2011 through October 2011. As of December 31, 2013 and March 31, 2014, we employed 304 and 427 full-time employees, respectively, as a consolidated entity. We have also experienced, and may continue to experience, turnover of the sales representatives that we hired or will hire in connection with the commercialization of our products, requiring us to hire and train new sales representatives. Our management, personnel, systems and facilities currently in place may not be adequate to support this recent and anticipated growth, and we may not be able to retain or recruit qualified personnel in the future due to competition for personnel among pharmaceutical businesses.

As our commercialization plans and strategies develop, we will need to continue recruiting and training sales and marketing personnel and expect to need to expand the size of our employee base for managerial, operational, financial and other resources. We may also need to further expand these capabilities, along with our field sales force size and capabilities, if we develop, acquire or in-license additional products. Our ability to manage any future growth effectively may require us to do, among other things, the following:

- continue to manage and expand the sales and marketing efforts for our existing products;
- enhance our operational, financial and management controls, reporting systems and procedures;
- expand our international resources;
- successfully identify, recruit, hire, train, maintain, motivate and integrate additional employees;
- establish and increase our access to commercial supplies of our products and product candidates;
- expand our facilities and equipment; and
- manage our internal development efforts effectively while complying with our contractual obligations to licensors, licensees, contractors, collaborators, distributors and other third parties.

Our management may also have to divert a disproportionate amount of its attention away from day-to-day activities and towards managing these growth activities. Our future financial performance and our ability to execute on our business plan will depend, in part, on our ability to effectively manage any future growth and our failure to effectively manage growth could have a material adverse effect on our business, results of operations, financial condition and prospects.



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*If we are unable to effectively train and equip our sales force, our ability to successfully commercialize our products in the United States will be harmed.*

As DUEXIS and RAYOS were not fully commercially launched in the United States until January 2012 and January 2013, respectively, and we did not begin commercializing VIMOVO in the United States until the first quarter of 2014, the members of our sales force have limited experience promoting any of our products. As a result, we are required to expend significant time and resources to train our sales force to be credible and persuasive in convincing physicians to prescribe and pharmacists to dispense our products. In addition, we must train our sales force to ensure that a consistent and appropriate message about our products is being delivered to our potential customers. Our sales representatives may also experience challenges promoting multiple products when they call on physicians and their office staff, and our representatives may also be distracted from selling DUEXIS and RAYOS now that we are commercializing VIMOVO as all of our representatives have to date been focused solely on selling DUEXIS and RAYOS. This is particularly true with respect to DUEXIS, since VIMOVO is approved for similar indications and prescribed to similar patients, and our sales representatives have previously been incentivized to increase DUEXIS market share at the expense of VIMOVO. We have also experienced, and may continue to experience, turnover of the sales representatives that we hire or will hire, requiring us to train new sales representatives. As a result of the managed care environment and pharmacies switching patient's prescriptions to a generic or over the counter brand, we have had to adjust the profile of the sales representatives we hire from the traditional pharmaceutical representative to a representative with business to business experience that is focused on the total office call in order to protect the prescription the physician has written and ensure the patient receives what their doctor ordered. If we are unable to effectively train our sales force and equip them with effective materials, including medical and sales literature to help them inform and educate potential customers about the benefits of our products and their proper administration and label indication, our efforts to successfully commercialize our products could be put in jeopardy, which could have a material adverse effect on our financial condition, stock price and operations.

*We face significant competition from other biotechnology and pharmaceutical companies, including those marketing generic products and our operating results will suffer if we fail to compete effectively.*

The biotechnology and pharmaceutical industries are intensely competitive. We have competitors both in the United States and international markets, including major multinational pharmaceutical companies, biotechnology companies and universities and other research institutions. Many of our competitors have substantially greater financial, technical and other resources, such as larger research and development staff, experienced marketing and manufacturing organizations and well-established sales forces. Additional mergers and acquisitions in the biotechnology and pharmaceutical industries may result in even more resources being concentrated in our competitors and we will have to find new ways to compete and may have to potentially merge with or acquire other businesses to stay competitive. Competition may increase further as a result of advances in the commercial applicability of technologies and greater availability of capital for investment in these industries. Our competitors may succeed in developing, acquiring or in-licensing on an exclusive basis, products that are more effective and/or less costly than our products.

DUEXIS and VIMOVO face competition from Celebrex®, marketed by Pfizer, and several other branded NSAIDs. DUEXIS and VIMOVO also face significant competition from the separate use of NSAIDs for pain relief and GI protective medications to reduce the risk of NSAID-induced upper GI ulcers. Both NSAIDs and GI protective medications are available in generic form and may be less expensive to use separately than DUEXIS or VIMOVO. Legislation enacted in most states in the United States allows or, in some instances mandates, that a pharmacist dispense an available generic equivalent when filling a prescription for a branded product, in the absence of specific instructions from the prescribing physician. Because pharmacists often have economic and other incentives to prescribe lower-cost generics, if physicians prescribe DUEXIS or VIMOVO, those prescriptions may not result in sales. If we are unsuccessful in convincing physicians to provide prescribing instructions prohibiting the substitution of generic ibuprofen and famotidine separately as a substitution for DUEXIS or generic naproxen and branded Nexium (esomeprazole) as a substitute for VIMOVO, sales of DUEXIS and VIMOVO may suffer despite any success we may have in promoting DUEXIS or VIMOVO to physicians. In addition, other product candidates that contain ibuprofen and famotidine in combination or naproxen and esomeprazole in combination, while not currently known to us, may be developed and compete with DUEXIS or VIMOVO, respectively, in the future.

On February 15, 2012, we received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an Abbreviated New Drug Application, or ANDA, with the FDA for a generic version of DUEXIS, containing 800 mg of ibuprofen and 26.6 mg of famotidine. In March 2012, we filed a patent infringement lawsuit in the United States District Court for the District of Delaware against Par Pharmaceutical, Inc. and Par Pharmaceutical Companies, Inc., or collectively Par, for filing an ANDA against DUEXIS and seeking an injunction to prevent the approval of Par's ANDA and/or prevent Par from selling a generic version of DUEXIS. In January 2013, we filed a second suit against Par in the United States District Court for the District of Delaware claiming patent infringement of additional patents that have been issued for DUEXIS and seeking an injunction to prevent the approval of Par's ANDA and/or prevent Par from selling a generic version of DUEXIS.

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On August 21, 2013, we entered into a settlement agreement, or Par settlement agreement, and license agreement, or Par license agreement, with Par relating to our patent infringement litigation. Under the Par license agreement, we granted Par a non-exclusive license (that is only royalty-bearing in some circumstances) to manufacture and commercialize Par's generic version of DUEXIS in the United States after the generic entry date and to take steps necessary to develop inventory of, and obtain regulatory approval for, but not commercialize, Par's generic version of DUEXIS prior to the generic entry date. The generic entry date is January 1, 2023; however, Par may be able to enter the market earlier in certain circumstances. Such events relate to the resolution of potential future third party DUEXIS patent litigation, the entry of other third party generic versions of DUEXIS or certain specific changes in DUEXIS market conditions. If any of the events that permit Par to enter the market with its generic version of DUEXIS prior to January 1, 2023 were to occur, we will likely face generic competition from Par shortly after the event, and our sales of DUEXIS would be substantially harmed. Also, despite our Par settlement agreement and Par license agreement with Par, additional third parties may file ANDAs with the FDA for their own generic versions of DUEXIS and we may not be successful in preventing any other generic products from entering the market.

Currently, patent litigation is pending against five generic companies intending to market VIMOVO before the expiration of patents listed in the FDA's Approved Drug Products with Therapeutic Equivalence Evaluations, commonly known as the Orange Book. These cases are in the District of New Jersey and are grouped in three sets: (i) Dr. Reddy's Laboratories, Inc., or Dr. Reddy's; Lupin Pharmaceuticals Inc., or Lupin; Anchen Pharmaceuticals Inc., or Anchen, or collectively, the DRL cases; (ii) Mylan Laboratories Limited or collectively, the Mylan cases; and (iii) Watson Pharma, Inc., or collectively, the Watson cases. We understand that Dr. Reddy's has entered into a settlement with AstraZeneca with respect to patent rights directed to Nexium for the commercialization of VIMOVO, and that according to the settlement agreement, Dr. Reddy's will not be able to commercialize VIMOVO under AstraZeneca's Nexium patent rights until May 28, 2014. As part of our acquisition of the U.S. rights to VIMOVO, we have taken over and are responsible for the patent litigations that include the Pozen patents licensed to us under the Pozen license agreement.

The DRL cases were filed on April 21, 2011, July 25, 2011, October 28, 2011, and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from Paragraph IV Notice Letters providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. We understand the Dr. Reddy's notice letters were dated March 11, 2011 and November 12, 2012; the Lupin notice letter was dated June 10, 2011; and the Anchen notice letter was dated September 16, 2011. The court has issued a claims construction order. The DRL cases do not have pretrial deadlines or a trial date set. We understand Anchen has recertified under Paragraph III and has filed a motion to dismiss on that basis.

The Watson cases were filed on May 10, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from a March 29, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Watson cases.

The Mylan cases were filed on June 28, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from a May 16, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Mylan cases.

RAYOS/LODOTRA competes with a number of pharmaceuticals on the market to treat rheumatoid arthritis, or RA, including corticosteroids, such as prednisone, disease modifying antirheumatic drugs, or DMARDs, such as methotrexate, and biologic agents such as HUMIRA®, marketed by Abbott, and Enbrel®, marketed by Amgen Inc. and Pfizer. It is typical for an RA patient to take a combination of a DMARD, an oral glucocorticoid, an NSAID and/or a biologic agent. Therefore, we believe that RAYOS/LODOTRA's principal competition is prednisone, the API in RAYOS/LODOTRA, or other oral corticosteroids, which, while they may be suboptimal, are less expensive than RAYOS/LODOTRA. In addition, other product candidates that contain prednisone or other oral corticosteroids in alternative delayed release forms, while not currently known to us, may be developed and compete with LODOTRA in the future.

On March 13, 2013, we received purported Notice Letters that a Paragraph IV Patent Certification had been filed by Alvogen Pine Brook, Inc., or Alvogen, advising that Alvogen had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. In the Notice Letters, Alvogen noted that as of March 13, 2013, the FDA had not accepted the ANDA for review. Alvogen has agreed that their Notice Letters do not constitute Notice as described in 21 U.S.C. 355(j)(2)(B).

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On July 15, 2013, we received a Paragraph IV Patent Certification from Watson Laboratories, Inc. — Florida, or Watson, advising that Watson had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Watson has not advised us as to the timing or status of the FDA's review of its filing. On August 26, 2013, we, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against Watson, Actavis Pharma, Inc., Andrx Corp., and Actavis, Inc., or collectively WLF. The lawsuit alleges that WLF has infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124, and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS containing 1 mg, 2 mg, and 5 mg of prednisone prior to the expiration of the patents. The subject patents are listed in the FDA's Orange Book. The commencement of the patent infringement lawsuit stays, or bars, FDA approval of WLF's ANDA for 30 months or until an earlier district court decision that the subject patents are not infringing or invalid.

On or about August 12, 2013, we received a Notice of Opposition to a European patent covering LODOTRA, EP 2049123, filed by Laboratorios Licons, S.A. In the European Union, the grant of a patent may be opposed by one or more private parties.

On September 12, 2013, we received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Par Pharmaceutical, Inc. has not advised us as to the timing or status of the FDA's review of its filing. On October 22, 2013, we, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against Par. The lawsuit alleges that Par has infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124 and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS prior to the expiration of the patents. The subject patents are listed in the FDA's Orange Book. On November 20, 2013, we were notified by counsel for Par that Par Pharmaceutical, Inc. had elected to withdraw its ANDA with the FDA for a generic version of RAYOS containing 2 mg and 5 mg of prednisone. On December 5, 2013, we entered into a Stipulation of Dismissal with Par Pharmaceutical, Inc. whereby Par Pharmaceutical, Inc. agreed to withdraw its application to market a generic version of RAYOS.

If we are unsuccessful in any of the on-going patent litigations, we will likely face generic competition with respect to VIMOVO and/or RAYOS and our sales of VIMOVO and/or RAYOS will be substantially harmed.

The availability and price of our competitors' products could limit the demand, and the price we are able to charge, for our products. We will not successfully execute on our business objectives if the market acceptance of our products is inhibited by price competition, if physicians are reluctant to switch from existing products to our products, or if physicians switch to other new products or choose to reserve our products for use in limited patient populations.

In addition, established pharmaceutical companies may invest heavily to accelerate discovery and development of novel compounds or to in-license and develop novel compounds that could make our products obsolete. Our ability to compete successfully with these companies and other potential competitors will depend largely on our ability to leverage our experience in clinical, regulatory and commercial development to:

- develop, acquire or in-license medicines that are superior to other products in the market;
- attract qualified clinical, regulatory, and sales and marketing personnel;
- obtain patent and/or other proprietary protection for our products and technologies;
- obtain required regulatory approvals; and
- successfully collaborate with pharmaceutical companies in the discovery, development and commercialization of new product candidates.

In addition, any new product that competes with an approved product must demonstrate compelling advantages in efficacy, convenience, tolerability and safety in order to be approved and overcome price competition and to be commercially successful. Accordingly, our competitors may succeed in obtaining patent protection, obtaining FDA approval or discovering, developing and commercializing medicines before we do, which would have a material adverse impact on our business. The inability to compete with existing products or subsequently introduced products would have a material adverse impact on our business, financial condition and prospects.

*A variety of risks associated with operating our business and marketing our products internationally could materially adversely affect our business.*

In addition to our U.S. operations, we have operations in Switzerland and Germany. Moreover, LODOTRA is currently being marketed in a limited number of countries outside the United States, and Mundipharma is in the process of obtaining pricing and reimbursement approval for, and preparing to market, LODOTRA in other European countries, as well as in certain Asian, Latin American, Middle Eastern and African countries. Also, Grünenthal S.A. is in the registration process for the commercialization of DUEXIS in Latin America. We face risks associated with our international operations, including possible unfavorable regulatory, pricing and reimbursement, political, tax and labor conditions, which could harm our business. We are subject to numerous risks associated with international business activities, including:

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- compliance with differing or unexpected regulatory requirements for our products;
- compliance with Swiss laws with respect to our Horizon Pharma AG subsidiary, including laws requiring maintenance of cash in the subsidiary to avoid overindebtedness, which requires Horizon Pharma AG to maintain assets in excess of its liabilities;
- difficulties in staffing and managing foreign operations;
- in certain circumstances, including with respect to the commercialization of LODOTRA in Europe and certain Asian, Latin American, Middle Eastern and African countries, and commercialization of DUEXIS in Latin America, increased dependence on the commercialization efforts and regulatory compliance of our distributors or strategic partners;
- compliance with German laws with respect to our Horizon Pharma GmbH subsidiary through which Horizon Pharma AG conducts most of its European operations;
- foreign government taxes, regulations and permit requirements;
- United States and foreign government tariffs, trade restrictions, price and exchange controls and other regulatory requirements;
- anti-corruption laws, including the Foreign Corrupt Practices Act;
- economic weakness, including inflation, natural disasters, war, events of terrorism or political instability in particular foreign countries;
- fluctuations in currency exchange rates, which could result in increased operating expenses and reduced revenues, and other obligations related to doing business in another country;
- compliance with tax, employment, immigration and labor laws, regulations and restrictions for employees living or traveling abroad;
- workforce uncertainty in countries where labor unrest is more common than in the United States;
- production shortages resulting from any events affecting raw material supply or manufacturing capabilities abroad;
- changes in diplomatic and trade relationships; and
- challenges in enforcing our contractual and intellectual property rights, especially in those foreign countries that do not respect and protect intellectual property rights to the same extent as the United States.

These and other risks associated with our international operations may materially adversely affect our business, financial condition and results of operations.

*If we fail to develop, acquire or in-license other product candidates or products, our business and prospects would be limited.\**

A key element of our strategy is to develop, acquire or in-license and commercialize a portfolio of other product candidates in addition to DUEXIS and RAYOS/LODOTRA, such as our November 2013 acquisition of the U.S. rights to VIMOVO and our addition of ACTIMMUNE pending our merger with Vidara Therapeutics International Ltd., or Vidara. Because we do not have proprietary drug discovery technology, the success of this strategy depends in large part upon the combination of our regulatory, development and commercial capabilities and expertise and our ability to identify, select and acquire or in-license clinically enabled product candidates for the treatment of pain-related diseases, or for therapeutic indications that complement or augment our current targets, or that otherwise fit into our development or strategic plans on terms that are acceptable to us. Identifying, selecting and acquiring, licensing promising product candidates requires substantial technical, financial and human resources expertise. Efforts to do so may not result in the actual acquisition or license of a particular product candidate, potentially resulting in a diversion of our management's time and the expenditure of our resources with no resulting benefit. If we are unable to identify, select and acquire or license suitable product candidates from third parties on terms acceptable to us, our business and prospects will be limited.

Moreover, any product candidate we identify, select and acquire or license may require additional, time-consuming development or regulatory efforts prior to commercial sale, including preclinical studies if applicable, and extensive clinical testing and approval by the FDA and applicable foreign regulatory authorities. All product candidates are prone to the risk of failure that is inherent in pharmaceutical product development, including the possibility that the product candidate will not be shown to be sufficiently safe and/or effective for approval by regulatory authorities. In addition, we cannot assure you that any such products that are approved will be manufactured or produced economically, successfully commercialized or widely accepted in the marketplace or be more effective or desired than other commercially available alternatives.

In addition, if we fail to successfully commercialize and further develop our products, there is a greater likelihood that we will fail to successfully develop a pipeline of other product candidates to follow our existing products, and our business and prospects would therefore be harmed.

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*Our November 2013 acquisition of the U.S. rights to VIMOVO, our proposed merger with Vidara, and any other strategic transactions that we may pursue in the future could have a variety of negative consequences, and we may not realize the benefits of such transactions or attempts to engage in such transactions.\**

We acquired the U.S. rights to VIMOVO in November 2013 and from time to time, we may seek to engage in additional strategic transactions with third parties, such as our proposed merger with Vidara, other acquisitions of companies or divisions of companies, asset purchases or in-licensing of product candidates or technologies that we believe will complement or augment our existing business. We may also consider a variety of other business arrangements, including spin-offs, strategic partnerships, joint ventures, restructurings, divestitures, business combinations and other investments. Any such transaction may require us to incur non-recurring and other charges, increase our near and long-term expenditures, pose significant integration challenges, create additional tax, legal, accounting and operational complexities in our business, require additional expertise, result in dilution to our existing stockholders and disrupt our management and business, which could harm our operations and financial results. For example, in connection with our acquisition of the U.S. rights to VIMOVO, we assumed primary responsibility for the existing patent infringement litigation with respect to VIMOVO, and have also agreed to reimburse certain legal expenses of Pozen with respect to its continued involvement in such litigation, and we expect that this will result in substantial on-going expenses and potential distractions to our management team. Because VIMOVO is approved for similar indications and prescribed to similar patients compared to DUEXIS, we may also experience lower prescriptions of DUEXIS as we seek to commercialize VIMOVO, particularly from the approximately 30% of physicians that currently prescribe both products. Moreover, we face significant competition in seeking appropriate strategic partners and transactions, and the negotiation process for any strategic transaction can be time-consuming and complex. In addition, we may not be successful in our efforts to engage in certain strategic transactions because our financial resources and research and development pipeline may be insufficient, our product candidates and programs may be deemed to be at too early of a stage of development for collaborative effort and/or third parties may not view our product candidates and programs as having the requisite potential. We may not be able to expand our business or realize our strategic goals if we do not have sufficient funding or cannot borrow or raise additional capital. There is no assurance that following our acquisition of the U.S. rights to VIMOVO, our proposed merger with Vidara or any other strategic transaction, we will achieve the anticipated revenues or net income that we believe to justify such transaction. Any failures or delays in entering into strategic transactions could also delay or negatively impact the development and commercialization of our product candidates and reduce their competitiveness even if they reach the market. In addition, any failures or delays in entering into strategic transactions anticipated by analysts or the investment community could result in a decline in our stock price.

*If we are not successful in attracting and retaining highly qualified personnel, we may not be able to successfully implement our business strategy.\**

Our ability to compete in the highly competitive biotechnology and pharmaceuticals industries depends upon our ability to attract and retain highly qualified managerial, scientific and medical personnel. We are highly dependent on our management, sales and marketing and scientific and medical personnel, including our Chairman, President and Chief Executive Officer, Timothy P. Walbert; our Executive Vice President and Chief Business Officer, Robert F. Carey; our Executive Vice President and Chief Financial Officer, Robert J. De Vaere; our Executive Vice President, Development, Manufacturing and Regulatory Affairs and Chief Medical Officer, Jeffrey W. Sherman, M.D.; and our Executive Vice President and Chief Commercial Officer, Todd Smith. In order to retain valuable employees at our company, in addition to salary and cash incentives, we provide incentive stock options that vest over time. The value to employees of stock options that vest over time will be significantly affected by movements in our stock price that are beyond our control, and may at any time be insufficient to counteract more lucrative offers from other companies.

Despite our efforts to retain valuable employees, members of our management, sales and marketing, regulatory, clinical affairs, medical affairs and development teams may terminate their employment with us on short notice. Although we have written employment arrangements with all of our employees, these employment arrangements generally provide for at-will employment, which means that our employees can leave our employment at any time, with or without notice. The loss of the services of any of our executive officers or other key employees and our inability to find suitable replacements could potentially harm our business, financial condition and prospects. We do not maintain “key man” insurance policies on the lives of these individuals or the lives of any of our other employees. Our success also depends on our ability to continue to attract, retain and motivate highly skilled junior, mid-level, and senior managers as well as junior, mid-level, and senior sales and marketing and scientific and medical personnel.

Many of the other biotechnology and pharmaceutical companies with whom we compete for qualified personnel have greater financial and other resources, different risk profiles and longer histories in the industry than we do. They also may provide more diverse opportunities and better chances for career advancement. Some of these characteristics may be more appealing to high quality candidates than that which we have to offer. If we are unable to continue to attract and retain high quality personnel, the rate and success at which we can develop and commercialize products and product candidates will be limited.

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*If we fail to obtain and maintain approval from regulatory authorities in international markets for DUEXIS and LODOTRA and any future product candidates for which we have rights in international markets, our market opportunities will be limited and our business will be adversely impacted.*

Sales of our products and product candidates outside of the United States will be subject to foreign regulatory requirements governing clinical trials and marketing approval. Even if the FDA grants marketing approval for a product candidate, comparable regulatory authorities of foreign countries must also approve the manufacturing and marketing of our product candidates in those countries. Approval procedures vary among jurisdictions and can involve requirements and administrative review periods different from, and greater than, those in the United States, including additional preclinical studies or clinical trials. In many countries outside the United States, a product candidate must be approved for reimbursement before it can be approved for sale in that country. In some cases, the price that we intend to charge for our products is also subject to approval. Obtaining foreign regulatory approvals and compliance with foreign regulatory requirements could result in significant delays, difficulties and costs for us and could delay or prevent the introduction of our products in certain countries. Further, clinical trials conducted in one country may not be accepted by regulatory authorities in other countries and regulatory approval in one country does not ensure approval in any other country, while a failure or delay in obtaining regulatory approval in one country may have a negative effect on the regulatory approval process in others.

*We are, with respect to DUEXIS, VIMOVO and RAYOS, and will be, with respect to any other product candidate for which we obtain FDA approval or acquire or in-license, subject to ongoing FDA obligations and continued regulatory review, which may result in significant additional expense. Additionally, any other product candidate, if approved by the FDA, could be subject to labeling and other restrictions and market withdrawal, and we may be subject to penalties if we fail to comply with regulatory requirements or experience unanticipated problems with our products.*

Any regulatory approvals that we obtain for our product candidates may also be subject to limitations on the approved indicated uses for which the product may be marketed or to the conditions of approval, or contain requirements for potentially costly post-marketing testing, including Phase 4 clinical trials and surveillance to monitor the safety and efficacy of the product candidate. In addition, if the FDA approves a product candidate, the manufacturing processes, labeling, packaging, distribution, adverse event reporting, storage, advertising, promotion and recordkeeping for the product will be subject to extensive and ongoing regulatory requirements. These requirements include submissions of safety and other post-marketing information and reports, registration, as well as continued compliance with current good manufacturing practices, or cGMPs, good clinical practices, or GCPs, international conference on harmonization regulations, or ICH regulations, and good laboratory practices, or GLPs, which are regulations and guidelines enforced by the FDA for all of our products in clinical development, for any clinical trials that we conduct post-approval. For example, as post-marketing requirements for DUEXIS, we are required by the FDA to develop a pediatric formulation for DUEXIS and conduct two clinical studies of the drug product for pediatric populations. In addition, in connection with our November 2013 acquisition of the U.S. rights to VIMOVO, we assumed responsibility for completing an ongoing Pediatric Research Equity Act post-marketing requirement study in children 12 years to 16 years and 11 months of age with Juvenile RA for which the FDA recently granted an extension with a final report due date of December 2015. Later discovery of previously unknown problems with a product, including adverse events of unanticipated severity or frequency, or with our third-party manufacturers or manufacturing processes, or failure to comply with regulatory requirements, may result in, among other things:

- restrictions on the marketing or manufacturing of the product, withdrawal of the product from the market, or voluntary or mandatory product recalls;
- fines, Warning Letters or holds on clinical trials;
- refusal by the FDA to approve pending applications or supplements to approved applications filed by us or our strategic partners, or suspension or revocation of product license approvals;
- product seizure or detention, or refusal to permit the import or export of products; and
- injunctions, the imposition of civil or criminal penalties, or exclusions.

If we are not able to maintain regulatory compliance, we may lose any marketing approval that we may have obtained and we may not achieve or sustain profitability, which would have a material adverse effect on our business, results of operations, financial condition and prospects.

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*Coverage and reimbursement may not be available, or reimbursement may be available at only limited levels, for our products, which could make it difficult for us to sell our products profitably or to successfully execute planned product price increases.*

Market acceptance and sales of our products will depend in large part on global coverage and reimbursement policies and may be affected by future healthcare reform measures, both in the United States and other key international markets. Successful commercialization of our products will depend in part on the availability of governmental and third-party payer reimbursement for the cost of our products. Government health administration authorities, private health insurers and other organizations generally provide reimbursement for healthcare. In particular, in the United States, private health insurers and other third-party payers often provide reimbursement for products and services based on the level at which the government (through the Medicare or Medicaid programs) provides reimbursement for such treatments. In the United States, the European Union and other significant or potentially significant markets for our products and product candidates, government authorities and third-party payers are increasingly attempting to limit or regulate the price of medical products and services, particularly for new and innovative products and therapies, which has resulted in lower average selling prices. Further, the increased emphasis on managed healthcare in the United States and on country and regional pricing and reimbursement controls in the European Union will put additional pressure on product pricing, reimbursement and usage, which may adversely affect our product sales and results of operations. These pressures can arise from rules and practices of managed care groups, judicial decisions and governmental laws and regulations related to Medicare, Medicaid and healthcare reform, pharmaceutical reimbursement policies and pricing in general. These pressures may create negative reactions to any product price increases, or limit the amount by which we may be able to increase our product prices, which may adversely affect our product sales and results of operations.

Outside of the United States, the success of our products, including LODOTRA and, if widely approved, DUEXIS, will depend largely on obtaining and maintaining government coverage, because in many countries patients are unlikely to use prescription drugs that are not covered by their government healthcare programs. To date, LODOTRA is approved in over 30 countries outside the United States, and reimbursement for LODOTRA has been obtained in Germany, Italy, Sweden and Switzerland. Mundipharma is seeking coverage for LODOTRA in a number of countries and currently sells LODOTRA without coverage in a limited number of countries. Negotiating coverage and reimbursement with governmental authorities can delay commercialization by 12 months or more. Coverage and reimbursement policies may adversely affect our ability to sell our products on a profitable basis. In many international markets, governments control the prices of prescription pharmaceuticals, including through the implementation of reference pricing, price cuts, rebates, revenue-related taxes and profit control, and we expect prices of prescription pharmaceuticals to decline over the life of the product or as volumes increase. Recently, many countries in the European Union have increased the amount of discounts required on pharmaceutical products, which we believe has impacted the reimbursement rates and timing to launch for LODOTRA to date, and we expect these discounts to continue as countries attempt to manage healthcare expenditures, especially in light of current economic conditions. For example, legislation was recently enacted in Germany that will increase the rebate on prescription pharmaceuticals and likely lower the revenues from the sale of LODOTRA in Germany that we would otherwise receive. As a result of these pricing practices, it may become difficult to achieve profitability or expected rates of growth in revenue or results of operations. Any shortfalls in revenue could adversely affect our business, financial condition and results of operations.

In light of such policies and the uncertainty surrounding proposed regulations and changes in the coverage and reimbursement policies of governments and third-party payers, we cannot be sure that coverage and reimbursement will be available for DUEXIS or LODOTRA in any additional markets or for any other product candidates that we may develop. Also, we cannot be sure that reimbursement amounts will not reduce the demand for, or the price of, our products. If coverage and reimbursement is not available or is available only at limited levels, we may not be able to successfully commercialize our products.

We expect to experience pricing pressures in connection with the sale of our products, due to the trend toward managed healthcare, the increasing influence of health maintenance organizations and additional legislative proposals. There may be additional pressure by payers and healthcare providers to use generic drugs that contain the active ingredients found in DUEXIS, VIMOVO and RAYOS/LODOTRA or any other product candidates that we may develop, acquire or in-license. If we fail to successfully secure and maintain coverage and adequate reimbursement for our products or are significantly delayed in doing so, we will have difficulty achieving market acceptance of our products and expected revenue and profitability which would have a material adverse effect on our business, results of operations, financial condition and prospects. We may also experience pressure from payers concerning certain promotional approaches that we may implement such as co-pay programs whereby we assist patients to achieve an acceptable co-pay for our product, which may be contrary to payers' financial interests. If we are unsuccessful with our co-pay initiatives, we would be at a competitive disadvantage in terms of pricing versus preferred branded and generic competitors.

*We are subject to federal, state and foreign healthcare laws and regulations and implementation or changes to such healthcare laws and regulations could adversely affect our business and results of operations.\**

The United States and some foreign jurisdictions are considering or have enacted a number of legislative and regulatory proposals to regulate and to change the healthcare system in ways that could affect our ability to sell our products profitably, described in greater detail in the Government Regulation Section of this report. In the United States and elsewhere, there is significant interest in promoting changes in healthcare systems with the stated goals of containing healthcare costs, improving quality and/or expanding access. In the United States, the pharmaceutical industry has been a particular focus of these efforts and has been significantly affected by major legislative initiatives.

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If we are found to be in violation of any of these laws or any other federal or state regulations, we may be subject to civil and/or criminal penalties, damages, fines, exclusion from federal health care programs and the restructuring of our operations. Any of these could have a material adverse effect on our business and financial results. Since many of these laws have not been fully interpreted by the courts, there is an increased risk that we may be found in violation of one or more of their provisions. Any action against us for violation of these laws, even if we ultimately are successful in our defense, will cause us to incur significant legal expenses and divert our management's attention away from the operation of our business.

We expect that the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Affordability Reconciliation Act, or collectively, the PPACA, as well as other healthcare reform measures that may be adopted in the future, may result in more rigorous coverage criteria and in additional downward pressure on the price that we may receive for any approved product. An expansion in the government's role in the U.S. healthcare industry may cause general downward pressure on the prices of prescription drug products, lower reimbursements for providers using our products, reduce product utilization and adversely affect our business and results of operations. It is unclear whether and to what extent, if at all, other anticipated developments resulting from the federal healthcare reform legislation, such as an increase in the number of people with health insurance and an increased focus on preventive medicine, may provide us additional revenue to offset the annual excise tax (on certain drug product sales) enacted under the PPACA, subject to limited exceptions. It is possible that the tax burden, if we are not excepted, would adversely affect our financial performance, which in turn could cause the price of our stock to decline. Any reduction in reimbursement from government programs may result in a similar reduction in payments from private payers. The implementation of cost containment measures or other healthcare reforms may prevent us from being able to generate revenue, attain profitability, or commercialize our current products and/or those for which we may receive regulatory approval in the future.

*We are subject, directly or indirectly, to federal and state healthcare fraud and abuse and false claims laws and regulations. Prosecutions under such laws have increased in recent years and we may become subject to such litigation. If we are unable to comply, or have not fully complied, with such laws, we could face substantial penalties.*

In the United States, we are subject directly, or indirectly through our customers, to various state and federal fraud and abuse laws, including, without limitation, the federal Anti-Kickback Statute, the federal False Claims Act, federal and state privacy and security laws, sunshine laws, government price reporting laws, and other fraud laws, as described in greater detail in the Government Regulation Section of this report. These laws may impact, among other things, our proposed sales, marketing and educational programs, as well as other possible relationships with customers, payers, and patients.

Compliance with these laws, including the development of a comprehensive compliance program, is difficult, costly and time consuming and companies that do not comply with these state laws face civil penalties. Even if we structure our programs with the intent of compliance with such laws, there can be no certainty that we would not need to defend our business activities against enforcement or litigation, in light of the fact that there is significant enforcement interest in pharmaceutical companies in the United States, and some of the applicable laws are quite broad in scope with very narrow exceptions.

We are unable to predict whether we could be subject to actions under any of these or other fraud and abuse laws, or the impact of such actions. If we are found to be in violation of any of the laws described above and other applicable state and federal fraud and abuse laws, we may be subject to penalties, including civil and criminal penalties, damages, fines, exclusion from government healthcare reimbursement programs and the curtailment or restructuring of our operations, all of which could have a material adverse effect on our business and results of operations.

*Our products or any other product candidate that we develop may cause undesirable side effects or have other properties that could delay or prevent regulatory approval or commercialization, result in product re-labeling or withdrawal from the market or have a significant impact on customer demand.*

Undesirable side effects caused by any product candidate that we develop could result in the denial of regulatory approval by the FDA or other regulatory authorities for any or all targeted indications, or cause us to evaluate the future of our development programs. In our two Phase 3 clinical trials with DUEXIS, the most commonly reported treatment-emergent adverse events were nausea, dyspepsia, diarrhea, constipation and upper respiratory tract infection. In Phase 3 endoscopic registration clinical trials with VIMOVO, the most commonly reported treatment-emergent adverse events were erosive gastritis, dyspepsia, gastritis, diarrhea, gastric ulcer, upper abdominal pain, nausea and upper respiratory tract infection. The most commonly reported treatment-emergent adverse events in the Phase 3 clinical trials with RAYOS/LODOTRA included flare in RA-related symptoms, abdominal pain, nasopharyngitis, headache, flushing, upper respiratory tract infection, back pain and weight gain. In addition, the FDA or other regulatory authorities may require, or we may undertake, additional clinical trials to support the safety profile of our product candidates.



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In addition, if we or others identify undesirable side effects caused by our products or any other product candidate that we may develop that receives marketing approval, or if there is a perception that the product is associated with undesirable side effects:

- regulatory authorities may require the addition of labeling statements, such as a “black box” warning or a contraindication;
- regulatory authorities may withdraw their approval of the product or place restrictions on the way it is prescribed; and
- we may be required to change the way the product is administered, conduct additional clinical trials or change the labeling of the product or implement a risk evaluation and mitigation strategy.

If any of these events occurred with respect to our products, our ability to generate significant revenues from the sale of these products would be significantly harmed.

*We rely on third parties to conduct our preclinical and clinical trials. If these third parties do not successfully carry out their contractual duties or meet expected deadlines or if they experience regulatory compliance issues, we may not be able to obtain regulatory approval for or commercialize our product candidates and our business could be substantially harmed.\**

We have agreements with third-party contract research organizations, or CROs, to conduct our clinical programs, including those required for post-marketing commitments. We may also have the need to enter into other such agreements in the future if we were to develop other product candidates. We rely heavily on these parties for the execution of our clinical studies, and control only certain aspects of their activities. Nevertheless, we are responsible for ensuring that each of our studies is conducted in accordance with the applicable protocol. We and our CROs are required to comply with current GCP or ICH regulations. The FDA enforces these GCP or ICH regulations through periodic inspections of trial sponsors, principal investigators and trial sites. If we or our CROs fail to comply with applicable GCP or ICH regulations, the data generated in our clinical trials may be deemed unreliable and our submission of marketing applications may be delayed or the FDA may require us to perform additional clinical trials before approving our marketing applications. We cannot assure you that, upon inspection, the FDA will determine that any of our clinical trials comply or complied with GCP or ICH regulations. In addition, our clinical trials must be conducted with product produced under cGMP regulations, and require a large number of test subjects. Our failure to comply with these regulations may require us to repeat clinical trials, which would delay the regulatory approval process. Moreover, our business may be implicated if any of our CROs violates federal or state fraud and abuse or false claims laws and regulations or healthcare privacy and security laws.

If any of our relationships with these third-party CROs terminate, we may not be able to enter into arrangements with alternative CROs on commercially reasonable terms, or at all. If CROs do not successfully carry out their contractual duties or obligations or meet expected deadlines, if they need to be replaced or if the quality or accuracy of the clinical data they obtain is compromised due to the failure to adhere to our clinical protocols or regulatory requirements or for other reasons, our clinical trials may be extended, delayed or terminated and we may not be able to obtain regulatory approval for or successfully commercialize our products and product candidates. As a result, our results of operations and the commercial prospects for our products and product candidates would be harmed, our costs could increase and our ability to generate revenues could be delayed.

Switching or adding additional CROs can involve substantial cost and require extensive management time and focus. In addition, there is a natural transition period when a new CRO commences work. As a result, delays may occur, which can materially impact our ability to meet our desired clinical development timelines. Though we carefully manage our relationships with our CROs, there can be no assurance that we will not encounter similar challenges or delays in the future or that these delays or challenges will not have a material adverse impact on our business, financial condition or prospects.

In addition, pursuant to a March 2011 letter agreement and in connection with our waiver of certain milestone payments, Mundipharma initiated a separate Phase 3 clinical trial for LODOTRA for the potential treatment of polymyalgia rheumatica, or PMR. We had limited control over the timing and implementation of the planned clinical trial and in February 2014, Mundipharma informed us that they had terminated the clinical trial primarily due to recruitment difficulties based on the inclusion criteria and as a result of the cessation of production of the comparator product Decortin® 1mg.

We also, as part of the April 23, 2011 FDA approval of DUEXIS, have a commitment under the Pediatric Research Equity Act, or PREA, to conduct an assessment of the safety and effectiveness of the product for the claimed indication in pediatric patients. The PREA PMR study is currently being delayed by the FDA and we are in discussions with the FDA to resolve this matter.

In addition, in connection with our November 2013 acquisition of the U.S. rights to VIMOVO, we assumed responsibility for completing an ongoing PREA post-marketing requirement study in children 12 years to 16 years and 11 months of age with Juvenile Idiopathic Arthritis for which the FDA recently granted an extension with a final report due date of December 2015. Although we are committed to carrying out these commitments, there are challenges in conducting studies in pediatric patients including availability of study sites, patients, and obtaining parental informed consent.

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*Clinical drug development involves a lengthy and expensive process with an uncertain outcome, and results of earlier studies and trials may not be predictive of future trial results.*

Clinical testing is expensive and can take many years to complete, and its outcome is uncertain. Failure can occur at any time during the clinical trial process. The results of preclinical studies and early clinical trials of potential product candidates may not be predictive of the results of later-stage clinical trials. Product candidates in later stages of clinical trials may fail to show the desired safety and efficacy traits despite having progressed through preclinical studies and initial clinical testing.

To the extent that we are required to conduct additional clinical development of DUEXIS, VIMOVO or RAYOS/LODOTRA or we conduct clinical development of earlier stage product candidates or for additional indications for RAYOS/LODOTRA, we may experience delays in these clinical trials. While we are currently not focusing any resources on internal development of new product candidates, we do not know whether any additional clinical trials will be initiated in the future, begin on time, need to be redesigned, enroll patients on time or be completed on schedule, if at all. Clinical trials can be delayed for a variety of reasons, including delays related to:

- obtaining regulatory approval to commence a trial;
- reaching agreement on acceptable terms with prospective CROs and clinical trial sites, the terms of which can be subject to extensive negotiation and may vary significantly among different CROs and trial sites;
- obtaining institutional review board or ethics committee approval at each site;
- recruiting suitable patients to participate in a trial;
- having patients complete a trial or return for post-treatment follow-up;
- clinical sites dropping out of a trial;
- adding new sites; or
- manufacturing sufficient quantities of product candidates for use in clinical trials.

Patient enrollment, a significant factor in the timing of clinical trials, is affected by many factors including the size and nature of the patient population, the proximity of patients to clinical sites, the eligibility criteria for the trial, the design of the clinical trial, competing clinical trials and clinicians' and patients' perceptions as to the potential advantages of the product candidate being studied in relation to other available therapies, including any new drugs that may be approved for the indications we are investigating. Furthermore, we expect to rely on CROs and clinical trial sites to ensure the proper and timely conduct of our future clinical trials and while we intend to have agreements governing their committed activities, we will have limited influence over their actual performance.

We could encounter delays if prescribing physicians encounter unresolved ethical issues associated with enrolling patients in clinical trials of our product candidates in lieu of prescribing existing treatments that have established safety and efficacy profiles. Further, a clinical trial may be suspended or terminated by us, our collaborators, the FDA or other regulatory authorities due to a number of factors, including failure to conduct the clinical trial in accordance with regulatory requirements or our clinical protocols, inspection of the clinical trial operations or trial site by the FDA or other regulatory authorities resulting in the imposition of a clinical hold, unforeseen safety issues or adverse side effects, failure to demonstrate a benefit from using a drug, changes in governmental regulations or administrative actions or lack of adequate funding to continue the clinical trial. If we experience delays in the completion of, or if we terminate, any clinical trial of our product candidates, the commercial prospects of our product candidates will be harmed, and our ability to generate product revenues from any of these product candidates will be delayed. In addition, any delays in completing our clinical trials will increase our costs, slow down our product development and approval process and jeopardize our ability to commence product sales and generate revenues. Any of these occurrences may harm our business, financial condition, results of operations and prospects significantly. In addition, many of the factors that cause, or lead to, a delay in the commencement or completion of clinical trials may also ultimately lead to the denial of regulatory approval of our product candidates.

*Business interruptions could seriously harm our future revenue and financial condition and increase our costs and expenses.*

Our operations could be subject to earthquakes, power shortages, telecommunications failures, water shortages, floods, hurricanes, typhoons, fires, extreme weather conditions, medical epidemics and other natural or man-made disasters or business interruptions. While we carry insurance for certain of these events and have implemented disaster management plans and contingencies, the occurrence of any of these business interruptions could seriously harm our business and financial condition and increase our costs and expenses. A majority of our management operates in our principal executive offices located in Deerfield, Illinois. If our Deerfield offices were affected by a natural or man-made disaster or other business interruption, our ability to manage our domestic and foreign operations could be impaired, which could materially and adversely affect our results of operations and financial condition. We currently rely, and intend to rely in the future, on third-party manufacturers and suppliers to produce our products. Our ability to obtain commercial supplies of our products could be disrupted and our results of operations and financial condition could be materially and adversely affected if the operations of these suppliers were affected by a man-made or natural disaster or other business interruption. The ultimate impact of such events on us, our significant suppliers and our general infrastructure is unknown.

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*If product liability lawsuits are brought against us, we may incur substantial liabilities and may be required to limit commercialization of our products.*

We face an inherent risk of product liability as a result of the commercial sales of our products and the clinical testing of our product candidates. For example, we may be sued if any of our products or product candidates allegedly causes injury or is found to be otherwise unsuitable during clinical testing, manufacturing, marketing or sale. Any such product liability claims may include allegations of defects in manufacturing, defects in design, a failure to warn of dangers inherent in the product, negligence, strict liability or a breach of warranties. Claims could also be asserted under state consumer protection acts. If we cannot successfully defend ourselves against product liability claims, we may incur substantial liabilities or be required to limit commercialization of our product candidates. Even a successful defense would require significant financial and management resources. Regardless of the merits or eventual outcome, liability claims may result in:

- decreased demand for our products or product candidates that we may develop;
- injury to our reputation;
- withdrawal of clinical trial participants;
- initiation of investigations by regulators;
- costs to defend the related litigation;
- a diversion of management's time and our resources;
- substantial monetary awards to trial participants or patients;
- product recalls, withdrawals or labeling, marketing or promotional restrictions;
- loss of revenue;
- exhaustion of any available insurance and our capital resources;
- the inability to commercialize our products or product candidates; and
- a decline in our stock price.

Our inability to obtain and retain sufficient product liability insurance at an acceptable cost to protect against potential product liability claims could prevent or inhibit the commercialization of products we develop. We currently carry product liability insurance covering our clinical studies and commercial product sales in the amount of \$20 million in the aggregate. Although we maintain such insurance, any claim that may be brought against us could result in a court judgment or settlement in an amount that is not covered, in whole or in part, by our insurance or that is in excess of the limits of our insurance coverage. If we determine that it is prudent to increase our product liability coverage due to the on-going commercialization of DUEXIS, VIMOVO and RAYOS in the United States and/or the potential commercial launches of DUEXIS and LODOTRA in additional markets, we may be unable to obtain such increased coverage on acceptable terms or at all. Our insurance policies also have various exclusions, and we may be subject to a product liability claim for which we have no coverage. We will have to pay any amounts awarded by a court or negotiated in a settlement that exceed our coverage limitations or that are not covered by our insurance, and we may not have, or be able to obtain, sufficient capital to pay such amounts.

*Our business involves the use of hazardous materials, and we and our third-party manufacturers must comply with environmental laws and regulations, which can be expensive and restrict how we do business.*

Our third-party manufacturers' activities involve the controlled storage, use and disposal of hazardous materials owned by us, including the components of our product candidates and other hazardous compounds. We and our manufacturers are subject to federal, state and local as well as foreign laws and regulations governing the use, manufacture, storage, handling and disposal of these hazardous materials. Although we believe that the safety procedures utilized by our third-party manufacturers for handling and disposing of these materials comply with the standards prescribed by these laws and regulations, we cannot eliminate the risk of accidental contamination or injury from these materials. In the event of an accident, state, federal or foreign authorities may curtail the use of these materials and interrupt our business operations. We do not currently maintain hazardous materials insurance coverage. If we are subject to any liability as a result of our third-party manufacturers' activities involving hazardous materials, our business and financial condition may be adversely affected. In the future we may seek to establish longer term third-party manufacturing arrangements, pursuant to which we would seek to obtain contractual indemnification protection from such third-party manufacturers potentially limiting this liability exposure.

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*Our employees may engage in misconduct or other improper activities, including noncompliance with regulatory standards and requirements and insider trading.*

We are exposed to the risk of employee fraud or other misconduct. Misconduct by employees could include intentional failures to comply with FDA regulations, provide accurate information to the FDA, comply with manufacturing standards we have established, comply with federal and state healthcare fraud and abuse laws and regulations, report financial information or data accurately or disclose unauthorized activities to us. In particular, sales, marketing and business arrangements in the healthcare industry are subject to extensive laws and regulations intended to prevent fraud, misconduct, kickbacks, self-dealing and other abusive practices. These laws and regulations may restrict or prohibit a wide range of pricing, discounting, marketing and promotion, sales commission, customer incentive programs and other business arrangements. Employee misconduct could also involve the improper use of information obtained in the course of clinical trials, which could result in regulatory sanctions and serious harm to our reputation. We have adopted a Code of Business Conduct and Ethics, but it is not always possible to identify and deter employee misconduct, and the precautions we take to detect and prevent this activity may not be effective in controlling unknown or unmanaged risks or losses or in protecting us from governmental investigations or other actions or lawsuits stemming from a failure to be in compliance with such laws or regulations. If any such actions are instituted against us, and we are not successful in defending ourselves or asserting our rights, those actions could have a significant impact on our business, including the imposition of significant fines or other sanctions.

### **Risks Related to Our Financial Position and Capital Requirements**

*We have incurred significant operating losses since our inception and anticipate that we will continue to incur losses for the foreseeable future.\**

We have a limited operating history. We have financed our operations primarily through equity and debt financings and the issuance of convertible notes and have incurred significant operating losses since our inception. We had net losses of \$206.3 million for the three months ended March 31, 2014 and \$149.0 million, \$87.8 million and \$113.3 million for the years ended December 31, 2013, 2012 and 2011, respectively. As of March 31, 2014, we had an accumulated deficit of \$663.4 million. We do not know whether or when we will become profitable. Our prior losses, combined with expected future losses, have had and will continue to have an adverse effect on our stockholders' deficit and working capital. Our losses have resulted principally from costs incurred in our development activities for our products and product candidates, commercialization activities related to our product launches and costs associated with derivative liability accounting. We anticipate that we will continue to incur operating losses until such time as the revenues we generate from the sale of our products are sufficient to cover our operating expenses.

*We have limited product revenues and other sources of revenues. We may never achieve or sustain profitability, which would depress the market price of our common stock and could cause our investors to lose all or a part of their investment.*

Our ability to become profitable depends upon our ability to generate revenues from sales of our products. DUEXIS was approved by the FDA on April 23, 2011, and we began generating revenues from sales of DUEXIS in late 2011 following the commercial launch in the United States. LODOTRA is approved for marketing in over 30 countries outside the United States, and to date we have generated only limited revenues from sales of LODOTRA. RAYOS was approved by the FDA on July 26, 2012, and we began marketing it in the United States through our full field sales force in late January 2013. Following our November 2013 acquisition of the U.S. rights to VIMOVO, we began commercialization efforts in the United States in the first quarter of 2014. We may never be able to successfully commercialize DUEXIS, VIMOVO or RAYOS or develop or commercialize other products in the United States, which we believe represents our most significant commercial opportunity, or sell DUEXIS in Europe, where we do not consider it to be material to our business. Our ability to generate future revenues depends heavily on our success in:

- commercializing DUEXIS, VIMOVO, RAYOS/LODOTRA and any other product candidates for which we obtain approval;
- securing additional foreign regulatory approvals for LODOTRA and DUEXIS; and
- developing, acquiring or in-licensing and commercializing a portfolio of other product candidates in addition to DUEXIS, VIMOVO and RAYOS/LODOTRA.

Even if we do generate additional product sales, we may never achieve or sustain profitability on a quarterly or annual basis. Our failure to become and remain profitable would depress the market price of our common stock and could impair our ability to raise capital, expand our business, diversify our product offerings or continue our operations.

*We may need to obtain additional financing to successfully commercialize or further develop DUEXIS, VIMOVO and RAYOS/LODOTRA, or to develop, acquire or in-license other products.\**

Our operations have consumed substantial amounts of cash since inception. We expect to continue to spend substantial amounts to:

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- commercialize DUEXIS, VIMOVO and RAYOS in the United States, including the substantial expansion of our sales force in connection with our November 2013 acquisition of the U.S. rights to VIMOVO;
- complete the regulatory approval process, and any future required clinical development related thereto, for DUEXIS, VIMOVO and RAYOS/LODOTRA;
- potentially acquire or in-license additional complementary products or products that augment our current therapeutic areas of focus;
- conduct clinical trials with respect to RAYOS/LODOTRA to generate clinical data in diseases beyond RA, such as PMR; and
- consummate our proposed merger with Vidara.

While we believe that our existing cash and cash equivalents at March 31, 2014, of \$103.4 million, together with interest thereon, will be sufficient to fund our operations to the point of generating positive cash flow based on our current expectations of continued revenue growth, we may need to raise additional funds if we choose to expand our commercialization or development efforts more rapidly than we presently anticipate, if we develop, acquire or in-license additional products or acquire companies, or if our revenues do not meet expectations.

We cannot be certain that additional funding will be available on acceptable terms, or at all. If we are unable to raise additional capital in sufficient amounts or on terms acceptable to us, we may have to significantly delay, scale back or discontinue the development or commercialization of one or more of our products or product candidates or one or more of our other research and development initiatives. We also could be required to:

- seek collaborators for one or more of our current or future product candidates at an earlier stage than otherwise would be desirable or on terms that are less favorable than might otherwise be available; or
- relinquish or license on unfavorable terms our rights to technologies or product candidates that we otherwise would seek to develop or commercialize ourselves.

While we have a commitment from Deerfield Management Company, L.P. for \$250.0 million to fund the required cash payments for our proposed merger with Vidara, we may not be able to meet the closing conditions or may otherwise have to seek alternative acquisition financing.

Even if we obtain additional financing, our Horizon Pharma AG subsidiary is subject to Swiss laws regarding overindebtedness that require Horizon Pharma AG to maintain assets in excess of its liabilities. As of March 31, 2014 and December 31, 2013, our Swiss subsidiary was overindebted, primarily as a result of operating losses at the subsidiary. We will continue to monitor and review steps to address any overindebtedness, until such time as our Swiss subsidiary may generate positive income at a statutory level, which could require us to have cash at our Swiss subsidiary in excess of its near term operating needs and could affect our ability to have sufficient cash at our U.S. subsidiary to meet its near term operating needs.

Any of the above events could significantly harm our business, financial condition and prospects and cause the price of our common stock to decline.

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

We may seek additional capital through a combination of private and public equity offerings, debt financings, receivables or royalty financings, strategic partnerships and alliances and licensing arrangements. 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 may include liquidation or other preferences that adversely affect the rights of our stockholders. Debt, receivables and royalty financings may be coupled with an equity component, such as warrants to purchase stock, which could also result in dilution of our existing stockholders' ownership. The incurrence of indebtedness would result in increased fixed payment obligations and could also result in certain restrictive covenants, such as limitations on our ability to incur additional debt, limitations on our ability to acquire or license intellectual property rights and other operating restrictions that could adversely impact our ability to conduct our business. If we raise additional funds through strategic partnerships and alliances and licensing arrangements with third parties, we may have to relinquish valuable rights to our product candidates, or grant licenses on terms that are not favorable to us.

In August 2012, we entered into a sales agreement with Cowen and Company, LLC, or Cowen, pursuant to which we may sell our common stock through Cowen in at-the-market, or ATM, offerings. Subject to the terms and conditions of the sales agreement, Cowen may sell the shares by methods deemed to be an ATM offering as defined in Rule 415 promulgated under the Securities Act of 1933, as amended, or the Securities Act, including sales made through The NASDAQ Global Market, on any other existing trading market for our common stock or to or through a market maker. The sale of additional shares of our common stock pursuant to the sales agreement will have a dilutive impact on our existing stockholders and could cause the market price of our common stock to be lower than it would otherwise be absent sales activities by Cowen. Sales of our common stock under the sales agreement, or the perception that such sales will occur, could also encourage short sales by third parties, which could contribute to a decline of our stock price.

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*We generally have broad discretion in the use of our cash and may not use it effectively.*

Our management has broad discretion in the application of our cash, and investors will be relying on the judgment of our management regarding the use of our cash. Our management may not apply our cash in ways that ultimately increase the value of any investment in our securities. We expect to use our existing cash to fund U.S. commercialization activities for DUEXIS, VIMOVO and RAYOS, to fund additional regulatory approvals of DUEXIS and RAYOS/LODOTRA, to fund development of RAYOS/LODOTRA for other indications and for working capital, capital expenditures and general corporate purposes. We may also invest our cash in short-term, investment-grade, interest-bearing securities. These investments may not yield a favorable return to our stockholders. If we do not invest or apply our cash in ways that enhance stockholder value, we may fail to achieve expected financial results, which could cause the price of our common stock to decline.

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

Under Section 382 of the Internal Revenue Code of 1986, as amended, if a corporation undergoes an “ownership change” (generally defined as a greater than 50% change (by value) in its equity ownership over a three year period), the corporation’s ability to use its pre-change net operating loss carryforwards and other pre-change tax attributes to offset its post-change income may be limited. In September 2012, the sale of our common stock and warrants to purchase shares of our common stock in a public equity offering triggered an “ownership change” limitation and, as a result, we will be subject to annual limits on our ability to utilize net operating loss carryforwards. We estimate that these annual limits will be a cumulative carryforward of \$49.9 million in 2014, and at a minimum, \$22.0 million for each of 2015 and 2016 assuming only the carryforward limitation. The net operating loss carryforward limitation is cumulative such that any use of the carryforwards below the limitation in one year will result in a corresponding increase in the limitation for the subsequent tax year. We may also experience ownership changes in the future as a result of consummating the proposed merger with Vidara or other subsequent shifts in our stock ownership, including potentially as a result of our debt and equity financings. Any limitation on our ability to use our net operating loss carryforwards will likely increase the taxes we would otherwise pay in future years if we were not subject to such limitations.

*Unstable market and economic conditions may have serious adverse consequences on our business, financial condition and stock price.\**

As widely reported, global credit and financial markets have experienced extreme disruptions in the past several years, including severely diminished liquidity and credit availability, declines in consumer confidence, declines in economic growth, increases in unemployment rates, and uncertainty about economic stability. While there has been some recent improvement in some of these financial metrics, there can be no assurance that further deterioration in credit and financial markets and confidence in economic conditions will not occur. Our general business strategy may be adversely affected by any such economic downturn, volatile business environment and continued unpredictable and unstable market conditions. If the current equity and credit markets deteriorate again, or do not improve, it may make any necessary debt or equity financing more difficult to complete, more costly, and more dilutive. Failure to secure any necessary financing in a timely manner and on favorable terms could have a material adverse effect on our growth strategy, financial performance and stock price and could require us to delay or abandon commercialization or development plans. In addition, there is a risk that one or more of our current service providers, manufacturers and other partners may not survive these difficult economic times, which could directly affect our ability to attain our operating goals on schedule and on budget.

At March 31, 2014, we had \$103.4 million of cash and cash equivalents consisting of cash and money market funds. While we are not aware of any downgrades, material losses, or other significant deterioration in the fair value of our cash equivalents or marketable securities since March 31, 2014, no assurance can be given that further deterioration in conditions of the global credit and financial markets would not negatively impact our current portfolio of cash equivalents or marketable securities or our ability to meet our financing objectives. Further dislocations in the credit market may adversely impact the value and/or liquidity of marketable securities owned by us.

*Changes in accounting rules or policies may affect our financial position and results of operations.*

U.S. generally accepted accounting principles and related implementation guidelines and interpretations can be highly complex and involve subjective judgments. Changes in these rules or their interpretation, the adoption of new guidance or the application of existing guidance to changes in our business could significantly affect our financial position and results of operations. In addition, the consolidation of Horizon Pharma AG and Horizon Pharma USA, Inc. adds additional complexity to the application of U.S. generally accepted accounting principles. Changes in the application of existing rules or guidance applicable to us or our wholly-owned subsidiaries could significantly affect our consolidated financial position and results of operations.

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*Servicing our debt requires a significant amount of cash, and we may not have sufficient cash flow from our business to pay our substantial debt.\**

In November 2013, we issued \$150.0 million aggregate principal amount of 5.00% Convertible Senior Notes due 2018, or the Convertible Senior Notes, to investors pursuant to note purchase agreements with such investors. As of March 31, 2014, all \$150.0 million principal amount of the Convertible Senior Notes remained outstanding. We also expect to substantially increase our overall indebtedness to finance our proposed merger transaction with Vidara. Our ability to make scheduled payments of the principal of, to pay interest on or to refinance our indebtedness, including the Convertible Senior Notes, depends on our future performance, which is subject to economic, financial, competitive and other factors beyond our control. Our business may not continue to generate cash flow from operations in the future sufficient to service our debt and make necessary capital expenditures. If we are unable to generate such cash flow, we may be required to adopt one or more alternatives, such as selling assets, restructuring debt or obtaining additional equity capital on terms that may be onerous or highly dilutive. Our ability to refinance our indebtedness will depend on the capital markets and our financial condition at such time. We may not be able to engage in any of these activities or engage in these activities on desirable terms, which could result in a default on our debt obligations.

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

*If we are unable to obtain or protect intellectual property rights related to our products and product candidates, we may not be able to compete effectively in our market.*

We rely upon a combination of patents, trade secret protection and confidentiality agreements to protect the intellectual property related to our products and product candidates. The strength of patents in the biotechnology and pharmaceutical field involves complex legal and scientific questions and can be uncertain. The patent applications that we own or in-license may fail to result in issued patents with claims that cover the products in the United States or in other foreign countries. If this were to occur, early generic competition could be expected against DUEXIS, VIMOVO, RAYOS/LODOTRA and other product candidates in development. There is no assurance that the potentially relevant prior art relating to our patents and patent applications has been found, which can invalidate a patent or prevent a patent from issuing based on a pending patent application. In particular, because the APIs in DUEXIS, VIMOVO and RAYOS/LODOTRA have been on the market as separate products for many years, it is possible that these products have previously been used off-label in such a manner that such prior usage would affect the validity of our patents or our ability to obtain patents based on our patent applications.

Even if patents do successfully issue, third parties may challenge their validity, enforceability or scope, which may result in such patents being narrowed or invalidated. On March 13, 2013, we received purported Notice Letters that a Paragraph IV Patent Certification had been filed by Alvogen, advising that Alvogen had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. In the Notice Letters, Alvogen noted that as of March 13, 2013, the FDA had not accepted the ANDA for review. Alvogen has agreed that their Notice Letters do not constitute Notice as described in 21 U.S.C. 355(j)(2)(B).

On July 15, 2013, we received a Paragraph IV Patent Certification from Watson, advising that Watson had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Watson has not advised us as to the timing or status of the FDA's review of its filing. On August 26, 2013, we, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against WLF. The lawsuit alleges that WLF has infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124, and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS containing 1 mg, 2 mg, and 5 mg of prednisone prior to the expiration of the patents. The subject patents are listed in the FDA's Orange Book. The commencement of the patent infringement lawsuit stays, or bars, FDA approval of WLF's ANDA for 30 months or until an earlier district court decision that the subject patents are not infringed or invalid.

On September 12, 2013, we received a Paragraph IV Patent Certification from Par Pharmaceutical, Inc. advising that Par Pharmaceutical, Inc. had filed an ANDA with the FDA for a generic version of RAYOS, containing up to 5 mg of prednisone. Par Pharmaceutical, Inc. has not advised us as to the timing or status of the FDA's review of its filing. On October 22, 2013, we, together with Jagotec, filed suit in the United States District Court for the District of New Jersey against Par. The lawsuit alleged that Par had infringed U.S. Patent Nos. 6,488,960, 6,677,326, 8,168,218, 8,309,124 and 8,394,407 by filing an ANDA seeking approval from the FDA to market generic versions of RAYOS prior to the expiration of the patents. The subject patents are listed in the FDA's Orange Book. On November 20, 2013, we were notified by counsel for Par that Par Pharmaceutical, Inc. had elected to withdraw its ANDA with the FDA for a generic version of RAYOS containing 2 mg and 5 mg of prednisone. On December 5, 2013, we entered into a Stipulation of Dismissal with Par Pharmaceutical, Inc. whereby Par Pharmaceutical, Inc. agreed to withdraw its application to market a generic version of RAYOS.

Currently there are patent litigations pending against five generics intending to market VIMOVO before the expiration of patents listed in the Orange Book. These cases are in the District of New Jersey and are grouped in three sets: (i) the DRL cases; (ii) the Mylan cases; and (iii) the Watson cases. We understand that Dr. Reddy's has entered into a settlement with AstraZeneca with respect to patent rights directed to Nexium for the commercialization of VIMOVO, and that according to the settlement agreement, Dr. Reddy's will not be able to commercialize VIMOVO under AstraZeneca's Nexium patent rights until May 28, 2014. As part of our acquisition of the U.S. rights to VIMOVO, we have taken over and are responsible for the patent litigations that include the Pozen patents licensed to us under the Pozen license agreement.

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The DRL cases were filed on April 21, 2011, July 25, 2011, October 28, 2011, and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from Paragraph IV Notice Letters providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. We understand the Dr. Reddy's notice letters were dated March 11, 2011 and November 12, 2012; the Lupin notice letter was dated June 10, 2011; and the Anchen notice letter was dated September 16, 2011. The court has issued a claims construction order. The case does not have pretrial deadlines or a trial date set. We understand Anchen has recertified under Paragraph III and has filed a motion to dismiss on that basis.

The Watson cases were filed on May 10, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from a March 29, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Watson cases.

The Mylan cases were filed on June 28, 2013 and October 23, 2013 and collectively include allegations of infringement of U.S. Patent Nos. 6,926,907 and 8,557,285. We understand the cases arise from a May 16, 2013 Paragraph IV Notice Letter providing notice of the filing of an ANDA with the FDA seeking regulatory approval to market a generic version of VIMOVO before the expiration of the patents-in-suit. The court has not yet set a trial date or schedule for the Mylan cases.

We intend to vigorously defend our intellectual property rights relating to DUEXIS, VIMOVO and RAYOS, but we cannot predict the outcome of the Alvogen or WLF matters related to RAYOS or the DRL cases, the Mylan cases, or the Watson cases related to VIMOVO. Any adverse outcome in these matters or any new generic challenges that may arise could result in one or more generic versions of DUEXIS, VIMOVO and/or RAYOS being launched before the expiration of the listed patents, which could adversely affect our ability to successfully execute our business strategy to increase sales of DUEXIS, VIMOVO and/or RAYOS and would negatively impact our financial condition and results of operations, including causing a significant decrease in our revenues and cash flows.

Furthermore, even if they are unchallenged, our patents and patent applications may not adequately protect our intellectual property or prevent others from designing around our claims. If the patent applications we hold with respect to DUEXIS, VIMOVO or RAYOS/LODOTRA fail to issue or if their breadth or strength of protection is threatened, it could dissuade companies from collaborating with us to develop them and threaten our ability to commercialize our products. We cannot offer any assurances about which, if any, patents will issue or whether any issued patents will be found not invalid and not unenforceable or will go unthreatened by third parties. Further, if we encounter delays in regulatory approvals, the period of time during which we could market DUEXIS, VIMOVO and RAYOS/LODOTRA under patent protection could be reduced. Since patent applications in the United States and most other countries are confidential for a period of time after filing, and some remain so until issued, we cannot be certain that we were the first to file any patent application related to DUEXIS, VIMOVO and RAYOS/LODOTRA or our other product candidates. Furthermore, if third parties have filed such patent applications, an interference proceeding in the United States can be provoked by a third party or instituted by us to determine who was the first to invent any of the subject matter covered by the patent claims of our applications.

In addition to the protection afforded by patents, we rely on trade secret protection and confidentiality agreements to protect proprietary know-how that is not patentable, processes for which patents are difficult to enforce and any other elements of our drug discovery and development processes that involve proprietary know-how, information or technology that is not covered by patents. Although we expect all of our employees to assign their inventions to us, and all of our employees, consultants, advisors and any third parties who have access to our proprietary know-how, information or technology to enter into confidentiality agreements, we cannot provide any assurances that all such agreements have been duly executed or that our trade secrets and other confidential proprietary information will not be disclosed or that competitors will not otherwise gain access to our trade secrets or independently develop substantially equivalent information and techniques.



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Our ability to obtain patents is highly uncertain because, to date, some legal principles remain unresolved, there has not been a consistent policy regarding the breadth or interpretation of claims allowed in patents in the United States and the specific content of patents and patent applications that are necessary to support and interpret patent claims is highly uncertain due to the complex nature of the relevant legal, scientific and factual issues. Changes in either patent laws or interpretations of patent laws in the United States and other countries may diminish the value of our intellectual property or narrow the scope of our patent protection. For example, 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 U.S. patent law. These include provisions that affect the way patent applications will be prosecuted and may also affect patent litigation. The United States Patent and Trademark Office, or U.S. PTO, has developed new and untested regulations and procedures to govern the full implementation 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 in March 2013. The Leahy-Smith Act has also introduced procedures making it easier for third-parties to challenge issued patents, as well as to intervene in the prosecution of patent applications. Finally, the Leahy-Smith Act contains new statutory provisions that still require the U.S. PTO to issue new regulations for their implementation and it may take the courts years to interpret the provisions of the new statute. Accordingly, it is too early to tell what, if any, impact the Leahy-Smith Act will have on the operation of our business and the protection and enforcement of our intellectual property. 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. An inability to obtain, enforce and defend patents covering our proprietary technologies would materially and adversely affect our business prospects and financial condition.

Further, the laws of some foreign countries do not protect proprietary rights to the same extent or in the same manner as the laws of the United States and Canada. As a result, we may encounter significant problems in protecting and defending our intellectual property both in the United States and abroad. For example, if the issuance to us, in a given country, of a patent covering an invention is not followed by the issuance, in other countries, of patents covering the same invention, or if any judicial interpretation of the validity, enforceability, or scope of the claims in, or the written description or enablement in, a patent issued in one country is not similar to the interpretation given to the corresponding patent issued in another country, our ability to protect our intellectual property in those countries may be limited. Changes in either patent laws or in interpretations of patent laws in the United States and other countries may materially diminish the value of our intellectual property or narrow the scope of our patent protection. If we are unable to prevent material disclosure of the non-patented intellectual property related to our technologies to third parties, and there is no guarantee that we will have any such enforceable trade secret protection, we may not be able to establish or maintain a competitive advantage in our market, which could materially adversely affect our business, results of operations and financial condition.

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

Our commercial success depends in part on our avoiding infringement of the patents and proprietary rights of third parties. There is a substantial amount of litigation, both within and outside the United States, involving patent and other intellectual property rights in the biotechnology and pharmaceutical industries, including patent infringement lawsuits, interferences, oppositions and inter party reexamination proceedings before the U.S. PTO. Numerous U.S. and foreign issued patents and pending patent applications, which are owned by third parties, exist in the fields in which we and our collaborators are developing product candidates. As the biotechnology and pharmaceutical industries expand and more patents are issued, the risk increases that our product candidates may be subject to claims of infringement of the patent rights of third parties.

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

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Parties making claims against us may obtain injunctive or other equitable relief, which could effectively block our ability to further develop and commercialize one or more of our product candidates. Defense of these claims, regardless of their merit, would involve substantial litigation expense and would be a substantial diversion of employee resources from our business. In the event of a successful claim of infringement against us, we may have to pay substantial damages, including treble damages and attorneys' fees for willful infringement, obtain one or more licenses from third parties, pay royalties or redesign our infringing products, which may be impossible or require substantial time and monetary expenditure. We cannot predict whether any such license would be available at all or whether it would be available on commercially reasonable terms. Furthermore, even in the absence of litigation, we may need to obtain licenses from third parties to advance our research or allow commercialization of our product candidates, and we have done so from time to time. We may fail to obtain any of these licenses at a reasonable cost or on reasonable terms, if at all. In that event, we would be unable to further develop and commercialize one or more of our product candidates, which could harm our business significantly. We cannot provide any assurances that third-party patents do not exist which might be enforced against our products, resulting in either an injunction prohibiting our sales, or, with respect to our sales, an obligation on our part to pay royalties and/or other forms of compensation to third parties.

*If we fail to comply with our obligations in the agreements under which we license rights to technology from third parties, we could lose license rights that are important to our business.*

We are a party to a number of technology licenses that are important to our business and expect to enter into additional licenses in the future. For example, we hold an exclusive license to SkyePharma AG's proprietary technology and know-how covering the delayed release of corticosteroids relating to RAYOS/LODOTRA. If we fail to comply with our obligations under our agreement with SkyePharma or our other license agreements, or we are subject to a bankruptcy, the licensor may have the right to terminate the license, in which event we would not be able to market products covered by the license, including RAYOS/LODOTRA.

In connection with our November 2013 acquisition of the U.S. rights to VIMOVO, we (i) received the benefit of a covenant not to sue under AstraZeneca's patent portfolio with respect to Nexium (which shall automatically become a license under such patent portfolio if and when AstraZeneca reacquires control of such patent portfolio from Merck Sharp & Dohme Corp. and certain of its affiliates), (ii) were assigned AstraZeneca's amended and restated collaboration and license agreement for the United States with Pozen under which AstraZeneca has in-licensed exclusive rights under certain of Pozen's patents with respect to VIMOVO, and (iii) acquired AstraZeneca's co-ownership rights with Pozen with respect to certain joint patents covering VIMOVO, all for the commercialization of VIMOVO in the United States. If we fail to comply with our obligations under our agreements with AstraZeneca or if we fail to comply with our obligations under our agreements with Pozen as we take over AstraZeneca's agreements with Pozen, our rights to commercialize VIMOVO in the United States may be adversely affected or terminated by AstraZeneca or Pozen.

*We may be involved in lawsuits to protect or enforce our patents or the patents of our licensors, which could be expensive, time consuming and unsuccessful.*

Competitors may infringe our patents or the patents of our licensors. To counter infringement or unauthorized use, we may be required to file infringement claims, which can be expensive and time-consuming. In addition, in an infringement proceeding, a court may decide that a patent of ours or our licensors is not valid or is unenforceable, or may 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 or defense proceedings could put one or more of our patents at risk of being invalidated or interpreted narrowly and could put our patent applications at risk of not issuing.

Interference proceedings provoked by third parties or brought by us may be necessary to determine the priority of inventions with respect to our patents or patent applications or those of our collaborators or licensors. An unfavorable outcome could require us to cease using the related technology or to attempt to license rights to it from the prevailing party. Our business could be harmed if the prevailing party does not offer us a license on commercially reasonable terms. Our defense of litigation or interference proceedings may fail and, even if successful, may result in substantial costs and distract our management and other employees. We may not be able to prevent, alone or with our licensors, misappropriation of our intellectual property rights, particularly in countries where the laws may not protect those rights as fully as in the United States.

Furthermore, because of the substantial amount of discovery required in connection with intellectual property litigation, there is a risk that some of our confidential information could be compromised by disclosure during this type of litigation. There could also be public announcements of the results of hearings, motions or other interim proceedings or developments. If securities analysts or investors perceive these results to be negative, it could have a material adverse effect on the price of our common stock.

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*Obtaining and maintaining our patent protection depends on compliance with various procedural, document submission, fee payment and other requirements imposed by governmental patent agencies, and our patent protection could be reduced or eliminated for non-compliance with these requirements.*

Periodic maintenance fees on any issued patent are due to be paid to the U.S. PTO and foreign patent agencies in several stages over the lifetime of the patent. The U.S. PTO and various foreign governmental patent agencies require compliance with a number of procedural, documentary, fee payment and other similar provisions during the patent application process. While an inadvertent lapse can in many cases be cured by payment of a late fee or by other means in accordance with the applicable rules, there are situations in which noncompliance can result in abandonment or lapse of the patent or patent application, resulting in partial or complete loss of patent rights in the relevant jurisdiction. Non-compliance events that could result in abandonment or lapse of a patent or patent application include, but are not limited to, failure to respond to official actions within prescribed time limits, non-payment of fees and failure to properly legalize and submit formal documents. If we or our licensors that control the prosecution and maintenance of our licensed patents fail to maintain the patents and patent applications covering our product candidates, our competitors might be able to enter the market, which would have a material adverse effect on our business.

*We may be subject to claims that our employees, consultants or independent contractors have wrongfully used or disclosed confidential information of third parties.*

We employ individuals who were previously employed at other biotechnology or pharmaceutical companies. We may be subject to claims that we or our employees, consultants or independent contractors have inadvertently or otherwise used or disclosed confidential information of our employees' former employers or other third parties. We may also be subject to claims that former employers or other third parties have an ownership interest in our patents. Litigation may be necessary to defend against these claims. There is no guarantee of success in defending these claims, and if we are successful, litigation could result in substantial cost and be a distraction to our management and other employees.

### **Risks Related to Ownership of our Common Stock**

*We do not know whether an active, liquid and orderly trading market will develop for our common stock or what the market price of our common stock will be and as a result it may be difficult for you to sell your shares of our common stock.*

Prior to our initial public offering there was no market for shares of our common stock. Although our common stock is listed on The NASDAQ Global Market, an active trading market for our shares may never fully develop or be sustained even if it does. Further, an inactive market may impair our ability to raise capital by selling shares of our common stock and may impair our ability to enter into strategic partnerships or acquire companies or products by using our shares of common stock as consideration.

*The market price of our common stock historically has been volatile and is likely to be highly volatile, and you could lose all or part of your investment.*

The trading price of our common stock following the completion of our initial public offering has been highly volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control, including limited trading volume. In addition to the factors discussed in this "Risk Factors" section and elsewhere in this report, these factors include:

- our failure to successfully execute our commercialization strategy with respect to our approved products, particularly our commercialization of DUEXIS, VIMOVO and RAYOS in the United States;
- disputes or other developments relating to intellectual property and other proprietary rights, including patents, litigation matters and our ability to obtain patent protection for our products and product candidates;
- unanticipated serious safety concerns related to the use of our products;
- adverse regulatory decisions;
- changes in laws or regulations applicable to our products or product candidates, including but not limited to clinical trial requirements for approvals;
- inability to obtain adequate commercial supply for any approved product or inability to do so at acceptable prices;
- developments concerning our commercial partners, including but not limited to those with our sources of manufacturing supply;
- our decision to initiate a clinical trial, not to initiate a clinical trial or to terminate an existing clinical trial;
- adverse results or delays in clinical trials;
- our failure to successfully develop, acquire, and/or in-license additional product candidates;
- introduction of new products or services offered by us or our competitors;

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- our inability to effectively manage our growth;
- overall performance of the equity markets and general political and economic conditions;
- failure to meet or exceed revenue and financial projections we may provide to the public;
- actual or anticipated variations in quarterly operating results;
- failure to meet or exceed the estimates and projections of the investment community;
- publication of research reports about us or our industry or positive or negative recommendations or withdrawal of research coverage by securities analysts;
- our inability to successfully enter new markets;
- the termination of a collaboration or the inability to establish additional collaborations;
- announcements of significant acquisitions, strategic partnerships, joint ventures or capital commitments by us or our competitors;
- our inability to maintain an adequate rate of growth;
- ineffectiveness of our internal controls or our inability to otherwise comply with financial reporting requirements;
- adverse U.S. and foreign tax exposure;
- additions or departures of key management, commercial or regulatory personnel;
- issuances of debt or equity securities;
- significant lawsuits, including patent or stockholder litigation;
- changes in the market valuations of similar companies;
- sales of our common stock by us or our stockholders in the future;
- trading volume of our common stock;
- effects of natural or man-made catastrophic events or other business interruptions; and
- other events or factors, many of which are beyond our control.

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

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

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

*Our officers, directors and funds affiliated with our directors own a significant percentage of our stock and will be able to influence matters subject to stockholder approval.\**

Our officers, directors and funds affiliated with our directors held in the aggregate approximately 17% of our outstanding voting stock as of March 31, 2014. Therefore, these stockholders have the ability to influence us through this ownership position, including through matters requiring stockholder approval. For example, these stockholders may be able to influence the elections of directors, amendments of our organizational documents, or approval of any merger, sale of assets, or other major corporate transaction, such as the proposed merger with Vidara. This may discourage unsolicited acquisition proposals or offers for our common stock that our stockholders may feel are in their best interest.

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*We have incurred and will continue to incur significant increased costs as a result of operating as a public company and our management will be required to devote substantial time to new compliance initiatives.*

As a public company, we have incurred and will continue to incur significant legal, accounting and other expenses that we did not incur as a private company. In particular, the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, as well as rules subsequently implemented by the SEC and the NASDAQ Stock Market, Inc., or NASDAQ, impose significant requirements on public companies, including requiring establishment and maintenance of effective disclosure and financial controls and changes in corporate governance practices. These rules and regulations have substantially increased our legal and financial compliance costs and have made some activities more time-consuming and costly. If these requirements divert the attention of our management and personnel from other business concerns, they could have a material adverse effect on our business, financial condition and results of operations. The increased costs will continue to decrease our net income or increase our net loss, and may require us to reduce costs in other areas of our business or increase the prices of our products or services. For example, these rules and regulations make it more difficult and more expensive for us to obtain and maintain director and officer liability insurance. We cannot predict or estimate the amount or timing of additional costs we may incur to respond to these requirements. The impact of these requirements could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors, our board committees or as executive officers. If we fail to comply with the continued listing requirements of NASDAQ, our common stock could be delisted from The NASDAQ Global Market, which would adversely affect the liquidity of our common stock and our ability to obtain future financing.

The Sarbanes-Oxley Act requires, among other things, that we maintain effective internal controls for financial reporting and disclosure controls and procedures. In particular, we are required to perform annual system and process evaluation and testing of our internal controls over financial reporting to allow management to report on the effectiveness of our internal controls over financial reporting, as required by Section 404 of the Sarbanes-Oxley Act, or Section 404. Our independent registered public accounting firm is also required to deliver a report on the effectiveness of our internal control over financial reporting. Our testing, or the testing by our independent registered public accounting firm, may reveal deficiencies in our internal controls over financial reporting that are deemed to be material weaknesses. Our compliance with Section 404 requires that we incur substantial accounting expense and expend significant management efforts, particularly because of our holding company structure and international operations. We currently do not have an internal audit group, and we may need to hire additional accounting and financial staff with appropriate public company experience and technical accounting knowledge, as well as retain and work with consultants with such knowledge. Moreover, if we are not able to comply with the requirements of Section 404 or if we or our independent registered public accounting firm identify deficiencies in our internal controls over financial reporting that are deemed to be material weaknesses, the market price of our common stock could decline and we could be subject to sanctions or investigations by NASDAQ, the SEC or other regulatory authorities, which would require additional financial and management resources.

New laws and regulations as well as changes to existing laws and regulations affecting public companies, including the provisions of the Sarbanes-Oxley Act and rules adopted by the SEC and by NASDAQ, would likely result in increased costs to us as we respond to their requirements.

*Sales of a substantial number of shares of our common stock in the public market could cause our stock price to decline.*

If our existing stockholders sell, or indicate an intention to sell, substantial amounts of our common stock in the public market, the trading price of our common stock could decline. In addition, shares of common stock that are either subject to outstanding options or reserved for future issuance under our employee benefit plans are or may become eligible for sale in the public market to the extent permitted by the provisions of various vesting schedules and Rule 144 and Rule 701 under the Securities Act. If these additional shares of common stock are sold, or if it is perceived that they will be sold, in the public market, the trading price of our common stock could decline.

Certain holders of shares of our common stock are entitled to rights with respect to the registration of their shares under the Securities Act. Registration of these shares under the Securities Act would result in the shares becoming freely tradable without restriction under the Securities Act, except for shares purchased by affiliates. Any sales of securities by these stockholders could have a material adverse effect on the trading price of our common stock.

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

Additional capital may be needed in the future to continue our planned operations. To the extent we raise additional capital by issuing equity securities, our stockholders may experience substantial dilution. We may sell common stock, convertible securities or other equity securities in one or more transactions at prices and in a manner we determine from time to time. If we sell common stock, convertible securities or other equity securities in subsequent transactions, our existing stockholders may be materially diluted. New investors in such subsequent transactions could gain rights, preferences and privileges senior to those of holders of our common stock.

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In August 2012, we entered into a sales agreement with Cowen pursuant to which we may sell common stock in ATM offerings under our registration statement on Form S-3, which became effective on August 9, 2012. As of March 31, 2014, Cowen had sold a cumulative total of 2,448,575 shares of our common stock with gross proceeds to us of \$6.2 million.

Pursuant to our 2011 equity incentive plan, or 2011 EIP, our board of directors is authorized to grant stock options to our employees, directors and consultants. The number of shares available for future grant under our 2011 EIP automatically increases on January 1 of each year by an amount equal to the lesser of 5% of our capital stock outstanding as of December 31 of the preceding calendar year or 1,474,304 shares, subject to the ability of our board of directors to take action to reduce the size of such increase in any given year. In addition, our board of directors may grant or provide for the grant of rights to purchase shares of our common stock pursuant to the terms of the 2011 employee stock purchase plan, or 2011 ESPP. The number of shares of our common stock reserved for issuance automatically increases on January 1 of each year by an amount equal to the lesser of 4% of our capital stock outstanding as of December 31 of the preceding calendar year or 1,053,074, subject to the ability of our board of directors to take action to reduce the size of such increase in any given year. On December 5, 2013, pursuant to the terms of our 2011 EIP and 2011 ESPP, our board of directors approved increases in the number of shares available for issuance under the 2011 EIP and the 2011 ESPP of 1,474,304 shares and 1,053,074 shares, respectively, effective January 1, 2014.

In addition, (i) on November 7, 2013, November 16, 2013 and March 3, 2014, our board of directors approved amendments to the 2011 EIP to reserve an additional 200,000 shares, 800,000 shares and 730,000 shares, respectively, of our common stock to be used exclusively for grants of awards to individuals who were not previously employees or directors of ours (or following a bona fide period of non-employment with us), as an inducement material to the individual's entry into employment with us within the meaning of Rule 5635(c)(4) of the NASDAQ Listing Rules and (ii) on January 10, 2014, our board of directors approved an amendment to the 2011 EIP to increase the number of shares available for issuance under the 2011 EIP by 703,400 shares, or the January 2014 amendment, with such increase to the number of shares available for issuance under the 2011 EIP subject to stockholder approval of the January 2014 amendment.

In November 2013, we issued \$150.0 million aggregate principal amount of the Convertible Senior Notes. The Convertible Senior Notes are convertible at the option of the holders at any time prior to the close of business on the business day immediately preceding August 15, 2018 only under certain conditions. On or after August 15, 2018 until the close of business on the second scheduled trading day immediately preceding the maturity date for the Convertible Senior Notes, holders will be able to convert their Convertible Senior Notes at their option at the conversion rate then in effect at any time, regardless of these conditions. Subject to certain limitations, we may settle conversions of the Convertible Senior Notes by paying or delivering, as the case may be, cash, shares of our common stock or a combination of cash and shares of our common stock, at our election.

*Some provisions of our charter documents and Delaware law may have anti-takeover effects that could discourage an acquisition of us by others, even if an acquisition would be beneficial to our stockholders and may prevent attempts by our stockholders to replace or remove our current management.*

Provisions in our amended and restated certificate of incorporation and amended and restated bylaws, as well as provisions of Delaware law, could make it more difficult for a third party to acquire us or increase the cost of acquiring us, even if doing so would benefit our stockholders or remove our current management. These provisions include:

- authorizing the issuance of "blank check" preferred stock, the terms of which may be established and shares of which may be issued without stockholder approval;
- limiting the removal of directors by the stockholders;
- creating a staggered board of directors;
- prohibiting stockholder action by written consent, thereby requiring all stockholder actions to be taken at a meeting of stockholders;
- eliminating the ability of stockholders to call a special meeting of stockholders; and
- establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted upon at stockholder meetings.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management. We are also subject to certain anti-takeover provisions under Delaware law, which may discourage, delay or prevent someone from acquiring us or merging with us whether or not it is desired by or beneficial to our stockholders. Under Delaware law, a corporation may not, in general, engage in a business combination with any holder of 15% or more of its capital stock unless the holder has held the stock for three years or, among other things, the board of directors has approved the transaction. Any provision of our certificate of incorporation or bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could depress the market price of our common stock.

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*If securities or industry analysts do not publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.*

The trading market for our common stock will depend in part on the research and reports that securities or industry analysts publish about us or our business. If one or more of the analysts who cover us downgrade our stock or publish inaccurate or unfavorable research about our business, our stock price would likely decline. If one or more of these analysts cease coverage of our company or fail to publish reports on us regularly, demand for our stock could decrease, which might cause our stock price and trading volume to decline.

*We may become involved in securities class action litigation that could divert management's attention and harm our business and could subject us to significant liabilities.*

The stock markets have from time to time experienced significant price and volume fluctuations that have affected the market prices for the common stock of pharmaceutical companies. These broad market fluctuations may cause the market price of our common stock to decline. In the past, securities class action litigation has often been brought against a company following a decline in the market price of its securities. This risk is especially relevant for us because biotechnology and biopharmaceutical companies have experienced significant stock price volatility in recent years. We may become involved in this type of litigation in the future. Even if we are successful in defending against any such claims, litigation could result in substantial costs and may be a distraction to management, and may result in unfavorable results that could adversely impact our financial condition and prospects.

### **Risks Related to the Proposed Merger with Vidara**

*Failure to consummate the proposed merger with Vidara could negatively impact our stock price and our future business and financial results.\**

If the proposed merger between us and Vidara is not consummated, our ongoing business may be adversely affected and, without realizing any of the benefits of having consummated the merger, we will be subject to a number of risks, including the following:

- we may be required to reimburse Vidara for certain expenses incurred by Vidara in connection with certain governmental filings or certain lawsuits;
- if the merger agreement is terminated under specified circumstances, we may be required to pay to Vidara a termination fee equal to \$23 million;
- if the merger is not consummated because our stockholders do not approve the merger, we will be obligated to pay Vidara \$13.5 million for expenses;
- if the merger is not consummated because we are not able to complete the merger after the conditions to closing are satisfied and Vidara is ready, willing and able to close the merger, then we will be obligated to pay Vidara \$44 million as a termination fee;
- we will be required to pay significant costs relating to the proposed reorganization and merger, including legal, accounting, filing and possible other fees and mailing, financial printing and other expenses in connection with the transaction whether or not the merger is consummated;
- the current price of our common stock may reflect a market assumption that the merger will occur, meaning that a failure to complete the merger could result in a decline in the price of our common stock; and
- matters relating to the reorganization and merger have required and will continue to require substantial commitments of time and resources by our management, which could otherwise have been devoted to other opportunities that may have been beneficial to us.

We also could be subject to litigation related to any failure to consummate the merger or to perform our obligations under the merger agreement, or related to any enforcement proceeding commenced against us. If the merger is not consummated, these risks may materialize and may adversely affect our business, financial results and stock price.

*Obtaining required approvals necessary to satisfy the conditions to the completion of the merger may delay or prevent completion of the merger, result in additional expenditures of money and resources and/or reduce the anticipated benefits of the merger.\**

The merger is subject to customary closing conditions. These closing conditions include, among others, the receipt of the requisite approval of our stockholders, the effectiveness of the registration statement filed with the SEC regarding the proposed merger and the consummation of the reorganization of Vidara.

We cannot assure you that the required stockholder approval will be obtained or that the required closing conditions will be satisfied, and, if all required consents and approvals are obtained and the closing conditions are satisfied, no assurance can be given as to the terms, conditions and timing of the approvals. This could result in a failure to consummate the merger or have a material adverse effect on the combined company's business and results of operations.

*Our business relationships, including customer relationships, may be subject to disruption due to uncertainty associated with the merger.\**

Parties with which we currently do business or may do business in the future, including customers and suppliers, may experience uncertainty associated with the merger, including with respect to current or future business relationships with us or the surviving entity in the merger. As a result, our business relationships may be subject to disruptions if customers, suppliers and others attempt to negotiate changes in existing business relationships or consider entering into business relationships with parties other than us. These disruptions could have an adverse effect on the business, financial condition, results of operations or prospects of us and the surviving entity following the closing of the merger. The adverse effect of such disruptions could be exacerbated by a delay in the consummation of the merger or termination of the merger agreement.



**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

We completed the following issuances of unregistered securities during the three months ended March 31, 2014:

- In January 2014, we issued 20,711 shares of common stock to Parallax Biomedical Fund L.P. upon the cash exercise of a warrant and we received proceeds of \$89,222.99 representing the aggregate exercise price of such warrant.
- In February 2014, we issued 20,711 shares of common stock to Cowen Overseas Investment L.P. upon the cash exercise of a warrant and we received proceeds of \$89,222.99 representing the aggregate exercise price of such warrant.
- In March 2014, we issued 34,774 shares of common stock to Silicon Valley Bank upon the cashless exercise of warrants to purchase an aggregate of 41,631 shares of common stock.

The offers, sales and issuances of the securities described above were deemed to be exempt from registration under the Securities Act of 1933, as amended, in reliance on Rule 506 of Regulation D in that each issuance of securities was to an accredited investor under Rule 501 of Regulation D and did not involve a public offering. The recipients of securities in each of these transactions acquired the securities for investment only and not with a view to or for sale in connection with any distribution thereof and appropriate legends were affixed to the securities issued in these transactions.

**Item 6. Exhibits**

The exhibits listed on the Index to Exhibits following the signature page are filed as part of this Quarterly Report on Form 10-Q.

**SIGNATURES**

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

**HORIZON PHARMA, INC.**

Date: May 9, 2014

By: /s/ Timothy P. Walbert

Timothy P. Walbert  
*Chairman, President and Chief Executive Officer*  
*(Principal Executive Officer)*

Date: May 9, 2014

By: /s/ Robert J. De Vaere

Robert J. De Vaere  
*Executive Vice President and Chief Financial Officer*  
*(Principal Financial and Accounting Officer)*

**INDEX TO EXHIBITS**

<u>Exhibit Number</u>	<u>Description of Document</u>
2.1(9)	Transaction Agreement and Plan of Merger, dated March 18, 2014, by and among Horizon Pharma, Inc., Vidara Therapeutics Holdings LLC, Vidara Therapeutics International Ltd., Hamilton Holdings (USA), Inc. and Hamilton Merger Sub, Inc.*
3.1(1)	Amended and Restated Certificate of Incorporation.
3.2(1)	Amended and Restated Bylaws.
4.1(2)	Form of Common Stock Certificate.
4.2(2)	Form of Warrant issued by Horizon Pharma, Inc. to bridge financing investors.
4.3(2)	Warrant issued by Horizon Pharma, Inc. on December 18, 2007 to Comerica Bank.
4.4(2)	Warrant issued by Horizon Pharma, Inc. on December 18, 2007 to Hercules Technology Growth Capital, Inc.
4.5(2)	Warrant issued by Horizon Pharma, Inc. on November 21, 2008 to Comerica Bank.
4.6(2)	Warrant issued by Horizon Pharma, Inc. on November 21, 2008 to Hercules Technology Growth Capital, Inc.
4.7(2)	Warrant issued by Horizon Pharma, Inc. on April 1, 2010 to Silicon Valley Bank.
4.8(2)	Investors' Rights Agreement, dated April 1, 2010, by and among Horizon Pharma, Inc. and certain of its stockholders.
4.9(2)	Form of Warrant issued by Horizon Pharma, Inc. on June 2, 2011 to Oxford Finance LLC.
4.10(2)	Warrant issued by Horizon Pharma, Inc. on June 2, 2011 to Silicon Valley Bank.
4.11(2)	Conversion and Amendment Agreement, dated June 16, 2011, by and among Horizon Pharma, Inc. and certain of its stockholders.
4.12(3)	Form of Warrant issued by Horizon Pharma, Inc. pursuant to the Securities Purchase Agreement, dated February 28, 2012, by and among Horizon Pharma, Inc. and the Purchasers and Warrant Holders listed therein.
4.13(3)	Amendment to Investors' Rights Agreement, dated February 22, 2012.
4.14(4)	Form of Warrant issued in Public Offering of Units.
4.15(5)	Indenture, dated as of November 22, 2013, by and between Horizon Pharma, Inc. and U.S. Bank National Association.
4.16(5)	Form of 5.00% Convertible Senior Note due 2018.
10.1+(6)	First Amendment to Amended and Restated Executive Employment Agreement, dated January 16, 2014, by and among Horizon Pharma, Inc., Horizon Pharma USA, Inc. and Timothy P. Walbert.
10.2+(6)	First Amendment to Amended and Restated Executive Employment Agreement, dated January 16, 2014, by and among Horizon Pharma, Inc., Horizon Pharma USA, Inc. and Robert J. De Vaere.
10.3+(6)	First Amendment to Amended and Restated Executive Employment Agreement, dated January 16, 2014, by and among Horizon Pharma, Inc., Horizon Pharma USA, Inc. and Jeffrey W. Sherman, M.D., FACP.
10.4+(6)	First Amendment to Executive Employment Agreement, dated January 16, 2014, by and among Horizon Pharma, Inc., Horizon Pharma USA, Inc. and Todd N. Smith.
10.5+(7)	Executive Employment Agreement, effective March 5, 2014, by and among Horizon Pharma, Inc., Horizon Pharma USA, Inc. and Robert F. Carey.

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<u>Exhibit Number</u>	<u>Description of Document</u>
10.6+(8)	2011 Equity Incentive Plan, as amended, and Form of Option Agreement and Form of Stock Option Grant Notice thereunder.
10.7(10)	Commitment Letter, dated March 18, 2014, by and among Horizon Pharma, Inc., Deerfield Management Company, L.P. and certain funds managed by Deerfield Management Company, L.P.
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act.
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act.
32.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(b) or 15d-14(b) of the Exchange Act and 18 U.S.C. Section 1350.
32.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(b) or 15d-14(b) of the Exchange Act and 18 U.S.C. Section 1350.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
*	Schedules have been omitted pursuant to Item 601(b)(2) of Regulation S-K. Horizon Pharma, Inc. undertakes to furnish supplemental copies of any of the omitted schedules upon request by the Securities and Exchange Commission.
+	Indicates management contract or compensatory plan.
(1)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on August 2, 2011.
(2)	Incorporated by reference to Horizon Pharma, Inc.'s Registration Statement on Form S-1 (No. 333-168504), as amended.
(3)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on March 1, 2012.
(4)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on September 20, 2012.
(5)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on November 25, 2013.
(6)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on January 16, 2014.
(7)	Incorporated by reference to Horizon Pharma, Inc.'s Annual Report on Form 10-K, filed on March 13, 2014.
(8)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on March 4, 2014.
(9)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on March 20, 2014.
(10)	Incorporated by reference to Horizon Pharma, Inc.'s Current Report on Form 8-K, filed on March 19, 2014.

*Certification*

I, Timothy P. Walbert, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Horizon Pharma, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 9, 2014

/s/ Timothy P. Walbert

Timothy P. Walbert  
President, Chief Executive Officer and  
Chairman of the Board  
(Principal Executive Officer)

*Certification*

I, Robert J. De Vaere, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Horizon Pharma, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal quarter (the registrant’s fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: May 9, 2014

/s/ Robert J. De Vaere

Robert J. De Vaere  
Executive Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

**CERTIFICATION**

Pursuant to the requirement set forth in Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and 18 U.S.C. Section 1350, I, Timothy P. Walbert, President, Chief Executive Officer and Chairman of the Board of Horizon Pharma, Inc. (the "Company"), certify to the best of my knowledge that:

1. the Company's Quarterly Report on Form 10-Q for the period ended March 31, 2014 (the "Report"), to which this Certification is attached as Exhibit 32.1, fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 9, 2014

/s/ Timothy P. Walbert

Timothy P. Walbert  
President, Chief Executive Officer and Chairman of the Board  
(Principal Executive Officer)

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

**CERTIFICATION**

Pursuant to the requirement set forth in Rule 13a-14(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and 18 U.S.C. Section 1350, I, Robert J. De Vaere, Executive Vice President and Chief Financial Officer of Horizon Pharma, Inc. (the "Company"), certify to the best of my knowledge that:

1. the Company's Quarterly Report on Form 10-Q for the period ended March 31, 2014 (the "Report"), to which this Certification is attached as Exhibit 32.2, fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: May 9, 2014

/s/ Robert J. De Vaere

Robert J. De Vaere  
Executive Vice President and Chief Financial Officer  
(Principal Financial and Accounting Officer)

A signed original of this written statement required by Section 906 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Exchange Act (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.



