

SPECTRUM PHARMACEUTICALS INC

Form 10-Q

August 08, 2014

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**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 10-Q**

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

**For the quarterly period ended June 30, 2014**

.. **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: 001-35006**

**SPECTRUM PHARMACEUTICALS, INC.**

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

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

**93-0979187**  
**(I.R.S. Employer**  
**Identification No.)**

**11500 South Eastern Avenue, Suite 240**

**Henderson, Nevada**  
**(Address of principal executive offices)**  
**(702) 835-6300**

**89052**  
**(Zip Code)**

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

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

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

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

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

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

As of July 31, 2014, 65,731,956 shares of the registrant's common stock were outstanding.

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**FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2014**  
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Item 2 through 5 of Part II have been omitted because they are not applicable with respect to the current reporting period.

**Table of Contents****PART I: FINANCIAL INFORMATION****SPECTRUM PHARMACEUTICALS, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share and par value amounts)****(Unaudited)**

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 132,405	\$ 156,306
Marketable securities	3,306	3,471
Accounts receivable, net of allowance for doubtful accounts of \$177 and \$206, respectively	56,742	49,483
Other receivables	11,802	7,539
Inventories	10,881	13,519
Prepaid expenses and other current assets	3,410	3,213
Deferred tax assets	1,587	1,659
Total current assets	220,133	235,190
Property and equipment, net of accumulated depreciation	1,407	1,535
Intangible assets, net of accumulated amortization	219,735	231,352
Goodwill	18,476	18,501
Other assets	15,197	12,577
Total assets	\$ 474,948	\$ 499,155
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable and other accrued liabilities	\$ 69,178	\$ 79,837
Accrued payroll and benefits	5,149	6,872
Deferred revenue	33	156
Drug development liability	3,119	3,119
Total current liabilities	77,479	89,984
Drug development liability, less current portion	14,069	14,623
Acquisition-related contingent obligations	10,058	8,329
Deferred tax liability	8,167	7,168
Other long-term liabilities	5,709	5,965
Convertible senior notes	93,812	91,480
Total liabilities	209,294	217,549

<b>Commitments and contingencies</b>		
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000,000 shares authorized:		
Series B junior participating preferred stock, \$0.001 par value; 1,500,000 shares authorized; no shares issued and outstanding		
Series E Convertible Voting Preferred Stock, \$0.001 par value and \$10,000 stated value; 2,000 shares authorized; 20 shares issued and outstanding at June 30, 2014 and December 31, 2013, respectively (convertible into 40,000 shares of common stock, with aggregate liquidation value of \$240)	123	123
Common stock, \$0.001 par value; 175,000,000 shares authorized; 65,730,897 and 64,104,173 shares issued and outstanding at June 30, 2014 and December 31, 2013, respectively	66	64
Additional paid-in capital	532,554	518,144
Accumulated other comprehensive income	1,734	894
Accumulated deficit	(268,823)	(237,619)
Total stockholders' equity	265,654	281,606
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	<b>\$ 474,948</b>	<b>\$ 499,155</b>

See accompanying notes to these unaudited condensed consolidated financial statements.

**Table of Contents****SPECTRUM PHARMACEUTICALS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(In thousands, except share and per share amounts)****(Unaudited)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
<b>Revenues:</b>				
Product sales, net	\$ 46,855	\$ 32,213	\$ 86,951	\$ 61,559
License fees and service revenue		1,019	28	10,340
<b>Total revenues</b>	<b>46,855</b>	<b>33,232</b>	<b>86,979</b>	<b>71,899</b>
<b>Operating costs and expenses:</b>				
Cost of product sales (excludes amortization and impairment of intangible assets)	6,156	7,268	12,434	14,050
Selling, general and administrative	25,399	22,584	48,802	44,598
Research and development	11,335	10,460	40,832	22,343
Amortization and impairment of intangible assets	5,361	5,449	10,721	9,894
<b>Total operating costs and expenses</b>	<b>48,251</b>	<b>45,761</b>	<b>112,789</b>	<b>90,885</b>
<b>Loss from operations</b>	<b>(1,396)</b>	<b>(12,529)</b>	<b>(25,810)</b>	<b>(18,986)</b>
<b>Other expenses:</b>				
Interest expense, net	(1,976)	(397)	(4,043)	(818)
Change in fair value of contingent consideration related to acquisitions	(1,005)		(1,729)	
Other income (expense), net	(487)	234	(845)	(663)
<b>Total other expenses</b>	<b>(3,468)</b>	<b>(163)</b>	<b>(6,617)</b>	<b>(1,481)</b>
<b>Loss before income taxes</b>	<b>(4,864)</b>	<b>(12,692)</b>	<b>(32,427)</b>	<b>(20,467)</b>
Benefit for income taxes	1,301	2,971	1,223	5,310
<b>Net loss</b>	<b>\$ (3,563)</b>	<b>\$ (9,721)</b>	<b>\$ (31,204)</b>	<b>\$ (15,157)</b>
<b>Net loss per share:</b>				
Basic and diluted	\$ (0.06)	\$ (0.16)	\$ (0.49)	\$ (0.26)
<b>Weighted average shares outstanding:</b>				
Basic and diluted	64,609,197	58,977,295	64,119,441	58,995,735

See accompanying notes to these unaudited condensed consolidated financial statements.

Table of Contents**SPECTRUM PHARMACEUTICALS, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS****(In thousands)****(Unaudited)**

	<b>Three Months Ended June 30,</b>		<b>Six Months Ended June 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Net loss	\$ (3,563)	\$ (9,721)	\$ (31,204)	\$ (15,157)
Other comprehensive income, net of income tax:				
Unrealized gain on available-for-sale securities	741	99	1,055	967
Income tax on unrealized gain on available-for-sale securities	(279)	57	(398)	171
Foreign currency translation adjustments	95	(37)	183	(361)
Other comprehensive income	557	119	840	777
Total comprehensive loss	\$ (3,006)	\$ (9,602)	\$ (30,364)	\$ (14,380)

See accompanying notes to these unaudited condensed consolidated financial statements.



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	<b>Six months ended June 30,</b>	
	<b>2014</b>	<b>2013</b>
<b>Cash Flows From Operating Activities:</b>		
Net loss	\$ (31,204)	\$ (15,157)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization of deferred service revenue		(10,300)
Depreciation and amortization	12,179	10,772
Stock-based compensation	5,525	5,671
Accretion of debt discount to interest expense on 2018 Convertible Notes (Note 11)	2,332	
Amortization of deferred financing costs to interest expense on 2018 Convertible Notes (Note 11)	308	
Bad debt (recovery) expense	(28)	44
Impairment of intangible assets		1,023
Unrealized foreign currency loss	606	654
Research and development expense for the value of stock issued to TopoTarget in connection with milestone achievement (Note 13)	7,790	
Change in fair value of contingent consideration related to acquisitions (Note 9)	1,729	
Change in fair value of drug development liability (Note 12)		(2,869)
Changes in operating assets and liabilities:		
Accounts receivable	(7,231)	39,746
Other receivables	(4,263)	
Inventories	2,638	(834)
Prepaid expenses and other current assets	(197)	(5,691)
Deferred tax assets	72	(6,039)
Other assets	(1,873)	
Accounts payable and other accrued obligations	(10,659)	(11,495)
Accrued payroll and benefits	(1,723)	(472)
Drug development liability (Note 12)	(554)	(2,352)
Deferred revenue	(123)	
Deferred tax liability	602	
Other long-term liabilities	(256)	743
Net cash (used in) provided by operating activities	(24,330)	3,444
<b>Cash Flows From Investing Activities:</b>		
Acquisition of C-E MELPHALAN license (Note 9)		(3,000)
Redemption of certificate of deposit	165	

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Purchases of property and equipment	(605)	(127)
Net cash used in investing activities	(440)	(3,127)
<b>Cash Flows From Financing Activities:</b>		
Proceeds from exercise of stock options	1,339	1,137
Proceeds from sale of stock under employee stock purchase plan	348	197
Payments to acquire treasury stock		(1,652)
Purchase and retirement of restricted stock to satisfy employee tax liability at vesting	(590)	(410)
Proceeds from Mundipharma related to FOLOTYN collaboration (Note 12)		7,000
Proceeds from revolving line of credit		100,000
Repayment of revolving line of credit		(125,000)
Net cash provided by (used in) financing activities	1,097	(18,728)
Effect of exchange rates on cash	(228)	(184)
Net (decrease) increase in cash and cash equivalents	(23,901)	(18,595)
Cash and cash equivalents beginning of period	156,306	139,698
Cash and cash equivalents end of period	\$ 132,405	\$ 121,103
<b>Supplemental disclosure of cash flow information:</b>		
C-E MELPHALAN license included in intangible assets and other long-term obligations	\$	\$ 4,700
Retirement of treasury shares	\$	\$ 1,652
Cash paid for income taxes	\$ 329	\$ 197
Cash paid for interest	\$ 1,588	\$ 421

See accompanying notes to these unaudited condensed consolidated financial statements.

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**SPECTRUM PHARMACEUTICALS, INC.**

**Notes to Condensed Consolidated Financial Statements**

**(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)**

**(Unaudited)**

**1. DESCRIPTION OF BUSINESS, BASIS OF PRESENTATION, AND OPERATING SEGMENT**

***(a) Description of Business***

Spectrum Pharmaceuticals, Inc. and its wholly-owned subsidiaries ( Spectrum , the Company , we , our , or us ), is a biotechnology company with fully integrated commercial and drug development operations, with a primary focus in oncology and hematology. Our strategy is comprised of acquiring, developing, and marketing a diverse pipeline of late-stage clinical and commercial products.

We currently market five drugs for the following indications:

FUSILEV® injection for patients in the U.S. with advanced metastatic colorectal cancer and to counteract certain effects of methotrexate therapy;

ZEVALIN® injection for patients in the U.S. and various international markets with follicular non-Hodgkin s lymphoma;

FOLOTYN® injection for patients in the U.S. with relapsed or refractory peripheral T-cell lymphoma ( PTCL );

MARQIBO® injection for patients in the U.S. with Philadelphia chromosome negative acute lymphoblastic leukemia; and

BELEODAQ injection for patients in the U.S. with relapsed or refractory PTCL. We did not launch this product until July 2014, and accordingly, no corresponding revenue is reported for any period presented in the accompanying Condensed Consolidated Financial Statements.

We also have ongoing indication expansion studies with several of our marketed products, and a diversified pipeline of product candidates in advanced-stage Phase 2 and Phase 3 studies. Our integrated in-house scientific team, includes formulation development and medical research, as well as expertise in regulatory and clinical affairs, biostatistics, and data management. In the U.S., we have full commercial operations for the sales and marketing of our drug products, and leverage the expertise of our worldwide partners to assist us with international sales and product development.

***(b) Basis of Presentation***

*Interim Financial Statements*

The interim financial data as of June 30, 2014 and 2013 is unaudited and is not necessarily indicative of the results for a full year. In the opinion of our management, the interim data includes normal and recurring adjustments necessary for a fair presentation of our financial results for the three and six months ended June 30, 2014 and 2013. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles in the United States of America ( GAAP ) have been condensed or omitted pursuant to U.S. Securities and Exchange Commission ( SEC ) rules and regulations relating to interim financial statements. The accompanying Condensed Consolidated Financial Statements should be read in conjunction with our audited Consolidated Financial Statements and Notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, filed with the SEC on March 12, 2014.

*Principles of Consolidation*

The accompanying Condensed Consolidated Financial Statements include the financial position, results of operations, and cash flows of Spectrum and its subsidiaries, all of which are wholly-owned (except for SPC, as discussed below). All inter-company accounts and transactions among the consolidated entities have been eliminated in consolidation.

*Variable Interest Entity*

We own fifty-percent of Spectrum Pharma Canada ( SPC ), organized in Quebec, Canada in January 2008. SPC is a variable interest entity as defined under applicable GAAP. Certain of our drug clinical studies are conducted through this entity, and we are obligated to fund all of its costs and have the sole rights to any revenue derived from its operations. Since we carry the full risks and rewards of this entity, we meet the applicable GAAP criteria as being its primary beneficiary . Accordingly, SPC s balance sheets and statements of operations are included in our Condensed Consolidated Financial Statements as if it were a wholly-owned subsidiary for all periods presented.

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**(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)**

**(Unaudited)**

***(c) Operating Segment***

We operate in one reportable operating segment that is focused exclusively on developing and commercializing oncology and hematology drug products. For the three and six months ended June 30, 2014 and 2013, all of our revenue and related expenses were solely attributable to these activities. Substantially all of our long-lived assets are located in the U.S.

**2. USE OF ESTIMATES AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The preparation of financial statements in conformity with GAAP requires our management to make informed estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent liabilities. On an on-going basis, our management evaluates its estimates, including those related to (i) gross-to-net revenue adjustments; (ii) the collectability of customer accounts; (iii) whether the cost of inventories can be recovered; (iv) the fair value of goodwill and intangible assets; (v) the realization of tax assets and estimates of tax liabilities; (vi) the likelihood of payment and value of contingent liabilities; (vii) the fair value of investments; (viii) assumptions used in reporting stock-based compensation; and (ix) the potential outcome of ongoing or threatened litigation.

Such estimates are based on our management's professional judgment which takes into account our Company's experience and all available facts. Nonetheless, actual results may materially differ from management's estimates. In our judgment, the accounting policies, estimates, and assumptions described below have the greatest potential to significantly impact the accompanying Condensed Consolidated Financial Statements:

***(i) Revenue Recognition***

*(a) Product Sales:* We sell our products to wholesalers and distributors. Our wholesalers and distributors in turn sell the products directly to end-users, such as clinics, hospitals, and private oncology-based practices. Revenue from product sales is recognized when title and risk of loss have transferred to our customer, and the following additional criteria are met:

- (1) appropriate evidence of a binding arrangement exists with our customer;
- (2) price is substantially fixed and determinable;

- (3) collection from our customer is reasonably assured;
- (4) our customer's obligation to pay us is not contingent on resale of the product;
- (5) we do not have significant obligations for future performance to directly bring about the resale of our product; and
- (6) we have a reasonable basis to estimate returns.

Our gross revenue is reduced by our gross-to-net ( GTN ) estimates, resulting in our reported Product sales, net in the accompanying Condensed Consolidated Statements of Operations. We defer revenue recognition in full if/when these estimates are not reasonably determinable at the time of sale. Information from external sources is used to estimate GTN adjustments. Such information includes written and oral information obtained from our wholesalers with respect to their inventory levels and sell-through to end-users during the period. The inventory information received from wholesalers is a product of their recordkeeping process. Our GTN estimates reduce revenue in the same period that the related sale is recorded and include the following major categories:

*Product Returns Allowances:* Our FUSILEV and MARQIBO customers (and BELEODAQ customers, beginning in the third quarter of 2014) are typically permitted to return products within six months of its expiration date, subject to certain restocking fees and preauthorization requirements. Returns for ZEVALIN and FOLOTYN expirations are not contractually or customarily allowed. We estimate potential returns, based on several factors, including historical rates of return, customer and end-user ordering patterns, inventory held by distributors, and sell through data of distributor sales to end users. In general, returned product is not resold.

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**(Unaudited)**

*Government Chargebacks:* Our products are subject to certain pricing limits under federal government programs. Qualifying entities purchase products through our distributors at the discounted price. Our distributors charge the difference between the list price and discounted price back to us, for which there may be significant lag time. Due to estimates inherent in determining the amount and volume of government chargebacks we will incur, the actual amount of government chargeback claims may be materially different from our estimates.

*Discounts:* Discounts for prompt payment are estimated based on the customer's payment history and our current expectations for timing of customer payment.

*Rebates:* Rebates are estimated based on the customer's actual purchase level during the quarterly or annual rebate purchase period, and the corresponding contractual rebate tier we expect the customer to achieve.

*Medicaid Rebates:* Our products are subject to state government-managed Medicaid programs whereby discounts and rebates are provided to participating state governments. Our calculations related to these rebate accruals require estimates, including estimates of customer mix, to determine which of our sales will be subject to rebates and the amount of such rebates. Our estimates are based on historical claims and forecasting techniques, as supplemented by management's judgment for many factors, including changes in sales trends and product pricing. Due to estimates and assumptions inherent in determining the amount of our product sales that will be subject to Medicaid rebates, and the time lag in us receiving these rebate notices (generally several months after the sale is made), the actual amount of these claims may be materially different from our estimates. As a result, Medicaid rebate adjustments affecting revenue may be prospectively recorded and reported over several periods after we reported the initial sale.

*Distribution, Data, and GPO Administrative Fees:* Distribution, data, and GPO administrative fees are paid to authorized wholesalers and specialty distributors of our products (except U.S. sales of ZEVALIN). These fees are based on a percentage of such estimated net sales and are for various services, including: contract administration, inventory management, product sales reporting by customer, and product returns processing.

*(b) License Fees:* We recognize revenue for our licensing of intellectual property to third parties, based on the terms of each contractual agreement. In general, this results in periodic revenue recognition as the licensee has sales for which we are entitled to a royalty, or in certain instances we may receive a lump-sum payment from licensees, in which case, revenue is fully recognized in that period.

*(c) Service Revenue:* We receive fees under certain arrangements for our research and development services. These services are generally performed in connection with a collaboration agreement with another pharmaceutical company. Payment may be triggered by the successful completion of a phase of development, results from a clinical trial, and/or regulatory approval events. We recognize revenue when the corresponding milestone is achieved, or the revenue is otherwise earned through our on-going activities.

ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) ( ASU 2014-09 ), was issued in May 2014 for our mandatory adoption beginning January 1, 2017 (no early adoption is permitted under this new revenue recognition standard). ASU 2014-09 requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve this core principle, the guidance provides that an entity should apply the following steps: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when, or as, the entity satisfies a performance obligation. We continue to evaluate the impact of ASU 2014-09 to our current revenue recognition models for *product sales*, *license fees*, and *service revenue*, as described above.

***(ii) Cash and Equivalents***

Our cash and equivalents consist of bank deposits and highly liquid investments with original maturities of three months or less from the original purchase date.



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**Notes to Condensed Consolidated Financial Statements**

**(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)**

**(Unaudited)**

***(iii) Marketable Securities***

Our marketable securities consist of our holdings in mutual funds and bank certificates of deposit. These are classified as available-for-sale, with any unrealized change in value reflected in unrealized gain (loss) on securities on the accompanying Condensed Consolidated Statements of Comprehensive Income (Loss). Realized gains and losses on available-for-sale securities are included in other expense on the accompanying Condensed Consolidated Statements of Operations.

***(iv) Accounts Receivable***

Our accounts receivable are derived from our product sales, license fees, and service revenue, and do not bear interest. The allowance for doubtful accounts is management's best estimate of the amount of probable credit losses in existing accounts receivable. Account balances are charged off against the allowance after appropriate collection efforts are exhausted.

***(v) Inventories***

We value inventory at the lower of the actual cost to purchase or manufacture it, or its market value (i.e., its net realizable value). Cost is determined on the first-in, first-out method (FIFO). We regularly review inventory quantities in process and on hand, and when appropriate, record a provision for obsolete and excess inventory to reduce it to its net realizable value.

Direct and indirect manufacturing costs related to the production of inventory in anticipation of FDA approval are expensed through research and development, rather than capitalized. Upon FDA approval, these direct and indirect manufacturing costs are subsequently capitalized to inventory as incurred.

***(vi) Property and Equipment***

Our property and equipment is stated at cost and depreciated on a straight-line basis over its estimated useful lives. In the case of leasehold improvements, depreciation is over the shorter of the estimated useful life or remaining term of the lease. We evaluate the recoverability of long-lived assets (which includes property and equipment) whenever events or changes in circumstances in our business indicate that the asset's carrying amount may not be recoverable through on-going operations.

***(vii) Goodwill and Intangible Assets***

Our goodwill represents the excess of our business acquisition cost over the estimated fair value of the net assets acquired in the corresponding transactions. Goodwill has an indefinite useful life and is not amortized, but is instead

tested for impairment on an annual basis, unless there are interim impairment indicators requiring earlier testing. We perform our annual evaluation as of October 1 each year.

We evaluate the recoverability of indefinite and definite lived intangible assets at least annually, or whenever events or changes in our business indicate that an intangible asset's carrying amount may not be recoverable. Such circumstances could include, but are not limited to the following:

- (a) a significant decrease in the market value of an asset;
- (b) a significant adverse change in the extent or manner in which an asset is used; or
- (c) an accumulation of costs significantly in excess of the amount originally expected for the acquisition of an asset.

**(viii) Stock-Based Compensation**

We recognize stock-based compensation expense for employees and directors over the equity award vesting period, on a straight-line basis, and is net of an estimated forfeiture rate which is periodically updated.

We use the Black-Scholes option pricing model to determine the fair value of stock option grants with service conditions for vesting, and the Monte Carlo valuation model to value equity awards with combined market conditions and service conditions for vesting. These models require the use of highly subjective assumptions, including the volatility of our stock price and the probability of the achievement of market capitalization thresholds.

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**Notes to Condensed Consolidated Financial Statements**

**(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)**

**(Unaudited)**

***(ix) Foreign Currency Translation and Transactions***

We translate the assets and liabilities of our foreign subsidiaries stated in local functional currencies to U.S. dollars at the rates of exchange in effect at the end of the period. Revenues and expenses are translated using rates of exchange in effect during the period. Gains and losses from the translation of financial statements denominated in the foreign functional currency are included as a separate component of accumulated other comprehensive loss in the Condensed Consolidated Balance Sheets.

We record foreign currency transactions, when denominated in something other than the respective functional currency of our applicable legal entity, at the exchange rate prevailing at the date of the transaction. Resulting unrealized and realized gains and losses are included in other income (expense), net within the Condensed Consolidated Statements of Operations. Foreign currency transaction gains and losses have not been significant for any period presented.

***(x) Basic and Diluted Net (Loss) Income per Share***

We calculate basic and diluted net (loss) income per share using the weighted average number of common shares outstanding during the periods presented. In periods of a net loss, basic and diluted loss per share are the same. For the diluted earnings per share calculation, we adjust the weighted average number of common shares outstanding to include only dilutive stock options, warrants, and other common stock equivalents outstanding during the period.

***(xi) Income Taxes***

Deferred tax assets and liabilities are recorded based on the estimated future tax effects of temporary differences between the tax basis of assets and liabilities and amounts reported in the financial statements, as well as operating losses and tax credit carry forwards using enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse. Realization of deferred tax assets is dependent upon future earnings, the timing and amount of which are uncertain.

We have recorded a valuation allowance to reduce our deferred tax assets, because we believe that, based upon a weighting of positive and negative factors, it is more likely than not that these deferred tax assets will not be realized. If/when we determine that our deferred tax assets are realizable, an adjustment to the corresponding valuation allowance would increase our net income in the period that such determination was made.

In the event that we are assessed interest and/or penalties from taxing authorities, such amounts would be included in income tax benefit (expense) within the Condensed Consolidated Statements of Operations and Comprehensive Income (Loss) in the period the notice was received.

***(xii) Research and Development Costs***

Our research and development costs are expensed as incurred.

***(xiii) Fair Value Measurements***

We determine measurement-date fair value based on the proceeds that would be received through the sale an asset, or that we would pay to settle or transfer a liability, in an orderly transaction between market participants. We utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. Fair value measurements are based on a three-tier hierarchy that prioritizes the inputs used to measure fair value. These tiers include the following:

*Level 1:* Quoted prices (unadjusted) in active markets for identical assets or liabilities that are publicly accessible at the measurement date.

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**SPECTRUM PHARMACEUTICALS, INC.**

**Notes to Condensed Consolidated Financial Statements**

**(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)**

**(Unaudited)**

*Level 2:* Observable prices that are based on inputs not quoted on active markets, but that are corroborated by market data. These inputs may include quoted prices for similar assets or liabilities or quoted market prices in markets that are not active to the general public.

*Level 3:* Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

Cash and cash equivalents within our accompanying Condensed Consolidated Balance Sheets include certificates of deposit and money market funds that are valued utilizing Level 2 inputs. Marketable securities consist of mutual funds that are also valued utilizing Level 2 inputs.

Other assets within our accompanying Condensed Consolidated Balance Sheets include equity securities that are valued using Level 1 inputs.

The fair value of our drug development liability within our accompanying Condensed Consolidated Balance Sheets was estimated using the discounted income approach model. The unobservable inputs (i.e., Level 3 inputs) in this valuation model that have the most significant effect on these liabilities include (i) estimates of research and development personnel costs needed to perform the research and development services, (ii) estimates of expected cash outflows to third parties for services and supplies over the expected period that the services will be performed, and (iii) an appropriate discount rate for these expenditures. These inputs are reviewed for reasonableness by management on at least on a quarterly basis.

Acquisition-related contingent obligations within our accompanying Condensed Consolidated Balance Sheets represent future amounts we may be required to pay in conjunction with various business combinations. See *Note 9(a)* for a discussion of contingent value rights granted as part of our acquisition of Talon, and *Note 9(b)* for the fair value of the liability associated with FDA approval of C-E MELPHALAN. These liabilities are valued using Level 3 inputs and include probabilities and assumptions related to the timing and likelihood of achievement of regulatory and sales milestones.

**3. BALANCE SHEET ACCOUNT DETAIL**

The composition of selected financial statement captions that comprise the accompanying Condensed Consolidated Balance Sheets are summarized below:

***(a) Cash and Cash Equivalents and Marketable Securities***

As of June 30, 2014 and December 31, 2013, our holdings included within cash and cash equivalents and marketable securities were at major financial institutions.

Our investment policy requires that investments in marketable securities be in only highly-rated instruments, which are primarily U.S. treasury bills or U.S. treasury-backed securities, with limitations on investing in securities of any single issuer. We maintain cash balances in excess of federally insured limits with reputable financial institutions. To a limited degree, the Federal Deposit Insurance Corporation (FDIC) and other third parties insure these investments. However, these investments are not insured against the possibility of a complete loss of earnings or principal and are inherently subject to the credit risk related to the continued credit worthiness of the underlying issuer and general credit market risks. We manage such risks on our portfolio by investing in highly liquid, highly rated instruments, and limit investing in long-term maturity instruments.

The carrying amount of our money market funds, bank certificate of deposits ( Bank CDs ), and mutual funds approximates their fair value (utilizing Level 2 inputs see *Note 2(xiii)*) because of our ability to immediately convert these instruments into cash with minimal expected change in value.

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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

The following is a summary of our cash and cash equivalents and marketable securities :

	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated fair Value	Cash and cash equivalents	Marketable Securities Current	Long Term
<b>June 30, 2014</b>							
Bank deposits	\$ 59,443	\$	\$	\$ 59,443	\$ 59,443	\$	\$
Money market funds	72,962			72,962	72,962		
Bank CDs	245			245		245	
Mutual funds	3,061			3,061		3,061	
Total cash and equivalents and marketable securities	\$ 135,711	\$	\$	\$ 135,711	\$ 132,405	\$ 3,306	\$
<b>December 31, 2013</b>							
Bank deposits	\$ 55,911	\$	\$	\$ 55,911	\$ 55,911	\$	\$
Money market funds	100,395			100,395	100,395		
Bank CDs	410			410		410	
Mutual funds	3,061			3,061		3,061	
Total cash and equivalents and marketable securities	\$ 159,777	\$	\$	\$ 159,777	\$ 156,306	\$ 3,471	\$

As of June 30, 2014, none of these securities had been in a continuous unrealized loss position longer than one year.

**(b) Property and Equipment**

Property and equipment, net of accumulated depreciation consist of the following:

	June 30, 2014	December 31, 2013
Computer hardware and software	\$ 3,258	\$ 5,154
Laboratory equipment	648	1,063
Office furniture	372	1,575

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Leasehold improvements	2,858	2,813
Property and equipment, at cost	7,136	10,605
(Less): Accumulated depreciation	(5,729)	(9,070)
Property and equipment, net of accumulated depreciation	\$ 1,407	\$ 1,535

Depreciation expense (included within operating costs and expenses in the accompanying Condensed Consolidated Statement of Operations) for the six months ended June 30, 2014 and 2013, was \$0.7 million in each period. During the three months ended June 30, 2014, we corrected our property and equipment to remove assets which were determined to no longer be in use (property and equipment at cost of \$4.2 million, less accumulated depreciation of \$4.0 million).

*(c) Inventories*

Inventories consist of the following:

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Raw materials	\$ 2,092	\$ 1,794
Work-in-process	2,095	3,312
Finished goods	6,694	8,413
	\$ 10,881	\$ 13,519



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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

*(d) Prepaid expenses and other current assets*

Prepaid expenses and other current assets consist of the following:

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Prepaid operating expenses	\$ 3,166	\$ 3,213
Research and development supplies	244	
	<b>\$ 3,410</b>	<b>\$ 3,213</b>

*(e) Other receivables*

Other receivables consist of the (i) amounts we expect to be refunded from taxing authorities for our income taxes paid, relating to fiscal year 2012 and the (ii) amounts we expect to be reimbursed from certain of our product development partners for incurred drug development expenses.

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Income tax receivable	\$ 9,098	\$ 7,539
Product development expenses reimbursement receivables	2,704	
	<b>\$ 11,802</b>	<b>\$ 7,539</b>

*(f) Intangible Assets and Goodwill*

Intangible assets, net of accumulated amortization consist of the following:

		<b>June 30, 2014</b>			
Historical Cost	Accumulated Amortization	Foreign Currency	Impairment	Net Amount	Full Amortization
					Remaining Amortization

	Translation				Period (years)		Period (years)	
MARQIBO IPR&D (NHL indication)	\$ 17,600	\$	\$	\$	\$ 17,600	n/a	n/a	
C-E MELPHALAN IPR&D	7,700				7,700	n/a	n/a	
MARQIBO distribution rights	26,900	(2,366)			24,534	11	9.7	
FOLOTYN distribution rights	118,400	(15,308)			103,092	13	10.9	
ZEVALIN distribution rights U.S.	41,900	(25,315)			16,585	10	4.5	
ZEVALIN distribution rights Ex-U.S.	23,490	(6,804)	453		17,139	8	5.6	
FUSILEV distribution rights	16,778	(5,546)			11,232	11	7.7	
FOLOTYN out-license*	27,900	(5,024)		(1,023)	21,853	10	8.0	
<b>Total intangible assets</b>	<b>\$ 280,668</b>	<b>\$(60,363)</b>	<b>\$ 453</b>	<b>\$ (1,023)</b>	<b>\$ 219,735</b>			

\* On May 29, 2013, we amended our collaboration agreement with Mundipharma in order to modify the scope of their licensed territories and the respective development obligations. As a result of the amendment, Europe and Turkey were excluded from Mundipharma's commercialization territory, and royalty and milestone rates were modified.

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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

The modification of our associated royalty and milestone rights constituted a change in the contractual provisions under which we measured our original acquired intangible asset (i.e., FOLOTYN rights). We determined that an impairment of the FOLOTYN out-license rights to Mundipharma of \$1.0 million resulted from this amendment.

	<b>December 31, 2013</b>				
	<b>Historical</b>	<b>Accumulated</b>	<b>Foreign</b>	<b>Impairment</b>	<b>Net Amount</b>
	<b>Cost</b>	<b>Amortization</b>	<b>Currency</b>		
	\$	\$	\$	\$	\$
MARQIBO IPR&D (NHL indication)	17,600	\$	\$	\$	17,600
C-E MELPHALAN IPR&D	7,700				7,700
MARQIBO distribution rights (ALL indication)	26,900	(1,107)			25,793
FOLOTYN distribution rights	118,400	(10,587)			107,813
ZEVALIN distribution rights U.S.	41,900	(23,455)			18,445
ZEVALIN distribution rights Ex-U.S.	23,490	(5,343)	682		18,829
FUSILEV distribution rights	16,778	(4,821)			11,957
FOLOTYN out-license	27,900	(3,662)		(1,023)	23,215
<b>Total intangible assets</b>	<b>\$ 280,668</b>	<b>\$(48,975)</b>	<b>\$ 682</b>	<b>\$ (1,023)</b>	<b>\$ 231,352</b>

Intangible asset amortization expense recognized in the six months ended June 30, 2014 and 2013 was \$11.4 million and \$9.9 million, respectively. Estimated intangible asset amortization expense (excluding incremental amortization from the reclassification of IPR&D to developed technology) for the remainder of 2014 and the five succeeding fiscal years and thereafter is as follows:

**Years Ending December 31**

Remainder of 2014	\$ 11,438
2015	22,877
2016	22,877
2017	22,877
2018	22,722
2019	19,157
2020 and thereafter	72,487

\$ 194,435

Goodwill is comprised of the following (by source):

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Acquisition of Talon	\$ 10,526	\$ 10,526
Acquisition of ZEVALIN Ex-U.S. distribution rights	2,525	2,525
Acquisition of Allos	5,346	5,346
Foreign currency exchange translation effects	79	104
	<b>\$ 18,476</b>	<b>\$ 18,501</b>

Table of Contents**SPECTRUM PHARMACEUTICALS, INC.****Notes to Condensed Consolidated Financial Statements****(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)****(Unaudited)****(g) Other assets**

Other assets are comprised of the following:

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Investments in equity securities	\$ 4,648	\$ 3,593
Supplies and other assets	691	
Deposits	193	190
2018 Convertible Notes issuance costs	3,124	3,432
Executive officer life insurance cash surrender value	6,541	5,362
	<b>\$ 15,197</b>	<b>\$ 12,577</b>

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## SPECTRUM PHARMACEUTICALS, INC.

## Notes to Condensed Consolidated Financial Statements

(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

*(h) Accounts payable and other accrued liabilities*

Accounts payable and other accrued liabilities are comprised of the following:

	June 30, 2014	December 31, 2013
Trade payables	\$ 7,620	\$ 12,796
Accrued research and development expenses	3,915	6,433
Accrued selling, general and administrative expenses	7,591	8,870
Accrued rebates	34,842	28,893
Accrued product royalty	3,599	9,498
Allowance for returns	1,500	2,900
Accrued data and distribution fees	2,934	2,430
Accrued GPO administrative fees	2,684	2,327
Inventory management fee	845	616
Allowance for chargebacks	3,648	5,074
	\$ 69,178	\$ 79,837

Amounts presented within accounts payable and other accrued liabilities in the accompanying Condensed Consolidated Balance Sheets specifically for GTN estimates (see *Note 2(i)*) are as follows:

Description	Rebates and Chargebacks	Data and Distribution, GPO Fees, and Inventory			Returns
		Management Fees	Prompt Pay Discount		
Balance as of December 31, 2012	\$ 26,176	\$ 14,149	\$ 1,451	\$ 5,056	
Add: provisions (recovery)	63,609	19,067	183	(2,034)	
(Less): credits or actual allowances	(55,818)	(27,843)	(1,317)	(122)	
Balance as of December 31, 2013	33,967	5,373	317	2,900	
Add: provisions (recovery)	34,721	9,416	5	(1,265)	

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(Less): credits or actual allowances	(30,198)	(8,326)	(281)	(135)
Balance as of June 30, 2014	\$ 38,490	\$ 6,463	\$ 41	\$ 1,500

*(i) Other long-term liabilities*

Other long-term liabilities are comprised of the following:

	<b>June 30, 2014</b>	<b>December 31, 2013</b>
Accrued executive deferred compensation	\$ 4,527	\$ 3,949
Deferred rent (non-current portion)	451	366
Business acquisition liability		298
Other tax liabilities	731	1,352
	<b>\$ 5,709</b>	<b>\$ 5,965</b>

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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

**4. GROSS-TO-NET PRODUCT SALES**

The below table presents a GTN product sales reconciliation for the accompanying Condensed Consolidated Statement of Operations:

	Three months ended		Six months ended	
	June 30,		June 30,	
	2014	2013	2014	2013
Gross product sales	\$ 68,329	\$ 57,522	\$ 129,828	\$ 100,494
Rebates and chargebacks	(17,772)	(20,365)	(34,721)	(31,083)
Data, distribution and GPO administrative fees	(4,920)	(5,704)	(9,416)	(10,046)
Prompt pay discount	(2)	(13)	(5)	(105)
Product returns allowance	1,220	773	1,265	2,299
Product sales, net	\$ 46,855	\$ 32,213	\$ 86,951	\$ 61,559

**5. PRODUCT SALES, NET BY GEOGRAPHIC REGION AND PRODUCT LINE**

The below table presents product sales, net by geography for the three and six months ended June 30, 2014 and 2013:

	Three months ended June 30,				Six months ended June 30,			
	2014		2013		2014		2013	
United States	\$ 44,541	95.1%	\$ 30,157	93.6%	\$ 81,998	94.3%	57,091	92.7%
International:								
Europe	796	1.7%	602	1.9%	1,836	2.1%	1,631	2.6%
Asia Pacific	1,518	3.2%	1,454	4.5%	3,117	3.6%	2,837	4.6%
Total international	2,314	4.9%	2,056	6.4%	4,953	5.7%	4,468	7.3%
Product sales, net	\$ 46,855	100.0%	\$ 32,213	100.0%	\$ 86,951	100.0%	61,559	100.0%

The below table presents product sales, net by product line for the three and six months ended June 30, 2014 and 2013:



	Three months ended June 30,				Six months ended June 30,			
	2014		2013		2014		2013	
FUSILEV	\$ 26,554	56.7%	\$ 12,864	39.9%	\$ 48,747	56.1%	\$ 24,706	40.1%
FOLOTYN	12,597	26.9%	12,557	39.0%	22,655	26.1%	22,481	36.5%
ZEVALIN	6,336	13.5%	6,792	21.1%	12,636	14.5%	14,372	23.3%
MARQIBO	1,368	2.9%		%	2,913	3.4%		%
Product sales, net	\$ 46,855	100.0%	\$ 32,213	100.0%	\$ 86,951	100.0%	\$ 61,559	100.0%

## 6. STOCK-BASED COMPENSATION

We classify our stock-based compensation expense (inclusive of our incentive stock plan, employee stock purchase plan, and 401(k) matching program) in the accompanying Condensed Consolidated Statements of Operations, based on the department to which the recipient belongs. Stock-based compensation expense included within operating costs and expenses for the three and six months ended June 30, 2014 and 2013 was as follows:

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Research and development	\$ 511	\$ 485	\$ 955	\$ 1,159
Selling, general and administrative	2,163	2,439	4,570	4,512
Total share-based compensation	\$ 2,674	\$ 2,924	\$ 5,525	\$ 5,671

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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

**7. NET LOSS PER SHARE**

Net loss per share was computed by dividing net loss by the weighted average number of common shares outstanding for the three and six months ended June 30, 2014 and 2013:

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Net loss	\$ (3,563)	\$ (9,721)	\$ (31,204)	\$ (15,157)
Weighted average shares basic and diluted	64,609,197	58,977,295	64,119,441	58,995,735
Net loss per share basic and diluted	\$ (0.06)	\$ (0.16)	\$ (0.49)	\$ (0.26)

The below-listed outstanding securities were excluded from our calculation of net loss per share, (using the treasury stock and if-converted method, as applicable), because their impact would have been anti-dilutive due to net loss per share in the three and six months ended June 30, 2014 and 2013:

	<b>Three months ended June 30,</b>		<b>Six months ended June 30,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
2018 Convertible Notes	11,401,284		11,401,284	
Common stock options	2,076,157	2,412,230	2,300,525	3,211,911
Restricted stock awards	1,021,825	1,102,654	1,021,825	1,102,654
Common stock warrants	111,601	115,249	129,512	173,031
Preferred stock	40,000	40,000	40,000	40,000
Total	14,650,867	3,670,133	14,893,146	4,527,596

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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

**8. FAIR VALUE MEASUREMENTS**

The below table summarizes certain asset and liability fair values that are included within our accompanying Condensed Consolidated Balance Sheets, and their designations among three fair value measurement categories (as described within *Note 2(xiii)*):

	<b>June 30, 2014</b>			
	<b>Fair Value Measurements</b>			
	<b>Level</b>			
	<b>1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<i>Assets:</i>				
Bank CDs	\$	\$ 245	\$	\$ 245
Money market currency funds		72,962		72,962
Mutual funds		3,061		3,061
Deferred compensation investments, including life insurance cash surrender value		6,541		6,541
Equity securities	4,648			4,648
	\$ 4,648	\$ 82,809	\$	\$ 87,457
<i>Liabilities:</i>				
Deferred executive compensation liability		4,527		4,527
Drug development liability			17,188	17,188
Ligand Contingent Consideration			4,300	4,300
Talon CVR			5,696	5,696
Corixa Liability			62	62
	\$	\$ 4,527	\$ 27,246	\$ 31,773

	<b>December 31, 2013</b>			
	<b>Fair Value Measurements</b>			
	<b>Level</b>			
	<b>1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
<i>Assets:</i>				
Bank CDs	\$	\$ 410	\$	\$ 410

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Money market currency funds	100,395		100,395
Mutual funds	3,061		3,061
Deferred compensation investments, including life insurance cash surrender value	5,362		5,362
Equity securities	3,593		3,593
	\$ 3,593	\$ 109,228	\$ 112,821

*Liabilities:*

Deferred executive compensation liability	3,949		3,949
Deferred development costs		17,742	17,742
Ligand Contingent Consideration		4,000	4,000
Talon CVR		4,329	4,329
	\$	\$ 3,949	\$ 26,071
			\$ 30,020

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(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)

(Unaudited)

The following summarizes the fair value measurement activity for our liabilities that utilize Level 3 inputs:

	<b>Fair Value Measurements of Unobservable Inputs (Level 3)</b>	
Balance at December 31, 2012	\$	14,520
Transfers in (out) of Level 3		
Deferred development costs		5,509
Deferred payment contingency		(2,287)
Ligand Contingent Consideration		4,000
Talon CVR		4,329
Balance at December 31, 2013		26,071
Transfers in (out) of Level 3		
Deferred development costs (see <i>Note 12</i> )		(554)
Ligand Contingent Consideration (see <i>Note 9(b)</i> )		300
Talon CVR (see <i>Note 9(a)</i> )		1,367
Corixa Liability (see <i>Note 13(b)(i)</i> )		62
Balance at June 30, 2014**	\$	27,246

\*\* This amount is comprised of current and long-term portion of drug development liability and acquisition-related contingent obligations on our accompanying Condensed Consolidated Balance Sheets.

**9. BUSINESS COMBINATIONS AND CONTINGENT CONSIDERATION*****(a) Acquisition of Talon Therapeutics, Inc.****Talon Acquisition Overview*

On July 17, 2013, we purchased all of the outstanding shares of common stock of Talon Therapeutics, Inc. ( Talon ). Through the acquisition of Talon, we gained worldwide rights to MARQIBO, an FDA-approved drug that we believe

complements our other hematology and oncology products.

The Talon purchase consideration comprised of (i) an aggregate upfront cash amount of \$11.3 million, (ii) issuance of 3.0 million shares of our common stock, then equivalent to \$26.3 million (based on a closing price of \$8.77 per share on July 17, 2013), and (iii) the issuance of contingent value rights ( CVR ) initially valued at \$6.5 million.

The CVR was valued using a valuation model that probability-weights expected outcomes (ranging from 50% to 100%) and discounts those amounts to their present value, using a discount rate of 25% (these represent unobservable inputs and are therefore classified as Level 3 inputs see Note 2 (xiii)). The CVR has a maximum payout of \$195.0 million if all sales and regulatory approval milestones are achieved, as summarized below:

\$5.0 million upon the achievement of net sales of MARQIBO in excess of \$30.0 million in any calendar year

\$10.0 million upon the achievement of net sales of MARQIBO in excess of \$60.0 million in any calendar year

\$25.0 million upon the achievement of net sales of MARQIBO in excess of \$100.0 million in any calendar year

\$50.0 million upon the achievement of net sales of MARQIBO in excess of \$200.0 million in any calendar year

\$100.0 million upon the achievement of net sales of MARQIBO in excess of \$400.0 million in any calendar year

\$5.0 million upon receipt of marketing authorization from the FDA regarding Menadione Topical Lotion

Table of Contents**SPECTRUM PHARMACEUTICALS, INC.****Notes to Condensed Consolidated Financial Statements****(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)****(Unaudited)***Talon CVR Fair Value as of June 30, 2014 and December 31, 2013*

The CVR fair value will continue to be evaluated on a quarterly basis. Current and future changes in its fair value results from the likelihood and timing of milestone achievement and/or the corresponding discount rate applied thereon. Adjustments to CVR fair value are recognized within change in fair value of contingent consideration related to acquisition in the accompanying Condensed Consolidated Statements of Operations.

	<b>Fair Value of Talon CVR</b>
December 31, 2013	\$ 4,329
Fair value adjustment for the six months ended June 30, 2014	1,367
June 30, 2014	\$ 5,696

***(b) Acquisition of Rights to Captisol-Enabled<sup>®</sup> Melphalan****Overview of Acquisition of Rights to Captisol-Enabled<sup>®</sup> Melphalan*

On March 8, 2013, we completed the acquisition of exclusive global development and commercialization rights to Captisol-enabled<sup>®</sup>, propylene glycol-free MELPHALAN ( C-E MELPHALAN ) for use as a conditioning treatment prior to autologous stem cell transplant for patients with multiple myeloma from CyDex Pharmaceuticals, Inc. a wholly-owned subsidiary of Ligand Pharmaceuticals Incorporated ( Ligand ) for an initial license fee of \$3.0 million (paid on April 1, 2013). Aggregate transaction costs were nominal for this acquisition.

We accounted for this transaction as a business combination (rather than as an asset acquisition), using the acquisition method of accounting. This requires that assets acquired and liabilities assumed be recognized on the balance sheet at their fair values, which involves our estimates of future cash flows and the application of appropriate discount rates as of the transaction date.

We are required to pay Ligand additional amounts up to an aggregate \$66.0 million, upon the achievement of certain regulatory milestones and net sales thresholds ( Ligand Contingent Consideration ), and we also assumed full responsibility for its ongoing clinical and regulatory development program. We also must pay royalties in the range of 15% to 25% on our future net sales of licensed products in all territories.

*Consideration Transferred*

The acquisition-date fair value of the consideration transferred consisted of the following items:

Cash consideration	\$ 3,000
Ligand Contingent Consideration	4,700
<b>Total purchase consideration</b>	<b>\$ 7,700</b>

*Fair Value Estimate of Asset Acquired and Liability Assumed*

The total purchase consideration is allocated to the acquisition of the net tangible and intangible assets based on their estimated fair values as of the closing date. The allocation of the total purchase price to the net assets acquired is as follows:

IPR&D Captisol-enabled <sup>®</sup> , propylene glycol-free MELPHALAN rights	\$ 7,700
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IPR&D is an intangible asset that is classified as indefinite-lived until the completion or abandonment of the associated R&D effort, and is subject to impairment testing. C-E MELPHALAN IPR&D will be amortized over an estimated useful life to be determined at the date the project is complete.

We estimated the fair value of this IPR&D using the income approach. The income approach uses valuation techniques to convert future amounts to a single present amount (discounted). Our measurement is based on the value indicated by current market expectations about those future amounts. The fair value estimate took into account our estimates of future incremental earnings that may be achieved upon regulatory approval, promotion, and distribution associated with the rights, and included estimated cash flows of approximately 10 years and a discount rate of approximately 25%.



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The fair value of the contingent consideration liability assumed was determined using the probability of success and the discounted cash flow method of the income approach, which assumes that FDA approval of C-E MELPHALAN will occur on or about December 31, 2015. Upon receipt of FDA approval, we will be obligated to make a milestone payment to Ligand.

*Ligand Contingent Consideration Fair Value as of June 30, 2014 and December 31, 2013*

The Ligand Contingent Consideration fair value will continue to be evaluated on a quarterly basis. This liability is included within acquisition-related contingent obligations in the accompanying Condensed Consolidated Balance Sheets. Current and future changes in its fair value results from the likelihood and timing of milestone achievement and/or the corresponding discount rate applied thereon. Adjustments to Ligand Contingent Consideration fair value are recognized within change in fair value of contingent consideration related to acquisition in the accompanying Condensed Consolidated Statements of Operations.

	<b>Fair Value of Ligand Contingent Consideration</b>
December 31, 2013	\$ 4,000
Fair value adjustment for the six months ended June 30, 2014	300
June 30, 2014	\$ 4,300

**10. REVOLVING LINE OF CREDIT**

We entered into a credit agreement on September 5, 2012 with Bank of America, N.A. as the administrative agent and Wells Fargo Bank, N.A. as an initial lender (the Credit Agreement). The Credit Agreement provided us with a committed \$50.0 million revolving line of credit facility (the Credit Facility). The Credit Facility was repaid in full, then immediately terminated, on December 20, 2013 in connection with the sale and issuance of our 2018 Convertible Notes (see Note 11).

The Credit Facility bore interest, at our election, at a rate equal to the London Interbank Offer Rate (LIBOR), plus an applicable margin (2.75% to 4.25%, dependent on a defined liquidity ratio). An unused line fee was payable quarterly in an amount ranging from 0.38% to 0.63%.

## 11. CONVERTIBLE SENIOR NOTES

On December 17, 2013, we entered into an agreement for the sale of \$120.0 million aggregate principal amount of 2.75% Convertible Senior Notes due December 2018 (the 2018 Convertible Notes ). The 2018 Convertible Notes are convertible into shares of our common stock at a conversion rate of 95 shares per \$1,000 principal amount of the 2018 Convertible Notes, totaling 11.4 million common shares if fully converted. The in-the-money conversion price is equivalent to \$10.53 per common share. The conversion rate and conversion price is subject to adjustment under certain limited circumstances. The 2018 Convertible Notes bear interest at a rate of 2.75% per year, payable semiannually in arrears on June 15 and December 15 of each year, beginning on June 15, 2014. The 2018 Convertible Notes will mature and become payable on December 15, 2018, subject to earlier conversion into common stock at the holders option.

The sale of the 2018 Convertible Notes closed on December 23, 2013 and our net proceeds were \$115.4 million, after deducting banker and professional fees of \$4.6 million. We used a portion of these net proceeds to simultaneously enter into bought call and sold warrant transactions with Royal Bank of Canada (collectively, the Note Hedge ). We recorded the Note Hedge on a net cost basis of \$13.1 million, as a reduction to additional paid-in capital in our accompanying Condensed Consolidated Balance Sheets. Under applicable GAAP, the Note Hedge transaction is not expected to be marked-to-market through earnings or comprehensive income in future reported periods.

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We entered into Note Hedge transactions to reduce the potential dilution to our stockholders and/or offset any cash payments that we are required to make in excess of the principal amount, upon conversion of the 2018 Convertible Notes (in the event that the market price of our common stock is greater than the conversion price). The strike price of the bought call is equal to the conversion price and conversion rate of the 2018 Convertible Notes, matching the 11.4 million common shares the 2018 Convertible Notes may be converted into. The strike price of our sold warrant is \$14.03 per share of our common stock, and is also for 11.4 million common shares.

As of June 30, 2014, the 2018 Convertible Notes could be converted into common stock. Prior to June 15, 2018, holders may convert all or a portion of their 2018 Convertible Notes only under the following circumstances: (1) during any fiscal quarter (and only during such fiscal quarter), if, for at least 20 trading days (whether or not consecutive) during the 30 consecutive trading day period ending on the last trading day of the immediately preceding fiscal quarter, the last reported sale price of our common stock on such trading day is greater than or equal to 130% of the applicable conversion price on such trading day; (2) during the five consecutive business day period immediately following any five consecutive trading day period in which, for each trading day of that measurement period, the trading price per \$1,000 principal amount of 2018 Convertible Notes for such trading day was less than 98% of the *product* of (i) the last reported sale price of our common stock on such trading day and (ii) the applicable conversion rate on such trading day; (3) upon the occurrence of certain corporate transactions; and (4) at any time prior to our stockholders' approval to settle the 2018 Convertible Notes in our common shares and/or cash. On and after June 15, 2018 until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert all or a portion of their 2018 Convertible Notes at any time.

We initially may only settle conversions of the 2018 Convertible Notes by delivering shares of our common stock. However, if we obtain stockholder approval, we may, at our election, settle conversions of the 2018 Convertible Notes by paying or delivering, as the case may be, cash, shares of common stock, or a combination of cash and shares of common stock.

The carrying value of the 2018 Convertible Notes as of June 30, 2014 is summarized as follows:

Principal amount	\$ 120,000
(Less): Unamortized debt discount (amortized through December 2018)	(26,188)
June 30, 2014	\$ 93,812

The following table sets forth the components of the interest expense recognized in the accompanying Condensed Consolidated Statements of Operations for the 2018 Convertible Notes for the six months ended June 30, 2014:

Contractual coupon interest expense	\$ 1,659
Amortization of debt issuance costs	308
Accretion of debt discount	2,332
Total	\$ 4,299
Effective interest rate	8.59%

## 12. MUNDIPHARMA AGREEMENT

As the result of our acquisition of Allos Therapeutics, Inc. on September 5, 2012 (through which we obtained distribution rights for FOLOTYN), we assumed its obligations under an active strategic collaboration agreement with a third-party, Mundipharma (the Mundipharma Collaboration Agreement ). Under the Mundipharma Collaboration Agreement, we retained full commercialization rights for FOLOTYN in the U.S. and Canada, with Mundipharma having exclusive rights to commercialize FOLOTYN in all other countries in the world (the Mundipharma Territories ).

On May 29, 2013, the Mundipharma Collaboration Agreement was amended and restated (the Amended Mundipharma Collaboration Agreement ), in order to modify: (i) the scope of the licensed territory, (ii) milestone payments, (iii) royalty rates, and (iv) development obligations. In connection with the Amended Mundipharma Collaboration Agreement, we received a one-time \$7.0 million payment from Mundipharma for certain research and development activities performed by us.

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As a result of the Amended Mundipharma Collaboration Agreement, (a) Europe and Turkey were excluded from Mundipharma's commercialization territory, (b) we may receive regulatory milestone payments of up to \$16.0 million, and commercial progress and sales-dependent milestone payments of up to \$107.0 million, (c) we will receive tiered double-digit royalties based on net sales of FOLOTYN within Mundipharma's licensed territories, and (d) we and Mundipharma will bear our own FOLOTYN development costs.

We recorded the initial September 2012 fair value of the related drug development liability of \$12.3 million, using the discounted cash flow method of the income approach. The fair value of this liability was determined to be \$17.2 million as of June 30, 2014 (inclusive of the \$7.0 million payment received from Mundipharma). This value is included in the current and long-term portions of drug development liability within the accompanying Condensed Consolidated Balance Sheets, and it includes our assumptions about personnel needed to perform these research and development activities, third party costs for projected clinical trial enrollment, and patient treatment-related follow up through approximately 2031.

We will assess this liability at each subsequent reporting date and record its adjustment through research and development expense in our Condensed Consolidated Statements of Operations.

	<b>Drug Development Liability, Current FOLOTYN</b>	<b>Drug Development Liability, Long Term FOLOTYN</b>	<b>Total Drug Development Liability FOLOTYN</b>
Balance at December 31, 2013	\$ 3,119	\$ 14,623	\$ 17,742
Transfer from long term to current			
(Less): Expenses incurred		(554)	(554)
Balance at June 30, 2014	\$ 3,119	\$ 14,069	\$ 17,188

**13. COMMITMENTS AND CONTINGENCIES****(a) Facility Leases**

We lease our principal executive office in Henderson, Nevada under a non-cancelable operating lease expiring April 30, 2019. We also lease our research and development facility in Irvine, California under a non-cancelable operating lease expiring May 31, 2019, in addition to several other administrative office leases. Each lease agreement contains scheduled rent increases which are accounted for on a straight-line basis.

***(b) Licensing Agreements, Co-Development Agreements, and Milestone Payments***

Our drug candidates are being developed pursuant to license agreements that provide us with territory-specific rights to its manufacture, sublicense, and sale. We are generally responsible for all development costs, patent filings and maintenance costs, sales and marketing costs, and liability insurance costs. We are also obligated to make certain milestone payments to third parties upon the achievement of regulatory and sales milestones that are specified in these license agreements. We estimate and present a corresponding liability on our Condensed Consolidated Balance Sheets when amounts are probable and reasonably estimable. In addition, we are obligated to pay royalties based on our current and future net sales of in-licensed products.

Our most significant of these agreements are listed and summarized below:

***(i) ZEVALIN U.S.: Licensing and development in the U.S.***

In December 2008, we acquired rights to commercialize and develop ZEVALIN in the U.S. as the result of a transaction with a third-party, Cell Therapeutics, Inc. ( CTI ) through our wholly-owned subsidiary, RIT Oncology LLC ( RIT ), where we assumed certain agreements with various third parties related to ZEVALIN intellectual property related to its manufacture, use, and sale in the U.S.

In accordance with the terms of assumed contracts, we are required to meet specified payment obligations, including a milestone payment to Corixa Corporation of \$5.0 million based on ZEVALIN sales in the U.S. (the Corixa Liability ). This milestone has not yet been met, and \$0.1 million for this potential milestone achievement is included within acquisition-related contingent obligations in our accompanying June 30, 2014 Condensed Consolidated Balance Sheet. Our U.S. net sales-based royalties are in the low to mid-single digits to Genentech, Inc. and mid-single digits to Corixa.

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***(ii) ZEVALIN Ex-U.S.: License and Asset Purchase Agreement with Bayer Pharma***

On April 1, 2012, through our wholly-owned subsidiary, Spectrum Pharmaceuticals Cayman, L.P., we completed the acquisition of licensing rights to market ZEVALIN outside of the U.S. from Bayer Pharma AG ( Bayer ).

ZEVALIN is currently approved in more than 40 countries outside the U.S. for the treatment of B-cell non-Hodgkin lymphoma, including countries in Europe, Latin America and Asia. In consideration for the rights granted under the agreement, concurrent with the closing, we paid Bayer a one-time fee of 19.0 million, and we will pay Bayer royalties based on a mid-teen digits percentage of net sales of the licensed products in all territories worldwide, except the U.S. Unless earlier terminated, the term of the agreement continues until the expiration of the last-to-expire patent covering the sale of a licensed product in the relevant country, or 15 years from the date of first commercial sale of the licensed product in such country, whichever is longer.

***(iii) FUSILEV: Amended and Restated License Agreement with Merck & Cie AG***

In May 2006, we amended and restated a license agreement with Merck & Cie AG ( Merck ), which we assumed in connection with our March 2006 acquisition of the assets of Targent. Pursuant to the license agreement with Merck, we obtained the exclusive license to use regulatory filings related to FUSILEV and a non-exclusive license under certain patents and know-how to develop, manufacture, use, and sell FUSILEV in the field of oncology in North America in return for royalties in the mid-single digits percentage of net sales. Merck is eligible to receive a \$0.2 million payment from us upon the achievement of a FDA approval of an oral form of FUSILEV. This milestone has not yet been met, and no such value is included within total liabilities in our accompanying Condensed Consolidated Balance Sheets for its potential achievement.

***(iv) FOLOTYN: License Agreement with Sloan-Kettering Institute, SRI International and Southern Research Institute***

In December 2002, Allos entered into the FOLOTYN License Agreement with Sloan-Kettering Institute for Cancer Research, SRI International, and Southern Research Institute. As a result of Allos becoming our wholly owned subsidiary on September 5, 2012, we are bound by the FOLOTYN License Agreement under which we obtained exclusive worldwide rights to a portfolio of patents and patent applications related to FOLOTYN and its uses. Under the terms of the FOLOTYN License Agreement, we are required to fund all development programs and will have sole responsibility for all commercialization activities. In addition, we pay the licensors royalties based on worldwide graduated annual levels of net sales of FOLOTYN, or sublicense revenues arising from sublicensing the product, if and when such sales or sublicenses occur. Royalties are 8% of annual worldwide net sales up to \$150 million; 9% of annual worldwide net sales of \$150 million through \$300 million; and 11% of annual worldwide net sales in excess of \$300 million.

**(v) C-E MELPHALAN: License Agreement with Cydex Pharmaceuticals, Inc.**

On March 8, 2013, we completed the acquisition of exclusive global development and commercialization rights to C-E MELPHALAN from Ligand (see *Note 9(b)*). We reported on April 23, 2014 that C-E MELPHALAN had met its primary endpoint in a pivotal trial for use as a conditioning treatment prior to autologous stem cell transplant for patients with multiple myeloma, and as a result, we intend to file a NDA with the FDA in the second half of 2014.

We assumed full responsibility for its ongoing clinical and regulatory development program. We are required to pay Ligand additional amounts of up to \$66 million, upon achievement of certain regulatory milestones and net sales thresholds, which we have valued at \$4.3 million and \$4.0 million within acquisition-related contingent obligations in our accompanying Condensed Consolidated Statements of Operations as of June 30, 2014 and December 31, 2013, respectively. We will also pay royalties in the range of 15% to 25% on our net sales of licensed products in all territories.

**(vi) MARQIBO: Agreement with Talon Therapeutics, Inc.**

On July 17, 2013, we completed the acquisition of Talon, through which we obtained exclusive global development and commercialization rights to MARQIBO (see *Note 9(a)*). As part of this acquisition, we issued the former Talon stockholders contingent value rights ( CVR ) that we have valued and presented on our accompanying Condensed



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Consolidated Balance Sheets as a \$5.7 million and \$4.3 million liability within acquisition-related contingent obligations as of June 30, 2014 and December 31, 2013, respectively. The CVR has a maximum payout of \$195 million if all sales and regulatory approval milestones are achieved.

***(vii) APAZQUONE: In-License Agreement with Allergan, Inc.***

In October 2008, we entered into an exclusive development and commercialization collaboration agreement with Allergan for APAZQUONE. Pursuant to the terms of the agreement, Allergan paid us an up-front non-refundable fee of \$41.5 million at closing (which we have amortized through revenue within license fees and service revenue in full as of December 31, 2013).

On January 29, 2013, we entered into a second amendment to the license, development, supply and distribution agreement with Allergan to amend the agreement and reacquire the rights originally licensed to Allergan in the U.S., Europe, and other territories in exchange for a tiered single-digit royalty on certain products containing APAZQUONE, and relieved Allergan of its development and commercialization obligations.

As a result of this amendment to the agreement, Allergan has no remaining obligations to us. We will be obligated to pay Allergan a tiered single-digit royalty not to exceed mid-single digits based upon our net sales of certain products containing APAZQUONE in specified territories. Additionally, we will be obligated to pay any royalties or other payments due to certain licensors of underlying intellectual property, as well as to provide indemnification of Allergan for claims arising from the manufacture, development, or commercialization of pharmaceutical products containing APAZQUONE by us.

***(viii) APAZQUONE: Collaboration Agreement with Nippon Kayaku Co. LTD.***

In November 2009, we entered into a collaboration agreement with Nippon Kayaku Co., LTD. ( Nippon Kayaku ) for the development and commercialization of APAZQUONE in Asia, except North and South Korea (the Nippon Kayaku Territory ). In addition, Nippon Kayaku received exclusive rights to APAZQUONE for the treatment of non-muscle invasive bladder cancer in Asia (other than North and South Korea), including Japan and China. Nippon Kayaku will conduct APAZQUONE clinical trials in the Nippon Kayaku Territory pursuant to a development plan. Further, Nippon Kayaku will be responsible for all expenses relating to the development and commercialization of APAZQUONE in the Nippon Kayaku Territory.

Pursuant to the terms of this agreement, Nippon Kayaku paid us an upfront fee of \$15.0 million (which we have amortized through revenue within license fees and service revenue in full as of December 31, 2013). Nippon Kayaku is also obligated to make additional payments to us based on the achievement of certain development, regulatory and commercialization milestones. Under the terms of the agreement, we are entitled to payment of \$10 million and \$126 million upon achievement of certain regulatory and commercialization milestones, respectively. Also, Nippon Kayaku

has agreed to pay us royalties based on a percentage of net sales of the subject products in the defined territory in the mid-teen digits.

Our license agreement with Nippon Kayaku provides for payments to us upon the achievement of development milestones, such as the completion of clinical trials or regulatory submissions, approvals by health authorities, and commercial launches of drug candidates. Given the challenges inherent in developing and obtaining approval for drug products and in achieving commercial launches, there was substantial uncertainty whether any such milestones would be achieved at the time of execution of such license agreement. Such revenue will only be recognized if/when such milestones are achieved.

***(ix) BELEODAQ: Licensing and Collaboration Agreement with TopoTarget***

In February 2010, we entered into a licensing and collaboration agreement with TopoTarget A/S ( TopoTarget ), as amended in October 2013, for the development and commercialization of BELEODAQ. The agreement provides that we have the exclusive right to manufacture, develop, and commercialize BELEODAQ in North America and India, with an option for China. Pursuant to the terms of this agreement, we paid TopoTarget an upfront fee of \$30.0 million in 2010.

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Under continuing terms, all development, including studies, will be conducted under a joint development plan, which we will fund 70% of such costs, and TopoTarget will fund 30%. We have final decision-making authority for all developmental activities in North America and India (and China upon exercise of its option). TopoTarget has final decision-making authority for all developmental activities in all other jurisdictions.

In February 2014, upon FDA acceptance of our new drug application (NDA), we issued TopoTarget 1.0 million shares of our common stock, and made a \$10.0 million milestone payment to them. The aggregate payout value of this first milestone was \$17.8 million and is recognized within research and development of the accompanying Condensed Consolidated Statement of Operations for the six months ended June 30, 2014.

In July 2014, we received approval from the FDA for BELEODAQ's use for injection for the treatment of PTCL, and as a result, we are obligated to TopoTarget for a second milestone payment of \$25.0 million by November 2014. As of June 30, 2014, no provision for this milestone (given its timing after our June 30, 2014 balance sheet date), or any other remaining regulatory or sales-based milestone aggregating \$278.0 million is included within total liabilities in our accompanying Condensed Consolidated Balance Sheets for potential achievement.

We will pay TopoTarget future royalties in the mid-teen digits based on net sales of BELEODAQ in the defined territory. The agreement will continue until the expiration of the last royalty payment period in the last country in the defined territory with certain provisions surviving, unless earlier terminated in accordance with its terms.

***(x) SPI-2012: Co-Development and Commercialization Agreement with Hanmi Pharmaceutical Company***

In January 2012, we entered into a co-development and commercialization agreement with Hanmi Pharmaceutical Company, ( Hanmi ), for SPI-2012, formerly known as LAPS-GCSF, a drug for the treatment of chemotherapy induced neutropenia based on Hanmi's proprietary LAPSCOVERY Technology, at which time we paid Hanmi \$1.0 million. Under the terms of the agreement, as amended in March 2014, we will share the expenses of this study, and we continue to have primary responsibility for the SPI-2012 development plan. If SPI-2012 is ultimately commercialized by us, we will have worldwide rights, except for Korea, China, and Japan upon our payment of agreed-upon fees to Hanmi. We will also be responsible for milestone payments related to SPI-2012 regulatory approvals and sales thresholds.

**(c) Service Agreements**

In connection with the research and development of our drug products, we have entered into contracts with numerous third party service providers, such as radio-pharmacies, distributors, clinical trial centers, clinical research organizations, data monitoring centers, and with drug formulation, development and testing laboratories. The financial terms of these agreements are varied and generally obligate us to pay in stages, depending on achievement of certain events specified in the agreements, such as contract execution, reservation of service or production capacity, actual

performance of service, or the successful accrual and dosing of patients.

At each period end, we accrue for all services received, with such accruals based on factors such as estimates of work performed, patient enrollment, completion of patient studies and other events. Should we decide to discontinue and/or slow-down the work on any project, the associated costs for those projects would be limited to the extent of the work completed. Generally, we are able to terminate these contracts due to the discontinuance of the related project(s) and thus avoid paying for the services that have not yet been rendered.

**(d) Supply Agreements**

We have entered into certain supply agreements, or have issued purchase orders, which require us to make minimum purchases from vendors for the manufacture of our products. These commitments do not exceed our planned commercial requirements (except for certain amounts accrued for within the accompanying Condensed Consolidated Financial Statements), and the contracted prices do not exceed their fair market value.

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**(e) Employment Agreement**

We have entered into an employment agreement with our Chief Executive Officer under which cash compensation and benefits would become payable in the event of termination by us for any reason other than cause, his resignation for good reason, or upon a change in control of our Company.

**(f) Deferred Compensation Plan**

The Spectrum Pharmaceuticals, Inc. Deferred Compensation Plan (the DC Plan ) is administered by the Compensation Committee of our Board of Directors and is intended to comply with the requirements of Section 409A of the Internal Revenue Code of 1986, as amended.

The DC Plan is maintained to provide deferred compensation benefits for a select group of our employees (the DC Participants ). Under the DC Plan, we provide the DC Participants with the opportunity to make annual elections to defer up to a specified amount or percentage of their eligible cash compensation, and we have the option to make discretionary contributions. At June 30, 2014 and December 31, 2013, DC Plan deferrals and contributions totaling \$4.5 million and \$3.9 million, respectively, are included within other long-term liabilities in the accompanying Condensed Consolidated Balance Sheets.

**(g) Litigation**

We are involved from time-to-time with various legal matters arising in the ordinary course of business. These claims and legal proceedings are of a nature we believe are normal and incidental to a pharmaceutical business, and may include product liability, intellectual property, employment matters, and other general claims.

We make provisions for liabilities when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Such provisions are reviewed at least quarterly and adjusted to reflect the impact of any settlement negotiations, judicial and administrative rulings, advice of legal counsel, and other information and events pertaining to a particular case. Litigation is inherently unpredictable. Although the ultimate resolution of these various matters cannot be determined at this time, we do not believe that such matters, individually or in the aggregate, will have a material adverse effect on our consolidated results of operations, cash flows, or financial condition.

We are presently responding to Abbreviated New Drug Applications ( ANDAs ) filed by companies seeking to launch generic forms of FUSILEV and FOLOTYN, respectively, and to certain shareholder suits that purportedly stem from our March 12, 2013 press release, in which we announced anticipated changes in customer ordering patterns of FUSILEV. These complaints allege that, as a result of the March 12, 2013 press release, our stock price declined.

***FUSILEV ANDA Litigation***

On January 20, 2012, March 2, 2012, and June 18, 2014, respectively, we filed suit against Sandoz Inc. and Innopharma Inc., and Ben Venue Laboratories, Inc., respectively, following Paragraph IV certifications in connection with their filing separate ANDAs, to manufacture a generic version of FUSILEV. We filed the lawsuits in the U.S. District Court for the Districts of Nevada and Delaware seeking to enjoin the approval of their ANDAs plus recovery of our litigation fees and costs incurred in such matters. On December 9, 2013, three Mylan entities collaborating with Innopharma were joined to Innopharma case. While we believe our patent rights are strong, the ultimate outcome of these cases is uncertain.

***FOLOTYN ANDA Litigation***

On June 19, 2014, we filed a lawsuit against five parties resulting from Paragraph IV certifications in connection with four separate ANDAs to manufacture a generic version of FOLOTYN: (1) Teva Pharmaceuticals USA, Inc., (2) Sandoz Inc., (3) Fresenius Kabi USA, LLC, and (4) Dr. Reddy's Laboratories, Ltd., and Dr. Reddy's Laboratories, Inc. We filed the lawsuit in the U.S. District Court for the District of Delaware seeking to enjoin the approval of their ANDAs plus recovery of our litigation fees and costs. While we believe our patent rights are strong, the ultimate outcome of such action is uncertain.

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***Shareholder Litigation***

*John Perry v. Spectrum Pharmaceuticals, Inc. et al.* (Filed March 14, 2013 in United States District Court, District of Nevada; Case Number 2:2013-cv-00433-LDG-CWH). This putative consolidated class action raises substantially identical claims and allegations against defendants Spectrum Pharmaceuticals, Inc., Dr. Rajesh C. Shrotriya, Brett L. Scott, and Joseph Kenneth Keller. The alleged class period is August 8, 2012 to March 12, 2013. The lawsuits allege a violation of Section 10(b) of the Securities Exchange Act of 1934 against all defendants and control person liability, as a violation of Section 20(b) of the Securities Exchange Act of 1934, against the individual defendants. The claims purportedly stem from the Company's March 12, 2013 press release, in which it announced that it anticipated a change in ordering patterns of FUSILEV. The complaints allege that, as a result of the March 12, 2013 press release, the Company's stock price declined. The complaints further allege that during the putative class period certain defendants made misleadingly optimistic statements about FUSILEV sales, which inflated the trading price of Company stock. The lawsuits seek relief in the form of monetary damages, costs and fees, and any other equitable or injunctive relief that the court deems appropriate. On March 21, 2014, the Court entered an order appointing Arkansas Teacher Retirement System as lead plaintiff. On May 20, 2014, Arkansas Teacher Retirement System filed a consolidated amended class action complaint. On July 18, 2014, we filed a motion to dismiss the consolidated amended class action complaint.

*Timothy Fik v. Rajesh C. Shrotriya, et al.* (Filed April 11, 2013 in United States District Court, District of Nevada; Case Number 2:2013-cv-00624-JCM-CWH); *Christopher J. Watkins v. Rajesh C. Shrotriya, et al.* (Filed April 22, 2013 in United States District Court, District of Nevada; Case Number 2:2013-cv-00684-JCM-VCF); and *Stefan Muenchhagen v. Rajesh C. Shrotriya, et al.* (Filed May 28, 2013 in United States District Court, District of Nevada; Case Number 2:2013-cv-00942-APG-PAL). These derivative complaints are brought by the respective purported shareholders on behalf of nominal plaintiff Spectrum against certain current and former directors and officers. The complaints generally allege breaches of fiduciary based on conduct relating to the events alleged in the consolidated *Perry* action. The complaints seek compensatory damages, corporate governance reforms, restitution and disgorgement of defendants' alleged profits, and costs and fees. On May 15, 2013, the court entered a consolidation order staying the actions pending resolution of the federal securities class action.

*Hardik Kakadia v. Rajesh C. Shrotriya, et al.* (Filed April 23, 2013 in the Eighth Judicial District Court of the State of Nevada in and for Clark County; Case Number A-13-680643-B); and *Joel Besner v. Rajesh C. Shrotriya, et al.* (Filed May 31, 2013 in the Eighth Judicial District Court of the State of Nevada in and for Clark County; Case Number A-13-682668-C) (collectively the State Derivative Actions). These consolidated State Derivative Actions are brought by the respective purported shareholders on behalf of nominal plaintiff Spectrum Pharmaceuticals, Inc. and are substantially similar to the consolidated federal derivative actions.

**(h) SEC Subpoena**

On April 1, 2013, we received a subpoena from the SEC for documents pursuant to a formal order of investigation. The subpoena followed our March 12, 2013 announcement that we anticipated a change in customer ordering patterns of FUSILEV. We continue to cooperate with this SEC investigation, though we cannot predict its outcome, or the timing of resolution.

#### **14. INCOME TAXES**

We apply an estimated annual effective tax rate ( ETR ) approach for calculating a tax provision for interim periods, as required under GAAP. We recorded a benefit for income taxes of \$1.2 million and \$5.3 million for the six months ended June 30, 2014 and 2013, respectively. Our ETR differs from the U.S. federal statutory tax rate of 35% primarily as a result of nondeductible expenses, state income taxes, foreign income taxes, and the impact of a valuation allowance on our deferred tax assets. In addition, in the six months ended June 30, 2014, we expensed approximately \$1.2 million related to the correction of our prior year estimate of carryback of federal net operating losses and of credits ineligible for offset against federal income taxes.

Our provision for income taxes is computed using the asset and liability method, under which deferred tax assets and liabilities are recognized for the expected future tax consequences of temporary differences between the financial reporting and tax bases of assets and liabilities, and for the expected future tax benefit to be derived from tax loss and credit carryforwards.



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**SPECTRUM PHARMACEUTICALS, INC.**

**Notes to Condensed Consolidated Financial Statements**

**(all tabular amounts presented in thousands, except share, per share, per unit, and number of years)**

**(Unaudited)**

Deferred tax assets and liabilities are determined using the enacted tax rates in effect for the years in which those tax assets are expected to be realized. A valuation allowance is established when it is more likely than not the future realization of all or some of the deferred tax assets will not be achieved. The evaluation of the need for a valuation allowance is performed on a jurisdiction by jurisdiction basis, and includes a review of all available positive and negative evidence.

We recognize excess tax benefits associated with share-based compensation to stockholders' equity only when realized. When assessing whether excess tax benefits relating to share-based compensation have been realized, we follow the with-and-without approach, excluding any indirect effects of the excess tax deductions. Under this approach, excess tax benefits related to share-based compensation are not deemed to be realized until after the utilization of all other tax benefits available to us. We recognize the impact of a tax position in our financial statements only if that position is more likely than not of being sustained upon examination by taxing authorities, based on the technical merits of the position. Any interest and penalties related to uncertain tax positions will be reflected in income tax expense.

**15. SUBSEQUENT EVENT**

*FDA Approval of BELEODAQ*

On July 3, 2014, the FDA granted us accelerated approval of BELEODAQ for injection for the treatment of patients with relapsed or refractory PTCL. As a result of this milestone achievement, we are obligated to pay TopoTarget \$25.0 million by November 2014 (*see Note 13(b)(ix)*). Since this event occurred after our balance sheet date of June 30, 2014, no provision or corresponding intangible asset has been recorded to our accompanying Condensed Consolidated Financial Statements.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Note Regarding Forward-Looking Statements**

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, without limitation, statements regarding our future product development activities and costs, the revenue potential (licensing, royalty and sales) of our products and product candidates, the success, safety and efficacy of our drug products, revenues, development timelines, product acquisitions, liquidity and capital resources and trends, and other statements containing forward-looking words, such as, believes, may, could, will, expects, intends, estimates, anticipates, plans, seeks, continues, or variation thereon or similar terminology (although not all forward-looking statements contain these words). Such forward-looking statements are based on the reasonable beliefs of our management as well as assumptions made by and information currently available to our management. Readers should not put undue reliance on these forward-looking statements. Forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified; therefore, our actual results may differ materially from those described in any forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in our periodic reports filed with the Securities and Exchange Commission, or the SEC, including our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, as well as those discussed elsewhere in this Quarterly Report on Form 10-Q, and the following factors:

our ability to successfully develop, obtain regulatory approval for and market our products;

our ability to continue to grow sales revenue of our marketed products;

risks associated with doing business internationally;

our ability to generate and maintain sufficient cash resources to fund our business;

our ability to enter into strategic alliances with partners for manufacturing, development and commercialization;

efforts of our development partners;

the ability of our manufacturing partners to meet our timelines;

the ability to timely deliver product supplies to our customers;

our ability to identify new product candidates and to successfully integrate those product candidates into our operations;

the timing and/or results of pending or future clinical trials, and our reliance on contract research organizations;

our ability to protect our intellectual property rights;

competition in the marketplace for our drugs;

delay in approval of our products or new indications for our products by the U.S. Food and Drug Administration, or the FDA;

actions by the FDA and other regulatory agencies, including international agencies;

securing positive reimbursement for our products;

the impact of any product liability, or other litigation to which we are, or may become a party;

the impact of legislative or regulatory reform of the healthcare industry and the impact of recently enacted healthcare reform legislation;

the availability and price of acceptable raw materials and components from third-party suppliers, and their ability to meet our demands;

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our ability, and that of our suppliers, development partners, and manufacturing partners, to comply with laws, regulations and standards, and the application and interpretation of those laws, regulations and standards, that govern or affect the pharmaceutical and biotechnology industries, the non-compliance with which may delay or prevent the development, manufacturing, regulatory approvals and sale of our products;

defending against claims relating to improper handling, storage or disposal of hazardous chemical, radioactive or biological materials which could be time consuming and expensive;

our ability to maintain the services of our key executives and technical and sales and marketing personnel;

the difficulty in predicting the timing or outcome of product development efforts and regulatory approvals; and

demand and market acceptance for our approved products.

All subsequent written and oral forward-looking statements attributable to us or by persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. We expressly disclaim any intent or obligation to update information contained in any forward-looking statement after the date thereof to conform such information to actual results or to changes in our opinions or expectations.

## **Company Overview**

We are a biotechnology company with fully integrated commercial and drug development operations with a primary focus in oncology and hematology. Our strategy is comprised of acquiring, developing, and commercializing a broad and diverse pipeline of late-stage clinical and commercial products.

We currently market five drugs:

FUSILEV® injection for patients in the U.S. with advanced metastatic colorectal cancer and to counteract certain side effects of methotrexate therapy;

ZEVALIN® injection for patients in the U.S. and various international markets with follicular non-Hodgkin's lymphoma;

FOLOTYN® injection for patients in the U.S. with relapsed or refractory PTCL;

MARQIBO® injection for patients in the U.S. with relapsed Philadelphia chromosome negative acute lymphoblastic leukemia; and

BELEODAQ injection for patients in the U.S. with relapsed or refractory PTCL. We did not launch this product until July 2014, and accordingly, no corresponding revenue is reported for any period presented in the accompanying Condensed Consolidated Financial Statements.

We also have ongoing indication expansion studies with several of our marketed products, and a diversified pipeline of product candidates in advanced-stage Phase 2 and Phase 3 studies. Our integrated in-house scientific team, includes formulation development and medical research, as well as expertise in regulatory and clinical affairs, biostatistics, and data management. In the U.S., we have full commercial operations for the sales and marketing of our drug products, and leverage the expertise of our worldwide partners to assist us with international sales and product development.

### **Business Strategy**

Our business strategy is comprised of the following three initiatives:

*Maximizing the revenue potential of our five currently-marketed drugs for the treatment of cancer.*

Our near-term outlook largely depends on sales and marketing successes for our five marketed drugs. It is this base business, along with potential additional indications for these drugs, that provides the working capital needed to operate our daily business and provides the necessary capital for opportunistic acquisitions.

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*Developing and commercializing the drugs for the treatment of cancer within our pipeline.*

Our strategy for our development portfolio is to focus on late-stage development drugs. We strive to complete clinical studies to demonstrate the safety and efficacy of these drugs in order to obtain regulatory approval in a timely manner. Upon obtaining approval, our sales and marketing function educates physicians on the safety of the drug and its effectiveness in treating patients for the approved indication, with the goal of achieving maximum commercial success.

*Expanding our pipeline of development-stage and commercial-stage drugs through business development activities.*

It is our goal to identify new strategic opportunities that are synergistic with our currently-marketed drugs. We will continue to (i) explore strategic collaborations as they relate to drugs that are either in clinical trials or are currently on the market, and (ii) identify and secure drugs that have significant growth potential through enhanced marketing and sales efforts and/or through pursuit of additional clinical development. We may also identify and pursue partnerships for out-licensing certain of our drugs in development.

See *Item 1.* of our Annual Report on Form 10-K for the year ended December 31, 2013, *Business* section for a discussion of:

*Cancer Background & Market Size*

*Product Portfolio*

*Manufacturing*

*Sales and Marketing*

*Customers*

*Competition*

*Research and Development*

**Recent Highlights in Our Business, Product Development Initiatives, and Regulatory Approvals**

During the first half of 2014, we accomplished various critical objectives for our business, which included:

**Commercial:** Product sales for the quarter surpassed \$40 million for the fourth consecutive quarter.

Medical: In July 2014, we received FDA approval of BELEODAQ for patients in the U.S. with relapsed or refractory PTCL. PTCL comprises of a group of rare and aggressive non-Hodgkin's Lymphomas (NHL) that develop from mature T-cells and accounts for approximately 10%-15% of all NHL cases in the U.S. These patients generally have poor prognosis with a low response rate (25%-27%) to available treatment options, and commonly experience repeated treatment failures until drug resistance or death. Accordingly, we believe this drug addresses an important unmet medical need for improved treatment options of PTCL patients.

In April 2014 we reported positive data from the pivotal study of C-E MELPHALAN, with an expected NDA filing by September 2014.

Our Phase 2 study for SPI-2012 is currently enrolling and we should be in position to make a Phase 3 decision by the end of the year.

### **CHARACTERISTICS OF OUR REVENUE AND EXPENSES**

See *Item 7* of our Annual Report on Form 10-K for the year ended December 31, 2013, *Characteristics of Our Revenue and Expenses* for a discussion of the nature of our revenue and operating expense line items within our accompanying Condensed Consolidated Statements of Operations.

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**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

See *Item 7* of our Annual Report on Form 10-K for the year ended December 31, 2013, *Critical Accounting Policies and Estimates* for a discussion of significant estimates and assumptions as part of the preparation of our accompanying condensed consolidated financial statements. These critical accounting policies and estimates arise in conjunction with the following accounts:

Revenue recognition

Inventories    lower of cost or market

Fair value of acquired assets and assumed liabilities

Goodwill and intangible assets    impairment evaluations

Income taxes

Stock-based compensation

Litigation accruals



**Table of Contents****RESULTS OF OPERATIONS****Operations Overview Three and six months ended June 30, 2014 and 2013**

	Three months ended June 30,				Six months ended June 30,			
	2014		2013		2014		2013	
Total revenues	\$ 46,855	100.0%	\$ 33,232	100.0%	\$ 86,979	100.0%	\$ 71,899	100.0%
Operating costs and expenses:								
Cost of product sales (excludes amortization and impairment of intangible assets)	6,156	13.1%	7,268	21.9%	12,434	14.3%	14,050	19.5%
Selling, general and administrative	25,399	54.2%	22,584	68.0%	48,802	56.1%	44,598	62.0%
Research and development	11,335	24.2%	10,460	31.5%	40,832	46.9%	22,343	31.1%
Amortization and impairment of intangible assets	5,361	11.4%	5,449	16.4%	10,721	12.3%	9,894	13.8%
Total operating costs and expenses	48,251	>100%	45,761	>100.0%	112,789	>100%	90,885	>100.0%
Loss from operations	(1,396)	(3.0)%	(12,529)	(37.7)%	(25,810)	(29.7)%	(18,986)	(26.4)%
Change in fair value of contingent consideration related to acquisitions	(1,005)	(2.1)%			(1,729)	(2.0)%		
Other expense, net	(2,463)	(5.3)%	(163)	(0.5)%	(4,888)	(5.6)%	(1,481)	(2.1)%
Loss before income taxes	(4,864)	(10.4)%	(12,692)	(38.2)%	(32,427)	(37.3)%	(20,467)	(28.5)%
Benefit for income taxes	1,301	2.8%	2,971	8.9%	1,223	1.4%	5,310	7.4%
Net loss	\$ (3,563)	(7.6)%	\$ (9,721)	(29.3)%	\$ (31,204)	(35.9)%	\$ (15,157)	(21.1)%

**THREE MONTHS ENDED JUNE 30, 2014 VERSUS 2013****Total Revenues**

	Three months ended June 30,			
	2014	2013	\$ Change	% Change
	(\$ in millions)			
Product sales, net:				
FUSILEV	\$ 26.6	\$ 12.9	\$ 13.7	>100.0%
FOLOTYN	12.6	12.5	0.1	0.8%
ZEVALIN	6.3	6.8	(0.5)	(7.4)%
MARQIBO	1.4		1.4	>100.0%
	\$ 46.9	\$ 32.2	\$ 14.7	45.7%
License fees and service revenue		1.0	(1.0)	>(100.0)%
Total revenues	\$ 46.9	\$ 33.2	\$ 13.7	41.3%

**Product sales, net.** Gross product sales are reduced by estimated provisions for product returns, sales discounts and rebates, distribution and data fees, and estimates for chargebacks established as of each period to arrive at presented product sales, net .

FUSILEV revenue increase is primarily due to (i) an increase in our average net price per unit as a result of certain non-recurring GTN adjustments in the current period, and (ii) an increase in unit sales to our wholesalers to satisfy end-user demand.

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FOLOTYN revenue remained consistent with the prior year period, with unit sales and average net sales price per unit largely unchanged. In the second quarter of 2014, we modified our FOLOTYN distribution model. This resulted in a \$1.0 million additional purchase of this product by our wholesalers in order to fulfill anticipated end-user demand, and is not expected to recur at this level in the second half of 2014.

ZEVALLIN revenue decrease is due to depressed unit demand for U.S. sales, partially offset by a U.S. and Ex-U.S. increase in our average net sales price per unit between these periods. Beginning in the second quarter of 2013, we terminated our ZEVALLIN services agreement with Bayer, and transitioned to a sales distribution model in Europe. This transition has had a favorable impact on unit sales in Europe, though we realize a much lower average price per unit for these sales, as compared both to our U.S. sales and former Bayer sales.

MARQIBO revenue derived in 2014 is a result of our acquisition of Talon in July 2013, as discussed in *Note 9(a)*.

**License fees and service revenue.** In the second quarter of 2013, we recognized \$1.0 million from the amortization of deferred revenue that corresponded with our contracted research and development services. This revenue is associated with an aggregate of \$16.0 million upfront payment we received from Nippon Kayaku in 2010, as discussed in *Note 13(b)(viii)*. As of December 31, 2013, these upfront payments have been recognized through license fees and service revenue in full, and as a result, did not recur in the second quarter of 2014.

**Operating Costs and Expenses & Total Other Expenses**

	<b>Three months ended June 30,</b>			
	<b>2014</b>	<b>2013</b>	<b>\$ Change</b>	<b>% Change</b>
	(\$ in millions)			
<b>Operating costs and expenses:</b>				
Cost of product sales (excludes amortization and impairment of intangible assets)	\$ 6.2	\$ 7.3	\$ (1.1)	(15.1)%
Selling, general and administrative	25.4	22.6	2.8	12.4%
Research and development	11.3	10.5	0.8	7.6%
Amortization and impairment of intangible assets	5.4	5.4		%
<b>Total operating costs and expenses</b>	<b>\$ 48.3</b>	<b>\$ 45.8</b>	<b>\$ 2.5</b>	<b>5.5%</b>
<b>Total other expenses</b>	<b>\$ (3.5)</b>	<b>\$ (0.2)</b>	<b>\$ (3.3)</b>	<b>&gt;(100.0)%</b>

**Cost of Product Sales.** Despite our large increase in product sales, net, in the second quarter of 2014 as compared to 2013, our cost of product sales decreased 15%. This is primarily due to (i) a higher realized net price, (ii) our product sales mix in the current period, and (iii) certain royalty adjustments for in-license contract amendments.

**Selling, General and Administrative.** Selling, general and administrative expenses increased primarily due to:

- (i) \$0.9 million increase in expense for intellectual property matters and various legal services;

(ii) \$0.7 million increase in travel-related expenses to support our sales growth;

(iii) \$0.6 million increase in marketing expenses to support our sales growth;

(iv) \$0.9 million increase in personnel and infrastructure expenses as we continue to build our sales team and enhance supporting administrative functions.

This increase is partially offset by the non-recurrence of \$0.7 million of Talon acquisition expenses, incurred in the second quarter of 2013.

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**Research and Development.** Research and development expense increase is primarily due to a reduction of our liability and corresponding expenses as a result of the amendment to our agreement with Mundipharma (see *Note 12*), which did not recur in 2014.

**Amortization and Impairment of Intangible Assets.** The amortization and impairment of intangible assets remained consistent with the prior year period.

**Total Other Expenses.** Total other expenses increased by \$3.3 million and was primarily due to (i) \$1.6 million increase in interest expense attributable to our convertible senior notes issued in December 2013; (ii) \$1.0 million increase to our acquisition-related contingent obligations liability to the former shareholders of Talon and Ligand, which resulted in an equal charge to our change in fair value of contingent consideration related to acquisitions; and (iii) an unrealized \$0.7 million loss in the current period for intercompany obligations denominated in foreign currency.

	Three months ended June 30,			
	2014	2013	\$ Change	% Change
	(\$ in millions)			
Benefit for income taxes	\$ 1.3	\$ 3.0	\$ (1.7)	(56.7)%

**Benefit for Income Taxes.** Our current period benefit for income taxes primarily represents the amount that we expect to be refunded from taxing authorities (for income taxes we paid for fiscal year 2012) upon the filing our 2014 U.S. income tax return based on our operating results in the first half of 2014 and our projected full-year operating results.

**SIX MONTHS ENDED JUNE 30, 2014 VERSUS 2013****Total Revenues**

	Six months ended June 30,			
	2014	2013	\$ Change	% Change
	(\$ in millions)			
Product sales, net:				
FUSILEV	\$ 48.7	\$ 24.7	\$ 24.0	97.2%
FOLOTYN	22.7	22.5	0.2	0.9%
ZEVALIN	12.7	14.4	(1.7)	(11.8)%
MARQIBO	2.9		2.9	>100.0%
	\$ 87.0	\$ 61.6	\$ 25.4	41.2%
License fees and service revenue		10.3	(10.3)	>(100.0)%
Total revenues	\$ 87.0	\$ 71.9	\$ 15.1	21.0%

**Product sales, net.** Gross product sales are reduced by estimated provisions for product returns, sales discounts and rebates, distribution and data fees, and estimates for chargebacks established as of each period to arrive at presented product sales, net.

FUSILEV revenue increase is primarily due to (i) an increase in our average net price per unit as a result of certain non-recurring GTN adjustments in the current period, and (ii) an increase in unit sales to our wholesalers to satisfy end-user demand.

FOLOTYN revenue remained consistent with the prior year period. Unit sales and average net sales price per unit were largely unchanged. In the first half of 2014, we modified our FOLOTYN distribution model. This resulted in a \$1.0 million additional purchase of this product by our wholesalers in order to fulfill anticipated end-user demand, and is not expected to recur at this level in the second half of 2014.

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ZEVALIN revenue decrease is due to depressed unit demand for U.S. sales, partially offset by an U.S. and Ex-U.S. increase in our average net sales price per unit between these periods. Beginning in the second quarter of 2013, we terminated our ZEVALIN services agreement with Bayer, and transitioned to a sales distribution model in Europe. This transition has had a favorable impact on unit sales in Europe, though we realize a much lower average price per unit for these sales, as compared both to our U.S. sales and former Bayer sales.

MARQIBO revenue derived in 2014 is a result of our acquisition of Talon in July 2013, as discussed in *Note 9(a)*.

**License fees and service revenue.** In the first six months of 2013, we recognized \$10.3 million from the amortization of deferred revenue that corresponded with our contracted research and development services. This revenue is associated with a \$41.5 million upfront payment we received from Allergan in 2008, and an aggregate of \$16.0 million upfront payment we received from Nippon Kayaku in 2010. As of December 31, 2013, these upfront payments have been recognized through license fees and service revenue in full, and as a result, did not recur in the first quarter of 2014. In the current period, we recognized \$28,000 from our out-license royalties, all derived from FOLOTYN sales in Mundipharma's (our co-development partner - see *Note 12*) territories.

**Operating Costs and Expenses & Total Other Expense**

	Six months ended June 30,			
	2014	2013	\$ Change	% Change
	(\$ in millions)			
Operating costs and expenses:				
Cost of product sales (excludes amortization and impairment of intangible assets)	\$ 12.4	\$ 14.0	\$ (1.6)	(11.4)%
Selling, general and administrative	48.8	44.6	4.2	9.4%
Research and development	40.8	22.3	18.5	83.0%
Amortization and impairment of intangible assets	10.7	9.9	0.8	8.1%
Total operating costs and expenses	\$ 112.8	\$ 90.8	\$ 22.0	24.2%
Total other expense	\$ (6.6)	\$ (1.5)	\$ (5.1)	>(100.0)%

**Cost of Product Sales.** Despite our large increase in product sales, net, in the first six months of 2014 as compared to 2013, our cost of product sales decreased 11%. This result was primarily driven by (i) a higher realized net price, (ii) an unusually large excess inventory charge for FUSILEV in the first half of 2013 that did not recur in the current period, and (iii) certain royalty adjustments for in-license contract amendments.

**Selling, General and Administrative.** Selling, general and administrative expenses increased primarily due to

- (i) \$0.8 million increase in personnel-related expenses as we continue to build our sales and marketing team;
- (ii) \$1.2 million increase in marketing expenses to support our sales growth;

(iii) \$0.6 million increase in expense for intellectual property matters and various legal services;

(iv) \$0.8 million increase in travel related expenses to support our sales growth; and

(v) \$0.7 million related to enhancements to our administrative capabilities and functions.

The increase in these expenses is partially offset by the non-recurrence of \$0.7 million of Talon acquisition expenses, incurred in the first half of 2013.

**Research and Development.** Research and development expense increase is primarily due to an aggregate \$17.8 million from cash payment and stock issuance to TopoTarget, upon the February 2014 contractual milestone achievement represented by the acceptance by the FDA of our new drug application (NDA) for the PTCL indication of BELEODAQ.



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**Amortization and Impairment of Intangible Assets.** The amortization and impairment of intangible assets increased \$0.8 million during the six months ended June 30, 2014, primarily due to the amortization of definite-lived intangible assets from the acquisition of Talon in July 2013 (through which we acquired MARQIBO distribution rights).

**Total Other Expenses.** Total other expenses increased by \$5.1 million and was primarily due to (i) \$3.2 million increase in interest expense attributable to our convertible senior notes issued in December 2013, and (ii) a \$1.7 million increase to our acquisition-related contingent obligations liability to the former shareholders of Talon and Ligand in the current period, which resulted in an equal charge to our change in fair value of contingent consideration related to acquisitions; and (iii) a \$0.2 million unrealized loss for intercompany obligations denominated in foreign currency.

	Six months ended June 30,		\$ Change	% Change
	2014	2013		
	(\$ in millions)			
Benefit for income taxes	\$ 1.2	\$ 5.3	\$ (4.1)	(77.4)%

**Benefit for Income Taxes.** Our current period benefit of \$1.2 million for income taxes primarily represents the amount that we expect to be refunded from taxing authorities (for income taxes we paid for fiscal year 2012) upon the filing our 2014 U.S. income tax return based on our operating results in the first half of 2014 and our projected full-year operating results. This amount is partially offset by \$1.2 million related to the correction of our prior year estimate of carryback of federal net operating losses and of credits ineligible for offset against federal income taxes.

**LIQUIDITY AND CAPITAL RESOURCES**

	June 30, 2014	December 31, 2013	June 30, 2013
	(in thousands, except financial metrics data)		
Cash and cash equivalents	\$ 132,405	\$ 156,306	\$ 121,103
Marketable securities	\$ 3,306	\$ 3,471	\$ 3,312
Accounts receivable, net	\$ 56,742	\$ 48,880	\$ 52,379
Total current assets	\$ 220,133	\$ 235,190	\$ 212,282
Total current liabilities	\$ 77,479	\$ 89,984	\$ 102,295
Working capital surplus (a)	\$ 142,654	\$ 145,206	\$ 109,987
Days sales outstanding ( DSO ) (b)	110	110	143
Current ratio (c)	2.9	2.6	2.1

(a) Total current assets at period end *minus* total current liabilities at period end.

(b) Net accounts receivable at period end *divided by* revenue, net for the second quarter *multiplied by* the number of days in the quarter.

(c) Total current assets at period end *divided by* total current liabilities at period end.

**Net Cash (Used In) Provided by Operating Activities**

Cash used in operating activities was \$24.3 million for the six months ended June 30, 2014, as compared to cash provided by operating activities of \$3.4 million in the prior year period. The decrease in cash provided by operating activities during the current year, as compared to the prior year is primarily a function of the working capital drivers of (i) decreased customer collections (see below), (ii) increased payments to our vendors to reduce trade payables between these periods (see below), and (iii) a \$10.0 payment for product milestone achievement (*see Note 13(b)(ix)*).

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For the six months ended June 30, 2014 and 2013, our cash collections from customers totaled \$113.7 million and \$123.0 million, respectively, representing 130.7% and 171.1% of reported net revenue for the same years. This decrease in customer collections is due to our accounts receivable, net, balances as of December 31, 2013 and 2012 of \$49.5 million and \$92.2 million, respectively, and corresponded with our decrease in product sales in 2013 as compared to 2012.

For the six months ended June 30, 2014 and 2013, cash payments to our employees and vendors for products, services, and rebates totaled \$135.0 million and \$163.5 million, respectively.

**Net Cash Used in Investing Activities**

Net cash used in investing activities of \$0.4 million in the first six months of 2014 was due to purchases of computer software and hardware to support our general business growth.

**Net Cash (Used In) Provided By Financing Activities**

Net cash (used in) provided by financing activities of \$1.1 million for the first six months ended June 30, 2014 relates to (i) \$1.3 million of proceeds from the issuance of common stock as a result of the exercise of employee stock options, and (ii) \$ 0.3 million of proceeds from employee stock purchases under our employee stock purchase plan. These proceeds were partially offset by our \$0.6 million purchase and retirement at vesting of restricted stock at our employees' election, so that corresponding minimum employee tax obligations could be met.

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### **Convertible Senior Notes Due 2018**

On December 17, 2013, we entered into an agreement for the sale of \$120.0 million aggregate principal amount of 2.75% Convertible Senior Notes due December 2018 (the 2018 Convertible Notes). The 2018 Convertible Notes are convertible into shares of our common stock at a conversion rate of 95 shares per \$1,000 principal amount of the 2018 Convertible Notes, totaling 11.4 million common shares if fully converted. The in-the-money conversion price is equivalent to \$10.53 per common share. The conversion rate and conversion price are subject to adjustment under certain limited circumstances. Initially, we may only settle conversions of the 2018 Convertible Notes by delivering shares of our common stock. However, if we obtain stockholder approval in accordance with applicable NASDAQ rules, we may then settle conversions of the 2018 Convertible Notes by paying or delivering, as the case may be, cash, shares of our common stock, or a combination of cash and shares, at our election.

The 2018 Convertible Notes bear interest at a rate of 2.75% per year, payable semiannually in arrears on June 15 and December 15 of each year, beginning on June 15, 2014. The 2018 Convertible Notes will mature and become payable on December 15, 2018, subject to earlier conversion into common stock at the holders' option.

The sale of the 2018 Convertible Notes closed on December 23, 2013 and our net proceeds were \$115.4 million, after deducting banker and professional fees of \$4.6 million. We used a portion of these proceeds to simultaneously enter into bought call and sold warrant transactions with Royal Bank of Canada (collectively, the Note Hedge). We recorded the Note Hedge on a net cost basis of \$13.1 million, as a reduction to additional paid-in capital in our accompanying Condensed Consolidated Balance Sheets. Under applicable GAAP, the Note Hedge transaction is not expected to be marked-to-market through earnings or comprehensive income in future reporting periods.

### **Retired Credit Facility**

On September 5, 2012, we entered into a credit agreement with Bank of America, N.A., as the administrative agent and an initial lender and Wells Fargo Bank, National Association, as an initial lender (the Credit Agreement). The Credit Agreement provided us with a committed \$50.0 million revolving line of credit facility (the Credit Facility). The Credit Facility was to expire on September 5, 2014, but was repaid in full and cancelled by us on December 20, 2013.

### **Future Capital Requirements**

We believe that the future growth of our business will depend on our ability to successfully develop and acquire new drugs for the treatment of cancer and successfully bring these drugs to market.

The timing and amount of our future capital requirements will depend on many factors, including:

the need for additional capital to fund future development programs;

the need for additional capital to fund strategic acquisitions;

the need for additional capital to fund licensing arrangements;

our requirement for additional information technology infrastructure and systems; and

adverse outcomes from potential litigation and the cost to defend such litigation.

We believe that our \$135.7 million in aggregate cash and equivalents, and marketable securities as of June 30, 2014, will allow us to fund our current and planned operations for at least the next twelve months. We may seek to obtain additional capital through the sale of debt or equity securities, if necessary, especially in conjunction with opportunistic acquisitions or licensing arrangements.

We may be unable to obtain such additional capital when needed, or on terms favorable to us or our stockholders, if at all. If we raise additional funds by issuing equity securities, the percentage ownership of our stockholders will be reduced, stockholders may experience additional dilution or such equity securities may provide for rights, preferences or privileges senior to those of the holders of our common stock. If additional funds are raised through the issuance of debt securities, the terms of such securities may place restrictions on our ability to operate our business.

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

We have no off-balance sheet arrangements (except for operating leases) that provide financing, liquidity, market or credit risk support, or involve derivatives. In addition, we have no arrangements that may expose us to liability that are not expressly reflected in the accompanying Condensed Consolidated Financial Statements and/or notes thereto.

As of June 30, 2014, we did not have any relationships with unconsolidated entities or financial partnerships, often referred to as structured finance or special purpose entities, established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. As such, we are not subject to any material financing, liquidity, market or credit risk that could arise if we had engaged in such relationships.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

In the normal course of business, our operations are exposed to risks associated with fluctuations in interest rates and foreign currency exchange rates.

The primary objective of our investment activities is to preserve principal, while at the same time maximizing yields without significantly increasing risk. We do not utilize hedging contracts or similar instruments. Because of our ability to generally redeem these investments at par at short notice and without penalty, changes in interest rates would have an immaterial effect on the fair value of these investments. If a 10% change in interest rates were to have occurred on June 30, 2014, any decline in the fair value of our investments would not be material in the context of our accompanying Condensed Consolidated Financial Statements. In addition, we are exposed to certain market risks associated with credit ratings of corporations whose corporate bonds we may purchase from time to time. If these companies were to experience a significant detrimental change in their credit ratings, the fair market value of such corporate bonds may significantly decrease. If these companies were to default on these corporate bonds, we may lose part, or all, of our principal. We believe that we effectively manage this market risk by diversifying our investments, and investing in highly rated securities.

We are exposed to foreign currency exchange rate fluctuations relating to payments we make to vendors, suppliers and license partners using foreign currencies. In particular, some of our obligations are incurred in Euros. We mitigate such risk by maintaining a limited portion of our cash in Euros and other currencies.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### ***Evaluation of Disclosure Controls and Procedures***

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2014. The term disclosure controls and procedures, as defined in *Rules 13a-15(e) and 15d-15(e)* under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure.

Based on the evaluation of our disclosure controls and procedures as of June 30, 2014, our chief executive officer and chief financial officer concluded that, as of that date, our disclosure controls and procedures were not effective because of the identification of the material weakness discussed below.

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***Changes in Internal Control Over Financial Reporting***

As of December 31, 2013, our management concluded that our internal control over financial reporting was not effective, as evaluated under the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework (1992 framework). As part of this conclusion, our management determined that we had ineffective design and operating effectiveness of our internal control over financial reporting. This material weakness conclusion specifically pertained to the accurate and timely reporting of our operating expense accruals which comprised (i) the ineffective design and operation of controls over our process of estimating the required period-end accruals for services performed under open purchase orders, which resulted in overstated operating expenses and accrued liabilities in multiple reporting periods in, and prior to, 2013; and (ii) ineffective design and operation of controls over our identification and recording of liabilities for vendor invoices received subsequent to year-end that related to our 2013 activities. The remediation of these matters will not be completed and concluded upon until management's next annual assessment as of December 31, 2014, thus this material weakness remained as of June 30, 2014.

A material weakness is a deficiency, or a combination of deficiencies, in internal controls over financial reporting, such that there is a reasonable possibility that a material misstatement of a company's annual or interim consolidated financial statements will not be prevented or detected on a timely basis.

Notwithstanding our continued material weakness, we have concluded that the financial statements and other financial information included in this Quarterly Report on Form 10-Q fairly present in all material respects our financial condition, results of operations and cash flows as of, and for, the periods presented.

Except as disclosed below, no change in our internal control over financial reporting occurred during the fiscal quarter ended June 30, 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

***Remediation Steps to Address Material Weakness***

We have developed, and are currently implementing, a remediation plan for this material weakness. We will continue to execute our previously communicated remediation plan, which includes hiring additional experienced accounting personnel and expanding training for our accounting personnel, as well as modifying and expanding our internal controls over our recording of complete and accurate period-end accruals. The successful remediation of this material weakness will require review and evidence of the effectiveness of the related internal controls as part of our next annual assessment of our internal controls over financial reporting as of December 31, 2014. As we continue these remediation efforts, we may determine that additional measures should be taken to address these or other control deficiencies, and/or that we should modify the remediation plan described above.

***Limitations of the Effectiveness of Internal Controls***

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the internal control system are met. Because of inherent limitations in any control systems, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected. We are continuously seeking to improve the efficiency and effectiveness of our operations and of our internal controls.

**PART II OTHER INFORMATION**



**ITEM 1. LEGAL PROCEEDINGS**

We are involved with various legal matters arising in the ordinary course of business. We make provisions for liabilities when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Such provisions are reviewed at least quarterly and adjusted to reflect the impact of any settlement negotiations, judicial and administrative rulings, advice of legal counsel, and other information and events pertaining to a particular case. Litigation is inherently unpredictable. Although the ultimate resolution of these various matters cannot be determined at this time, we do not believe that such matters, individually or in the aggregate, will have a material adverse effect on our condensed consolidated results of operations, cash flows or financial condition.

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Certain of the legal proceedings in which we are involved are discussed in *Note 13, Commitments and Contingencies*, to our accompanying Condensed Consolidated Financial Statements, and are hereby incorporated by reference.

**ITEM 1A. RISK FACTORS**

As of the date of this filing, there have been no material changes to the RISK FACTORS included in our Annual Report on Form 10-K for the year ended December 31, 2013, filed with the Securities and Exchange Commission on March 12, 2014.

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<b>Exhibit Number</b>	<b>Description</b>
10.1+	Lease Agreement, dated April 7, 2014, by and between Spectrum Pharmaceuticals, Inc. and 11500 South Eastern Avenue, LLC.
10.2+	First Amendment to Executive Employment Agreement, dated as of April 17, 2014, by and between Spectrum Pharmaceuticals, Inc. and Dr. Rajesh C. Shrotriya.
10.3	First Amendment to License Agreement, dated as of June 20, 2014, by and between Spectrum Pharmaceuticals, Inc. and Merck Eprova AG. (Filed as Exhibit 99.1 to Form 8-K, as filed with the Securities and Exchange Commission on June 26, 2014, and incorporated herein by reference.)
31.1+	Certification of Principal Executive Officer, pursuant to Rule 13a-14(a)/15d-14(a) promulgated under the Securities Exchange Act of 1934.
31.2+	Certification of Principal Financial Officer, pursuant to Rule 13a-14(a)/15d-14(a) promulgated under the Securities Exchange Act of 1934.
32.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14(b)/15d-14(b) promulgated under the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350.
32.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14(b)/15d-14(b) promulgated under the Securities Exchange Act of 1934 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.

+ Filed herewith.

\* Furnished herewith.

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**SIGNATURES**

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

SPECTRUM PHARMACEUTICALS, INC.

Date: August 8, 2014

By: /s/ Kurt A. Gustafson  
Kurt A. Gustafson  
Executive Vice President and Chief Financial  
Officer  
(Authorized Signatory and Principal Financial and  
Accounting Officer)