DEPOMED INC
Form 10-Q
May 10, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED March 31, 2018

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER 001-13111

DEPOMED, INC.

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

CALIFORNIA	94-3229046
(STATE OR OTHER JURISDICTION OF INCORPORATION OR ORGANIZATION)	(I.R.S. EMPLOYER IDENTIFICATION NUMBER)

7999 Gateway Boulevard, Suite 300

Newark, California 94560

(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES, INCLUDING ZIP CODE)

(510) 744-8000

(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 Exchange Act during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

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

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

The number of issued and outstanding shares of the Registrant's Common Stock, no par value, as of May 4, 2018 was 63,587,401.

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DEPOMED, INC

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PART I — FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

DEPOMED, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

(Unaudited)

	March 31, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 101,693	$ 126,884
Short-term investments	—	1,205
Accounts receivable, net	62,428	72,482
Inventories	5,368	13,042
Prepaid and other current assets	23,815	17,238
Total current assets	193,304	230,851
Property and equipment, net	11,658	13,024
Intangible assets, net	768,429	793,873
Other long-term assets	28,680	869
Total assets	$ 1,002,071	$ 1,038,617
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 10,203	$ 14,732
Accrued rebates, returns and discounts	93,099	135,828
Accrued liabilities	32,609	60,496
Income taxes payable	126	126
Current portion of Senior Notes	107,500	82,500
Contingent consideration liability, current portion	—	156
Interest payable	11,164	13,220
Other current liabilities	2,427	3,522
Total current liabilities	257,128	310,580
Contingent consideration liability, long-term portion	1,249	1,457
Senior Notes	250,727	274,720
Convertible Notes	273,920	269,510
Other long-term liabilities	12,957	12,842

Commitments and contingencies		
Shareholders’ equity:		
Common stock	316,727	313,857
Additional paid-in capital	75,050	75,164
Accumulated deficit	(185,684)	(219,508)
Accumulated other comprehensive loss, net of tax	(3)	(5)
Total shareholders’ equity	206,090	169,508
Total liabilities and shareholders' equity	$ 1,002,071	$ 1,038,617

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

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DEPOMED, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except share and per share amounts)

(Unaudited)

	Three Months Ended March 31,	
	2018	2017
Revenues:		
Product sales, net	$ 44,354	$ 90,285
Commercialization agreement	83,800	—
Royalties	250	162
Total revenues	128,404	90,447
Costs and expenses:		
Cost of sales (excluding amortization of intangible assets)	12,044	17,774
Research and development expenses	1,528	5,084
Selling, general and administrative expenses	29,033	48,519
Amortization of intangible assets	25,444	25,735
Restructuring charges	9,017	—
Total costs and expenses	77,066	97,112
Income (loss) from operations	51,338	(6,665)
Other income (expense):		
Interest and other income	229	250
Interest expense	(18,068)	(20,124)
Total other expense	(17,839)	(19,874)
Net income (loss) before income taxes	33,499	(26,539)
Benefit from (provision for) income taxes	325	(202)
Net income (loss)	$ 33,824	$ (26,741)
Basic net income (loss) per share	$ 0.53	$ (0.43)
Diluted net income (loss) per share	$ 0.48	$ (0.43)
Shares used in computing basic net income (loss) per share	63,502,566	62,128,862
Shares used in computing diluted net income (loss) per share	81,877,097	62,128,862

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

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DEPOMED, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(in thousands)

(Unaudited)

	Three Months Ended March 31,	
	2018	2017
Net income (loss)	$ 33,824	$ (26,741)
Unrealized gain on available-for-sale securities, net of tax	2	15
Comprehensive income (loss)	$ 33,826	$ (26,726)

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

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DEPOMED, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(Unaudited)

	Three Months Ended March 31,	
	2018	2017
Operating Activities		
Net income (loss)	$ 33,824	$ (26,741)
Adjustments for non-cash items:		
Depreciation and amortization	26,918	26,349
Accretion of debt discount and debt issuance costs	5,418	4,650
Provision for inventory obsolescence	218	201
Gain on disposal of property and equipment	(134)	(50)
Stock-based compensation	2,234	3,556
Change in fair value of contingent consideration	(201)	(5,301)
Other	34	192
Changes in assets and liabilities:		
Accounts receivable	10,055	34,775
Inventories	7,457	873
Prepaid and other assets	(34,497)	703
Accounts payable and other accrued liabilities	(33,515)	(17,833)
Accrued rebates, returns and discounts	(42,730)	(2,970)
Interest payable	(2,055)	(2,440)
Income taxes payable	(1)	42
Net cash (used in) provided by operating activities	(26,975)	16,006
Investing Activities		
Purchases of property and equipment	(1)	(470)
Proceeds from disposal of property and equipment	145	50
Proceeds from sale of other assets	80	—
Maturities of marketable securities	1,200	52,831
Net cash provided by investing activities	1,424	52,411
Financing Activities		
Payment of contingent consideration liability	(162)	(913)
Proceeds from issuance of common stock	636	2,597
Shares withheld for payment of employee's withholding tax liability	(114)	—
Net cash provided in financing activities	360	1,684
Net (decrease) increase in cash and cash equivalents	(25,191)	70,101

Cash and cash equivalents at beginning of year	126,884	117,709
Cash and cash equivalents at end of period	$ 101,693	$ 187,810
Supplemental Disclosure of Cash Flow Information		
Net cash paid for income taxes	$ 1	$ —
Cash paid for interest	$ 14,653	$ 17,362
Capital expenditures incurred but not yet paid	$ 119	$ 123

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

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DEPOMED, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

Depomed (Depomed or the Company) is a specialty pharmaceutical company focused on pain and other central nervous system (CNS) conditions. The Company's current specialty pharmaceutical business includes the following three products which we market in the United States (U.S.):

- Gralise® (gabapentin), a once daily product for the management of postherpetic neuralgia (PHN), was launched in October 2011.

- CAMBIA® (diclofenac potassium for oral solution), a non-steroidal anti-inflammatory drug for the acute treatment of migraine attacks, was acquired in December 2013.

- Zipsor® (diclofenac potassium) liquid filled capsules, a non-steroidal anti-inflammatory drug for the treatment of mild to moderate acute pain, was acquired in June 2012.

In January 2018, pursuant to the terms of a Commercialization Agreement the Company entered into with Collegium Pharmaceutical, Inc. (Collegium) in December 2017, the Company granted Collegium the right to commercialize the NUCYNTA franchise of pain products in the U.S. Pursuant to the Commercialization Agreement, Collegium assumed all commercialization responsibilities for the NUCYNTA franchise effective January 9, 2018, including sales and marketing. The Company will receive a royalty on all NUCYNTA revenues based on certain net sales thresholds, with a minimum royalty of $132.0 million for the year ended December 31, 2018 and $135.0 million per year for the years ended December 31, 2019 to December 31, 2021, subject to certain conditions. Both the Company and Collegium may terminate the agreement under certain circumstances. The Company may terminate the agreement if aggregate net sales of the NUCYNTA products fall below certain thresholds or within the first year upon the payment of an $80.0 million termination fee. Collegium may terminate at any time after the first anniversary of the transaction

by giving 12 months' notice and, if the termination date is prior to the fourth anniversary of the transaction, by paying us a $25.0 million termination fee. The NUCYNTA franchise includes two products currently marketed in the U.S. by Collegium:

•NUCYNTA® ER (tapentadol extended release tablets), a product for the management of pain severe enough to require daily, around the clock, long term opioid treatment, including neuropathic pain associated with diabetic peripheral neuropathy (DPN) in adults, and for which alternate treatment options are inadequate; and

•NUCYNTA® IR (NUCYNTA) (tapentadol), an immediate release version of tapentadol for the management of moderate to severe acute pain in adults.

In November 2017, we entered into definitive agreements with Slán Medicinal Holdings Limited (Slán) pursuant to which the Company acquired Slán's rights to market the specialty drug cosyntropin (Synthetic ACTH Depot) in the U.S., and Slán acquired the Company's rights to Lazanda® (fentanyl) nasal spray. The Company believes cosyntropin can be second-to-market behind Mallinckrodt plc's marketed product, H-P Acthar gel. The Company expects Slán to file an NDA for cosyntropin in late 2018.

The Company actively seeks to expand our product portfolio through acquiring or in licensing commercially available products or late stage product candidates that may be marketed and sold effectively with our existing products through our sales and marketing capabilities.

The Company also has royalty and milestone producing license arrangements based on our proprietary Acuform® gastroretentive drug delivery technology, including with Ironwood Pharmaceuticals, Inc. (Ironwood).

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Basis of Presentation

The unaudited condensed consolidated financial statements and the related footnote information of the Company have been prepared pursuant to the requirements of the Securities and Exchange Commission (SEC) for interim reporting. As permitted under those rules and regulations, certain footnotes or other financial information that are normally required by U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to such rules and regulations. In the opinion of the Company's management, the accompanying interim unaudited condensed consolidated financial statements include all adjustments necessary for a fair presentation of the information for the periods presented. The results for the three months ended March 31, 2018 are not necessarily indicative of results to be expected for the entire year ending December 31, 2018 or future operating periods.

The accompanying unaudited condensed consolidated financial statements and related financial information should be read in conjunction with the audited financial statements and the related notes thereto for the year ended December 31, 2017 included in the Company's Annual Report on Form 10-K filed with the SEC (the 2017 Form 10-K). The balance sheet as of December 31, 2017 has been derived from the audited financial statements at that date, as filed in the Company's 2017 Form 10-K.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Depomed Bermuda Ltd (Depo Bermuda), Depo NF Sub, LLC (Depo NF Sub) and Depo DR Sub, LLC (Depo DR Sub). All intercompany accounts and transactions have been eliminated on consolidation.

On November 17, 2015, the Company entered into a definitive agreement to acquire the U.S. and Canadian rights to cebranopadol and its related follow-on compound from Grünenthal GmbH (Grünenthal). The acquisition of these rights closed on December 30, 2015 at which point the Company assigned its rights under the agreement to Depo Bermuda, a Company which was formed in Bermuda on December 22, 2015.

Depo NF Sub was formed on March 26, 2015, in connection with a Note Purchase Agreement dated March 12, 2015, governing the Company's issuance of $575.0 million aggregate principal amount of Senior Notes on April 2, 2015, for aggregate gross proceeds of approximately $562.0 million. On April 2, 2015, the Company and Depo NF Sub entered into a Pledge and Security Agreement with the Collateral Agent pursuant to which the Company and Depo NF Sub each granted the Collateral Agent (on behalf of the Purchasers) a security interest in substantially all of their assets, other than specifically excluded assets.

Depo DR Sub was formed in October 2013 for the sole purpose of facilitating the PDL BioPharma, Inc. (PDL) Transaction. The Company contributed to Depo DR Sub all of its rights, title and interests in each of the license agreements to receive royalty and contingent milestone payments. Immediately following the transaction, Depo DR Sub sold to PDL, among other things, such rights to receive royalty and contingent milestone payments, for an upfront cash purchase price of $240.5 million.

The Company and Depo DR Sub continue to retain certain administrative duties and obligations under the specified license agreements. These include the collection of the royalty and milestone amounts due and enforcement of related provisions under the specified license agreements, among others. In addition, the Company and Depo DR Sub must prepare a quarterly distribution report relating to the specified license agreements, containing, among other items, the amount of royalty payments received by the Company, reimbursable expenses and set offs. The Company and Depo DR Sub must also provide PDL with notice of certain communications, events or actions with respect to the specified license agreements and infringement of any underlying intellectual property.

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Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Estimates are used when accounting for amounts recorded in connection with acquisitions, including initial fair value determinations of assets and liabilities as well as subsequent fair value measurements. Additionally, estimates are used in determining items such as sales discounts and returns, depreciable and amortizable lives, share-based compensation assumptions and taxes on income. Although management believes these estimates are based upon reasonable assumptions within the bounds of its knowledge of the Company's business and operations, actual results could differ materially from these estimates.

Acquisitions

The Company accounts for acquired businesses using the acquisition method of accounting, which requires that assets acquired and liabilities assumed be recorded at date of acquisition at their respective fair values. The fair value of the consideration paid, including contingent consideration, is assigned to the underlying net assets of the acquired business based on their respective fair values. Any excess or shortfall of the purchase price over the estimated fair values of the net assets acquired is recorded as goodwill or bargain purchase, as applicable.

Significant judgments are used in determining the estimated fair values assigned to the assets acquired and liabilities assumed and in determining estimates of useful lives of long-lived assets. Fair value determinations and useful life estimates are based on, among other factors, estimates of expected future net cash flows, estimates of appropriate discount rates used to present value expected future net cash flows, the assessment of each asset's life cycle, and the impact of competitive trends on each asset's life cycle and other factors. These judgments can materially impact the estimates used to allocate acquisition date fair values to assets acquired and liabilities assumed and the resulting timing and amounts charged to, or recognized in current and future operating results. For these and other reasons, actual results may vary significantly from estimated results.

Any changes in the fair value of contingent consideration resulting from a change in the underlying inputs is recognized in operating expenses until the contingent consideration arrangement is settled. Changes in the fair value of contingent consideration resulting from the passage of time are recorded within interest expense until the contingent consideration is settled.

If the acquired net assets do not constitute a business under the acquisition method of accounting, the transaction is accounted for as an asset acquisition and no goodwill is recognized. In an asset acquisition, the amount allocated to acquired in-process research and development (IPR&D) with no alternative future use is charged to expense at the acquisition date.

Revenue Recognition

The Company accounts for revenue arising from contracts and customers in accordance with Accounting Standards Update (ASU or Update) No. 2014-09, Revenue from Contracts with Customers (ASC 606), which was adopted on January 1, 2018 using the modified retrospective transition method. There was no adjustment to the Company's opening balance of accumulated deficit resulting from the adoption of this guidance.

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

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Variable consideration arising from sales or usage-based royalties, promised in exchange for a license of the Company's Intellectual Property, is recognized at the later of (i) when the subsequent product sales occur or (ii) the performance obligation, to which some or all of the sales-based royalty has been allocated, has been satisfied.

The Company recognizes a contract asset relating to its conditional right to consideration for completed performance obligations. Accounts receivable are recorded when the right to consideration becomes unconditional. A contract liability is recorded for payments received in advance of the related performance obligation being satisfied under the contract.

The Company derives revenue from license fees, under its Commercialization Agreement with Collegium, sale of its products, and from license fees, milestones and royalties earned on license and collaborative arrangements.

Product Sales

The Company sells commercial products to wholesale distributors and retail pharmacies. Product sales revenue is recognized when title has transferred to the customer and the customer has assumed the risks and rewards of ownership, which typically occurs on delivery to the customer. The Company's performance obligation is to deliver product to the customer, and the performance obligation is completed upon delivery. The transaction price consists of a fixed invoice price and variable product sales allowances, which include rebates, discounts and returns. Product sales revenues are recorded net of applicable reserves for these product sales allowances. Receivables related to product sales are typically collected one to two months after delivery.

Product Sales Allowances—The Company considers products sales allowances to be variable consideration and estimates and recognizes product sales allowances as a reduction of product sales in the same period the related revenue is recognized. Product sales allowances are based on actual or estimated amounts owed on the related sales. These estimates take into consideration the terms of the Company's agreements with customers, historical product returns, rebates or discounts taken, estimated levels of inventory in the distribution channel, the shelf life of the product and specific known market events, such as competitive pricing and new product introductions. The Company uses the most likely method in estimating product sales allowances. If actual future results vary from the Company's estimates, the Company may need to adjust these estimates, which could have an effect on product sales and earnings in the period of adjustment. The Company's sales allowances include:

Product Returns—The Company allows customers to return product for credit with respect to product that within six months before and up to 12 months after its product expiration date. The Company estimates product returns and associated credit on NUCYNTA ER and NUCYNTA, Gralise, CAMBIA, Zipsor and Lazanda. Estimates for returns are based on historical return trends by product or by return trends of similar products, taking into consideration the shelf life of the product at the time of shipment, shipment and prescription trends, estimated distribution channel

inventory levels and consideration of the introduction of competitive products. The Company did not assume financial responsibility for returns of NUCYNTA ER and NUCYNTA previously sold by Janssen Pharma or Lazanda product previously sold by Archimedes Pharma US Inc. Under the Commercialization Agreement with Collegium for NUCYNTA ER and NUCYNTA and the divestiture of Lazanda to Slán, the Company is only financially responsible for product returns for product that were sold by the Company, which are identified by specific lot numbers.

The shelf life of NUCYNTA ER and NUCYNTA is 24 months to 36 months from the date of tablet manufacture. The shelf life of Gralise is 24 months to 36 months from the date of tablet manufacture. The shelf life of CAMBIA is 24 months to 48 months from the manufacture date. The shelf life of Zipsor is 36 months from the date of tablet manufacture. The shelf life of Lazanda is 24 to 36 months from the manufacture date. Because of the shelf life of the Company's products and its return policy of issuing credits with respect to product that is returned within six months before and up to 12 months after its product expiration date, there may be a significant period of time between when the product is shipped and when the Company issues credit on a returned product. Accordingly, the Company may have to adjust these estimates, which could have an effect on product sales and earnings in the period of adjustments.

Wholesaler and Retail Pharmacy Discounts — The Company offers contractually determined discounts to certain wholesale distributors and retail pharmacies that purchase directly from it. These discounts are either taken off invoice at the time of shipment or paid to the customer on a quarterly basis one to two months after the quarter in which product was shipped to the customer.

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Prompt Pay Discounts—The Company offers cash discounts to its customers (generally 2% of the sales price) as an incentive for prompt payment. Based on the Company's experience, the Company expects its customers to comply with the payment terms to earn the cash discount.

Patient Discount Programs—The Company offers patient discount co-pay assistance programs in which patients receive certain discounts off their prescriptions at participating retail pharmacies. The discounts are reimbursed by the Company approximately one month after the prescriptions subject to the discount are filled.

Medicaid Rebates—The Company participates in Medicaid rebate programs, which provide assistance to certain low income patients based on each individual state's guidelines regarding eligibility and services. Under the Medicaid rebate programs, the Company pays a rebate to each participating state, generally two to three months after the quarter in which prescriptions subject to the rebate are filled.

Chargebacks—The Company provides discounts to authorized users of the Federal Supply Schedule (FSS) of the General Services Administration under an FSS contract with the Department of Veterans Affairs. These federal entities purchase products from the wholesale distributors at a discounted price, and the wholesale distributors then charge back to the Company the difference between the current retail price and the price the federal entity paid for the product.

Managed Care Rebates—The Company offers discounts under contracts with certain managed care providers. The Company generally pays managed care rebates one to three months after the quarter in which prescriptions subject to the rebate are filled.

Medicare Part D Coverage Gap Rebates—The Company participates in the Medicare Part D Coverage Gap Discount Program under which it provides rebates on prescriptions that fall within the "donut hole" coverage gap. The Company generally pays Medicare Part D Coverage Gap rebates two to three months after the quarter in which prescriptions subject to the rebate are filled.

Royalties

For arrangements that include sales-based royalties and the license is deemed to be the predominant item to which the royalties relate, the Company recognizes royalty revenue at the later of (1) when the related sales occur, or (2) when the performance obligation to which some or all of the royalty has been allocated has been satisfied (or partially satisfied).

The Company currently receives royalties based on sales of Cambia in Canada and sales of NUCYNTA ER in Canada and Japan, which are recognized as revenue when the related sales occur as there are no continuing performance obligations by the Company under those agreements.

Stock Based Compensation

The Company uses the Black Scholes option valuation model to determine the fair value of stock options and employee stock purchase plan (ESPP) shares. The determination of the fair value of stock based payment awards on the date of grant using an option valuation model is affected by the Company's stock price as well as assumptions, which include the Company's expected term of the award, the expected stock price volatility, risk free interest rate and expected dividends over the expected term of the award.

The Company uses historical option exercise data to estimate the expected term of the options. The Company estimates the volatility of its common stock price by using the historical volatility over the expected term of the options. The Company bases the risk free interest rate on U.S. Treasury zero coupon issues with terms similar to the expected term of the options as of the date of grant. The Company does not anticipate paying any cash dividends in the foreseeable future and therefore uses an expected dividend yield of zero in the option valuation models. As a result of adopting ASU 2016-09 Improvements to Employee Share-Based Payment Accounting, the Company made an accounting policy election to account for forfeitures as they occur, rather than estimating expected forfeitures at the time of the grant.

The fair value of each restricted stock unit (RSU) that does not contain a market condition is equal to the market value of our common stock as of the date of the grant. The Company's Performance Stock Units (PSUs) vest over a

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three year period based on the Relative Total Shareholder Return (TSR) of the Company's common stock against the Russell 3000 Pharmaceuticals Total Return Index over the period. The grant-date fair value of the PSUs is determined using the Monte Carlo simulation method.

Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU or Update) No. 2014-09, Revenue from Contracts with Customers. This guidance outlines a new, single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. This new revenue recognition model provides a five-step analysis in determining when and how revenue is recognized. The new model requires revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration a company expects to receive in exchange for those goods or services. On July 9, 2015, the FASB deferred the effective date of this Update to fiscal years beginning after December 15, 2017.

The Company adopted ASC 606 using the modified retrospective method as of January 1, 2018. The Company determined that there was no cumulative effect of applying the new guidance to all contracts with customers that were not completed as of January 1, 2018, therefore no adjustment was required to the accumulated deficit as of the adoption date. Furthermore, upon adoption of the new guidance no adjustments to any prior year periods would have been reportable to present the condensed consolidated balance sheets, statements of operations, or statements of cash flows on a comparable basis to any current year reported balances or amounts.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. ASU 2016-15 addresses how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The standard was effective for us beginning January 1, 2018. The Company early adopted this guidance on January 1, 2017, and the adoption of this guidance did not materially affect the Company's consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which provides clarification on the definition of a business and adds guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The standard was effective for us beginning January 1, 2018. The future impact of ASU No. 2017-01 will be dependent upon the nature of the Company's future acquisition or disposition transactions, if any.

In May 2017, the FASB issued accounting guidance to clarify which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. The new standard was required to be applied prospectively. The guidance was effective for us beginning January 1, 2018. The adoption of this guidance did

not have a material impact on the Company's consolidated financial statements.

In March 2018, the FASB issued ASU No. 2018-05, Income Taxes (Topic 740): Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118, which provides clarification and guidance on the income tax accounting implications of the Tax Cuts and Jobs Act. The standard was effective for us beginning January 1, 2018.

In January of 2016, the FASB issued ASU No. 2016-01, Financial Instruments – Overall (Subtopic 405-20), Recognition and Measurement of Financial Assets and Financial Liabilities. ASU 2016-01 changed accounting for equity investments, financial liabilities under the fair value option and the presentation and disclosure requirements for financial instruments. In addition, it clarified guidance related to the valuation allowance assessment when recognizing deferred tax assets resulting from unrealized losses on available-for-sale debt securities. The guidance became effective for us on January 1, 2018 and required adoption using a modified retrospective approach, with certain exceptions. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

Recently Issued Accounting Standards

In February 2016, the FASB issued ASU No. 2016-02, Leases. This guidance requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease, respectively. A lessee is also

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required to record a right-of-use asset and a lease liability for all leases with a term of greater than twelve months regardless of classification. If the available accounting election is made, leases with a term of twelve months or less can be accounted for similar to existing guidance for operating leases. Additionally, in January 2018, the FASB issued ASU 2018-01, Leases, (Topic 842); which allows a Land Easement Practical Expedient for Transition to Topic 842. For a public entity, the amendments in this guidance are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early application of the amendments in this guidance is permitted for all entities. The Company is currently evaluating the impact that implementation will have on the Company's consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13 (ASU 2016-13), Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments which requires the measurement and recognition of expected credit losses for financial assets held at amortized cost. ASU 2016-13 replaces the existing incurred loss impairment model with an expected loss methodology, which will result in more timely recognition of credit losses. ASU 2016-13 is effective for annual reporting periods, and interim periods within those years beginning after December 15, 2019. The Company is currently in the process of evaluating the impact of the adoption of ASU 2016-13 on the Company's consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, that provides companies with an option to reclassify stranded tax effects resulting from enactment of the Tax Cuts and Jobs Act (TCJA) from accumulated other comprehensive income to retained earnings. The guidance will be effective for the Company beginning in the first quarter of 2019 with early adoption permitted, and would be applied either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the tax rate as a result of TCJA is recognized. The Company has not made a determination as to which alternative methods it will use when it adopts this standard, but does not expect the adoption of this ASU to have a material impact on its results of operations, financial position and cash flows.

NOTE 2. CASH, CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS

Securities classified as cash and cash equivalents and short-term investments as of March 31, 2018 and December 31, 2017 are summarized below (in thousands). Estimated fair value is based on quoted market prices for these investments.

March 31, 2018	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value

Cash and cash equivalents				
Cash	$ 76,631	$ —	$ —	$ 76,631
Money market funds	46	—	—	46
Commercial paper	2,400	—	—	2,400
U.S. Agency discount notes	22,615	1	—	22,616
Total cash and cash equivalents	$ 101,692	$ 1	$ —	$ 101,693

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December 31, 2017	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents				
Cash	$ 103,119	$ —	$ —	$ 103,119
Money market funds	95	—	—	95
Commercial paper	23,670	—	—	23,670
Total cash and cash equivalents	126,884	—	—	126,884
Short-term investments				
Corporate debt securities and commercial paper with maturities less than 1 year	1,210	—	(5)	1,205
Total short-term investments	1,210	—	(5)	1,205
Total	$ 128,094	$ —	$ (5)	$ 128,089

The Company considers all highly liquid investments with a maturity at date of purchase of three months or less to be cash equivalents. Cash and cash equivalents generally consist of cash on deposit with banks, money market instruments, U.S. Agency discount notes, commercial paper and corporate debt securities.

The Company invests its cash in money market funds and marketable securities including U.S. Treasury and government agency securities, commercial paper, and high quality debt securities of financial and commercial institutions. To date, the Company has not experienced material losses on any of its balances. These securities are carried at fair value, which is based on readily available market information, with unrealized gains and losses included in “accumulated other comprehensive loss” within shareholders’ equity on the consolidated balance sheets. The Company uses the specific identification method to determine the amount of realized gains or losses on sales of marketable securities. Realized gains or losses have been insignificant and are included in “interest and other income” in the consolidated statement of operations.

As of March 31, 2018, the Company held zero securities in an unrealized loss position or that have been in a continuous loss position. The following table shows the gross unrealized losses and fair value of the Company’s investments with unrealized losses that were not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2017 (in thousands):

	Less than 12 months		12 months or greater		Total	
December 31, 2017	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Corporate Debt Securities	$ 1,205	$ (5)	$ —	$ —	$ 1,205	$ (5)

The gross unrealized losses above were caused by interest rate increases. No significant facts or circumstances have arisen to indicate that there has been any deterioration in the creditworthiness of the issuers of the securities held by the Company. Based on the Company's review of these securities, including the assessment of the duration and severity of the unrealized losses and the Company's ability and intent to hold the investments until maturity, there were no material other than temporary impairments for these securities at March 31, 2018 or December 31, 2017. Gross realized gains and losses on marketable securities were not material for the three months ended March 31, 2018 or 2017.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs.

· Level 1: Quoted prices in active markets for identical assets or liabilities.

· Level 2: Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

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

The following tables represent the Company's fair value hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2018 and December 31, 2017 (in thousands):

March 31, 2018	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 46	$ —	$ —	$ 46
Commercial paper	—	2,400	—	2,400
U.S. Agency discount notes	—	22,616	—	22,616
Total	$ 46	$ 25,016	$ —	$ 25,062
Liabilities:				
Contingent consideration—Zipsor	$ —	$ —	$ 238	$ 238
Contingent consideration—CAMBIA	—	—	1,011	1,011
Total	$ —	$ —	$ 1,249	$ 1,249

December 31, 2017	Level 1	Level 2	Level 3	Total
Assets:				
Money market funds	$ 95	$ —	$ —	$ 95
Commercial paper	—	23,670	—	23,670
Corporate debt securities	—	1,205	—	1,205
Total	$ 95	$ 24,875	$ —	$ 24,970
Liabilities:				
Contingent consideration—Zipsor	$ —	$ —	$ 464	$ 464
Contingent consideration—Lazanda	—	—	156	156
Contingent consideration—CAMBIA	—	—	993	993
Total	$ —	$ —	$ 1,613	$ 1,613

The fair value measurement of the contingent consideration obligations arises from the Zipsor, CAMBIA and Lazanda acquisitions and relates to fair value of the potential future contingent milestone payments and royalties payable under the respective agreements which are determined using Level 3 inputs. The remaining contingent consideration liability following the divestiture of Lazanda in November 2017 was $0.2 million. This liability was settled in the first quarter of 2018. The key assumptions in determining the fair value are the discount rate and the probability assigned to the potential milestones and royalties being achieved. At each reporting date, the Company re-measures the contingent consideration obligation arising from the above acquisitions to their estimated fair values. Any changes in the fair

value of contingent consideration resulting from a change in the underlying inputs are recognized in operating expenses until the contingent consideration arrangement is settled. Changes in the fair value of contingent consideration resulting from the passage of time are recorded within interest expense until the contingent consideration is settled. The table below provides a summary of the changes in fair value recorded in interest expense and selling, general and administrative expenses for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31,	
	2018	2017
Fair value, beginning of the period	$ 1,613	$ 14,825
Changes in fair value recorded in interest expense	40	531
Changes in fair value recorded in selling, general and administrative expenses	(242)	(5,000)
Royalties and milestone paid	(162)	(1,745)
Total	$ 1,249	$ 8,611

The estimated fair value of the 2.50% Convertible Senior Notes Due 2021, which the Company issued on September 9, 2014 is based on a market approach. The estimated fair value was approximately $281.5 million and $295.4 million (par value $345.0 million) as of March 31, 2018 and December 31, 2017, respectively, and represents a Level 2 valuation. The principal amount of the Senior Notes approximates their fair value as of March 31, 2018 represents a Level 2 valuation. When determining the estimated fair value of the Company’s debt, the Company uses a

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commonly accepted valuation methodology and market-based risk measurements that are indirectly observable, such as credit risk.

There were no transfers between Level 1, Level 2 or Level 3 of the fair value hierarchy during the three months ended March 31, 2018 and 2017.

NOTE 3. NET INCOME (LOSS) PER SHARE

Basic net income (loss) per share is calculated by dividing the net income (loss) by the weighted-average number of shares of common stock outstanding during the period. Diluted net income (loss) per share is calculated by dividing the net income (loss) by the weighted-average number of shares of common stock outstanding during the period, plus potentially dilutive common shares, consisting of stock options, RSUs, PSUs, ESPP and convertible debt. The Company uses the treasury-stock method to compute diluted earnings per share with respect to its stock options and equivalents. The Company uses the if-converted method to compute diluted earnings per share with respect to its convertible debt. For purposes of this calculation, options to purchase stock, including stock options, RSUs, PSUs and ESPP, are considered to be potential common shares and are only included in the calculation of diluted net income (loss) per share when their effect is dilutive. Basic and diluted earnings per common share are calculated as follows:

	Three Months Ended March 31,	
(in thousands, except for per share amounts)	2018	2017
Basic and diluted net income (loss) per share		
Net income (loss)	$ 33,824	$ (26,741)
Denominator	63,503	62,129
Basic net income (loss) per share	$ 0.53	$ (0.43)
Diluted net income (loss) per share		
Numerator:		
Net income (loss)	$ 33,824	$ (26,741)
Add interest expense on convertible debt, net of tax	5,187	—
	$ 39,011	$ (26,741)
Denominator:		
Denominator for basic income (loss) per share	63,503	62,129
Add effect of diluted securities:		
Stock options and equivalents	443	—
Convertible debt	17,931	—
Denominator for diluted income (loss) per share	81,877	62,129
Diluted net income (loss) per share	$ 0.48	$ (0.43)

The following table sets forth outstanding potentially dilutive common shares that are not included in the computation of diluted net income (loss) per share because to do so would be anti-dilutive:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Convertible debt	—	17,931
Stock options and equivalents	4,248	8,517
Total potentially dilutive common shares	4,248	26,448

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NOTE 4. REVENUE

Disaggregated Revenue

The following table summarizes revenue from contracts with customers for the three months ended March 31, 2018 and 2017 (in thousands):

	Three Months Ended March 31,	
	2018	2017
Product sales, net		
Gralise	$ 14,827	$ 17,600
CAMBIA	6,416	7,190
Zipsor	4,746	4,651
Total neurology product sales, net	25,989	29,441
NUCYNTA products	18,145	56,919
Lazanda	220	3,925
Total product sales, net	44,354	90,285
Commercialization agreement:		
Commercialization rights and facilitation services	28,095	—
Revenue from transfer of inventory	55,705	—
Royalties	250	162
Total revenues	$ 128,404	$ 90,447

During the three months ended March 31, 2018, the Company released $12.5 million of NUCYNTA sales reserves which were primarily recorded in the fourth quarter of 2017, as financial responsibility for those reserves transferred to Collegium upon closing of the Commercialization Agreement. The benefit of this released is reflected within the NUCYNTA product sales recorded for the three months ended March 31, 2018.

Commercialization Agreement with Collegium

In January 2018, the Company entered into a Commercialization Agreement with Collegium (Commercialization Agreement), pursuant to which the Company granted Collegium the right to commercialize the NUCYNTA pain products in the U.S. Under the Commercialization Agreement, Collegium assumed all commercialization responsibilities for NUCYNTA effective January 9, 2018, including sales and marketing. The Company will receive a royalty on all NUCYNTA revenues based on certain net sales thresholds, with a minimum royalty of $132 million for the year ended December 31, 2018 and $135 million per year for the years ended December 31, 2019, to December

31, 2021. In addition to the minimum royalties, the Company will also receive (i) a 25% royalty on annual net sales of NUCYNTA between $233.0 million to $258.0 million and (ii) 17.5% on annual net sales of NUCYNTA above $258.0 million for the years ended December 31, 2018 to December 31, 2021. From and after January 1, 2022, the Company will receive (i) a 58% royalty on annual net sales of NUCYNTA up to $233.0 million (ii) 25% royalty on annual net sales of NUCYNTA of $233.0 million to $258.0 million and (iii) 17.5% on annual net sales of NUCYNTA above $258.0 million. The Company received an upfront payment of $10.0 million as well as $6.2 million with respect to the inventory of finished goods which was transferred to Collegium on closing of the transaction in January 2018.

The Company identified the following three performance obligations under the Commercialization Agreement:

1. License to commercialize the NUCYNTA pain products,
2. Services to arrange for supplies of NUCYNTA pain products using the Company's existing contract manufacturing contracts with third parties; and
3. Transfer control of all NUCYNTA finished goods held at closing.

The Company determined the total transaction price to be $553 million, which consists of $537 million in total annual minimum royalty payments, the $10.0 million upfront fee, and a $6.2 million payment for NUCYNTA finished goods inventory at cost. In accordance with the relevant Accounting Standard, the Company determined that the duration of the Commercialization Agreement begins on the effective date of January 9th, 2018 and lasts through December 31, 2021, which is consistent with the contractual period in which the Company and Collegium has enforceable rights and

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obligations which include the minimum royalty period and the period in which Collegium would incur a $25 million termination penalty on terminating the agreement.

The transaction price was allocated to the performance obligations noted above in proportion to their standalone selling prices and will be recognized as this performance obligations are satisfied by the Company. The transaction price allocated to the inventory transferred to Collegium on closing was $55.7 million and was recognized on the closing date as the control of such inventory was transferred to Collegium. The transaction price allocated to the other remaining performance obligations of the license to commercialize NUCYNTA and the related services to arrange for supplies was $497.5 million. This amount will be recognized ratably over the time through December 31, 2021, which represents the period over which enforceable rights and obligations exist after considering the various termination rights for either parties that exist in the contract. For the three months ended March 31, 2018, the Company recognized $28.1 million related to the right to commercialize NUCYNTA and related facilitation services. Total revenue recognized for the three months ended March 31, 2018 was $83.8 million. Any amounts receivable in excess of the minimum royalties due up to December 31, 2021, will be recognized during the period that NUCYNTA net sales by Collegium exceed $233.0 million. Royalties receivable after January 1, 2022 will be recognized based on subsequent NUCYNTA net sales recorded by Collegium.

The annual minimum royalty amounts are payable by Collegium in equal quarterly installments of $33.8 million, and are initially received through a lockbox sweep mechanism. Remittances from customers on product sales of NUCYNTA made by Collegium are deposited to a designated lockbox account, separate from Collegium's other receivables. On a daily basis, 35% of the cash receipts in this lockbox account are swept to Depomed's bank accounts up to the minimum cash royalty amounts which are $30.8 million for the three months ended March 31, 2018 and $33.8 million per quarter, thereafter. If the cash receipts received by Depomed in a quarter are lower than the minimum quarterly royalty, or if the royalty receivable to Depomed is above the minimum quarterly amount, Collegium is responsible to remit the remaining royalty payment within 45 days after the end of the each quarter. For the three months ended March 31, 2018, $13.1 million was received by Depomed during the quarter and $17.7 million has been classified as a receivable on the unaudited Condensed Consolidated Balance Sheets.

Contract Assets and Liabilities

The following table presents changes in the Company's contract assets and liabilities for the three months ended March 31, 2018 (in thousands):

	Balance Beginning of Period	Additions	Deductions	Balance End of Period
Contract assets:				
Contract asset	$ —	$ 55,705	$ (18,855)	$ 36,850

The Company receives payments from Collegium based on the above described schedule as established in our contracts. Contract asset relates to our conditional right to consideration for our completed performance under the Commercialization agreement. This contract asset relates to the revenue recognized by the Company from transfer of inventory to Collegium on the date of closing of the agreement in January 2018. Accounts receivable are recorded when the right to consideration becomes unconditional. $9.9 million and $27.0 million of the contract asset has been recorded within “Prepaid and other assets” and “Other long-term assets,” respectively.

The Company acquired the U.S. rights to NUCYNTA from Janssen Pharmaceuticals, Inc. (Janssen) in April 2015. As part of that transaction, the Company also acquired the related royalty obligations for NUCYNTA to Grünenthal, the originator of tapentadol. Pursuant to the terms of the commercialization agreement, Collegium is now responsible for those royalty obligations. However, as a condition of giving its consent to the commercialization agreement with Collegium, Grünenthal amended the terms of the original royalty agreement to require payment of a minimum royalty of $34.0 million per year on net sales of NUCYNTA greater than $180.0 million and equal to, or less than, $243.0 million for each of the years ended December 31, 2018 through 2021. Collegium is responsible for payments of royalties to Grünenthal and the Company is obligated to cover any shortfall between the minimum royalty amount of $34.0 million and the amounts paid to Grünenthal by Collegium for each of the years ended December 31, 2018 through 2021. Under the terms of this amended royalty agreement, the maximum amount that the Company could be obligated to pay is $8.8 million per year for each of the years ended December 31, 2018 through 2021. In return for this agreement to pay

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minimum royalties, we received the right to share royalties with Grünenthal on net sales of NUCYNTA above $243.0 million during the same period.

The Company reviews the net sales of NUCYNTA by Collegium and recognizes an estimated liability for the amount it believes is likely to be paid for the year. As this estimation process requires a significant amount of judgment and is based on expected net sales of NUCYNTA by Collegium, the liability recorded as of a reporting period may not necessarily be reflective of the amount ultimately due to Grünenthal for the year.

Collaboration and License Agreements

Ironwood Pharmaceuticals, Inc. In July 2011, the Company entered into a collaboration and license agreement with Ironwood (Ironwood Agreement) granting Ironwood a license for worldwide rights to certain patents and other intellectual property rights to our Acuform drug delivery technology for IW 3718, an Ironwood product candidate under evaluation for refractory GERD. The Company has received $3.4 million under the agreement, including a contingent milestone payment of $1.0 million in March 2014 as a result of the initiation of clinical trials relating to IW 3718 by Ironwood. The Company is entitled to receive additional contingent milestone payments upon the occurrence of certain development milestones and royalties on net sales of the product if approved, including a $5.0 million contingent milestone payment if Ironwood commences Phase 3 clinical trials for IW-3718.

The Company identified the following two performance obligations under the Ironwood Agreement: (1) the license to the Acuform technology and (2) formulation work associated with IW-3718. The license was granted in 2011 and the formulation work was completed in 2012. The Company has no ongoing performance obligations and has recognized all proceeds received to date as revenue.

The future contingent milestones under the Ironwood Agreement are considered variable consideration and are estimated using the most likely method. As part of implementation of ASC 606, the Company evaluated whether the future milestones under the Ironwood Agreement should have been included as part of the transaction price in periods before January 1, 2018. The Company concluded that because of development and regulatory risks at the time, it was probable that a significant revenue reversal could have occurred. Accordingly, the associated future contingent milestone values were not included in the transaction price for periods before January 1, 2018. At the end of each subsequent reporting period, the Company re-evaluates the probability or achievement of each such milestone and any related constraint, and if necessary, adjusts its estimates of the overall transaction price. Any such adjustments are recorded on a cumulative catch-up basis, which would affect revenues and earnings in the period of adjustment. The Company did not recognize any revenue under this agreement for the three months ended March 31, 2018 or March 31, 2017, respectively.

NOTE 5. STOCK-BASED COMPENSATION

Employee Stock Purchase Plan

The following table presents stock-based compensation expense recognized for stock options, stock awards, restricted stock units and the Company's Employee Stock Purchase Program (ESPP) in the Company's Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended March 31,	
	2018	2017
Cost of sales	$ 14	$ 36
Research and development expense	53	346
Selling, general and administrative expense	1,909	3,174
Restructuring charges	258	—
Total	$ 2,234	$ 3,556

At March 31, 2018, the Company had $19.4 million of total unrecognized compensation expense related to stock option grants and restricted stock units that will be recognized over an average vesting period of 2.34 years.

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Performance-based Restricted Stock Units

During the three months ended March 31, 2018, the Company granted Performance Stock Units (PSUs) with an aggregate target award of 344,700 units and a weighted-average grant-date fair value of $10.07 per unit. The PSUs vest in annual cliffs over a three year period based on the Relative Total Shareholder Return (TSR) of the Company's common stock against the Russell 3000 Pharmaceuticals Total Return Index over the period. The ultimate award, which is determined at the end of the three-year cycle, can range from zero to 200% of the target. The recipients of the PSU awards will have voting rights and the right to receive a dividend once the underlying shares have been issued. The grant-date fair value is based upon the Monte Carlo simulation method.

The following table summarizes the PSU activity for the three months ended March 31, 2018 under the 2014 Plan (in thousands, except per share data):

	Number of Shares	Weighted Average Grant Date Fair Value Per Share	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Non-vested performance-based restricted stock units at December 31, 2017	—	$ —		
Granted	344,700	10.07		
Vested	—	—		
Forfeited	—	—		
Non-vested performance-based restricted stock units at March 31, 2018	344,700	$ 10.07	2.85	$ 3,472

As of March 31, 2018, total unrecognized compensation cost related to PSUs was $3.5 million, which is expected to be recognized over the remaining weighted-average vesting period of 2.85 years.

NOTE 6. INVENTORIES

Inventories consist of finished goods, raw materials and work in process and are stated at the lower of cost or market and consist of the following (in thousands):

	March 31, 2018	December 31, 2017
Raw materials	$ 2,317	$ 3,008
Work-in-process	801	204
Finished goods	2,250	9,830
Total	$ 5,368	$ 13,042

NOTE 7. ACCOUNTS RECEIVABLES

Accounts receivables consist of the following (in thousands):

	March 31, 2018	December 31, 2017
Product sales, net	$ 23,733	$ 71,919
Commercialization agreement	38,353	—
Receivables from collaborative partners	342	563
Total accounts receivable, net	$ 62,428	$ 72,482

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NOTE 8. ACCRUED LIABILITIES

Accrued liabilities consist of the following (in thousands):

	March 31, 2018	December 31, 2017
Accrued compensation	$ 2,920	$ 7,345
Accrued royalties	3,197	17,370
Accrued restructuring and one-time termination costs	6,820	9,483
Other accrued liabilities	19,672	26,298
Total accrued liabilities	$ 32,609	$ 60,496

NOTE 9. DEBT

Senior Notes

On April 2, 2015, the Company issued $575.0 million aggregate principal amount of senior secured notes (the Senior Notes) for aggregate gross proceeds of approximately $562.0 million pursuant to a Note Purchase Agreement dated March 12, 2015, among the Company and Deerfield Private Design Fund III, L.P., Deerfield Partners, L.P., Deerfield International Master Fund, L.P., Deerfield Special Situations Fund, L.P., Deerfield Private Design Fund II, L.P., Deerfield Private Design International II, L.P., BioPharma Secured Investments III Holdings Cayman LP, Inteligo Bank Ltd. and Phemus Corporation (collectively, the Purchasers) and Deerfield Private Design Fund III, L.P., as collateral agent. The Company used $550.0 million of the net proceeds received upon the sale of the Senior Notes to fund a portion of the Purchase Price paid to Janssen Pharma in connection with the NUCYNTA acquisition. The Company incurred debt issuance costs of $0.5 million for 2015.

The Senior Notes will mature on April 14, 2021 (unless earlier prepaid or repurchased), are secured by substantially all of the assets of the Company and any subsidiary guarantors, and bear interest at the rate equal to the lesser of (i) 9.75% over the three month London Inter-Bank Offer Rate (LIBOR), subject to a floor of 1.0% and (ii) 11.95% (through the third anniversary of the purchase date) and 12.95% (thereafter). The interest rate is determined at the first business day of each fiscal quarter, commencing with the first such date following April 2, 2015. The interest rate as of March 31, 2018 and 2017 was 11.45% and 10.75%, respectively.

In April 2017, the Company prepaid and retired $100.0 million of the Senior Notes and paid a $4.0 million prepayment fee; and in November 2017, the Company prepaid and retired an additional $10 million of the Senior Notes and paid a $0.4 million prepayment fee. The Company recorded a net loss on prepayment of the Senior Notes of $5.9 million which represented the prepayment fees of $4.4 million and the immediate recognition of unamortized balances of debt discount and debt issuance costs of $1.5 million in 2017. This loss is recorded as a loss on prepayment of Senior Notes in the consolidated statements of operations for 2017.

The remaining $365.0 million of Senior Notes can be prepaid, at the Company’s option. The Company is required to repay the outstanding Senior Notes in full if the principal amount outstanding on its existing 2.50% Convertible Senior Notes due 2021 as of March 31, 2021, is greater than $100.0 million. In addition, if the successor entity in a Major Transaction, as defined in the Note Purchase Agreement, does not satisfy specified qualification criteria, the Purchasers may require the Company to prepay the Senior Notes upon consummation of the Major Transaction in an amount equal to the principal amount of outstanding Senior Notes, accrued and unpaid interest and a prepayment premium in an amount equal to what the Company would have otherwise paid in an optional prepayment described in the following paragraph. The Company is required to make mandatory prepayments on the Senior Notes in an amount equal to the proceeds it receives in connection with asset dispositions in excess of $10.0 million, together with accrued and unpaid interest on the principal amount prepaid.

Pursuant to the Note Purchase Agreement, upon the consummation of the sale of the Senior Notes on April 2, 2015, the Company and Depo NF Sub, LLC entered into a Pledge and Security Agreement with the Deerfield Private Design Fund III, L.P. (the Collateral Agent), pursuant to which the Company and Depo NF Sub each granted the Collateral

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Agent (on behalf of the Purchasers) a security interest in substantially all of their assets, other than specifically excluded assets.

On December 4, 2017, the Company and the Purchasers entered into an Amendment to the existing Note Purchase Agreement. The Amendment facilitated the Company's entry into a Commercialization Agreement, by and between the Company and Collegium and Collegium NF, LLC, a Delaware limited liability company and wholly owned subsidiary of Collegium, on December 4, 2017, pursuant to which the Company, or one of its subsidiaries, granted the right to Collegium and its sub licensees to commercialize NUCYNTA® in the U.S. of America, the District of Columbia and Puerto Rico.

In connection with its entry into the Commercialization Agreement, the Purchasers (i) waived the requirement that some or all of the Asset Disposition Proceeds realized from the granting of the Exclusive License be used to prepay the outstanding principal amount of the Notes pursuant to Section 2.7(b) of the Note Purchase Agreement and (ii) agreed to (a) replace the minimum net sales covenant in Section 6.7 of the Note Purchase Agreement with a minimum EBITDA covenant, and (b) made certain other amendments related to the amortization of the Notes. In addition, the prepayment premiums were amended to 4% of the principal amount of the Notes to be prepaid, if such prepayment occurs after the second anniversary of the Purchase Date but on or prior to the fifth anniversary of the Purchase Date; and (iii) zero, if such prepayment occurs after the fifth anniversary of the Purchase Date. The minimum EBITDA covenants stipulate that the Company's EBITDA, measured as of the last day of the twelve month measurement period be (i) for the twelve month period from October 1, 2017 through to September 30, 2018 be at least $90 million and (ii) $125 million, thereafter. The Amendment also modified the repayment schedule; and required the Company to prepay and retire $10.0 million of the Senior Notes and pay a $0.4 million prepayment fee. The Company paid a $3.0 million upfront non-refundable amendment fee which, pursuant to the terms of the modification, can be off-set dollar for dollar against any future prepayment fees.

The Company accounted for the amendment as a debt modification in accordance with the applicable accounting standards. Accordingly, the $3.0 million amendment fee paid to the Purchasers was capitalized and is being amortized over the remaining term of the Senior Notes.

The Senior Notes and related indenture contain customary covenants, including, among other things, and subject to certain qualifications and exceptions, covenants that restrict the Company's ability and the ability of its subsidiaries to: incur or guarantee additional indebtedness; create or permit liens on assets; pay dividends on capital stock or redeem, repurchase or retire capital stock or subordinated indebtedness; make certain investments and other restricted payments; engage in mergers, acquisitions, consolidations and amalgamations; transfer and sell certain assets; and engage in transactions with affiliates.

The principal amount of the Senior Notes is repayable as of March 31, 2018 is as follows (amounts in thousands):

2018 (remainder)	$ 82,500
2019	120,000
2020	80,000
2021	82,500
Total	$ 365,000

The Company is scheduled to make the 2018 Senior Notes principal payments of $57.5 million in April 2018 and $25.0 million in October 2018.

The following is a summary of the carrying value of the Senior Notes as of March 31, 2018 and December 31, 2017 (in thousands):

	March 31, 2018	December 31, 2017
Principal amount of the Senior Notes	$ 365,000	$ 365,000
Unamortized debt discount balance	(4,106)	(4,717)
Unamortized debt issuance costs	(2,667)	(3,063)
Total Senior Notes	$ 358,227	$ 357,220

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The debt discount and debt issuance costs are being amortized as interest expense through April 2021 using the effective interest method. The following is a summary of interest expense for the three months ended March 31, 2018 and 2017 (in thousands):

	Three Months Ended March 31,	
	2018	2017
Contractual interest expense	$ 10,441	$ 12,766
Amortization of debt discount and debt issuance costs	1,008	602
Total interest expense Senior Notes	$ 11,449	$ 13,368

Convertible Debt

On September 9, 2014, the Company issued $345.0 million aggregate principal amount of 2.50% Convertible Senior Notes Due 2021 (the Convertible Notes) resulting in net proceeds to the Company of $334.2 million after deducting the underwriting discount and offering expenses of $10.4 million and $0.4 million, respectively.

The Convertible Notes were issued pursuant to an indenture, as supplemented by a supplemental indenture dated September 9, 2014, between the Company and The Bank of New York Mellon Trust Company, N.A., as trustee (the Trustee), and mature on September 1, 2021, unless earlier converted, redeemed or repurchased. The Convertible Notes bear interest at the rate of 2.50% per annum, payable semi-annually in arrears on March 1 and September 1 of each year, beginning March 1, 2015.

Prior to March 1, 2021, holders of the 2021 Convertible Notes can convert their securities, at their option: (i) during any calendar quarter commencing after December 31, 2015, if the last reported sale price of the common stock for at least 20 trading days (whether or not consecutive) during the period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter is greater than or equal to $25.01 (130% of the $19.24 conversion price) on each applicable trading day; (ii) during the five business day period after any five consecutive trading day period in which the trading price per $1,000 principal amount of notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of our common stock and the conversion rate on each such trading day; and (iii) at any time upon the occurrence of specified corporate transactions, to include a change of control (as defined in the Notes Indenture). On or after March 1, 2021 to the close of business on the second scheduled trading day immediately preceding the maturity date, the holders of the 2021 Convertible Notes may convert all or any portion of their notes, in multiples of $1,000 principal amount, at the option of the holder regardless of the foregoing circumstances. The initial conversion rate of 51.9852 shares of common stock per $1,000 principal amount of Convertible Notes is equivalent to a conversion price of approximately $19.24 per share of common stock.

Upon conversion, the Company will pay or deliver, as the case may be, cash, shares of the Company's common stock or a combination of cash and shares of the Company's common stock, at the Company's election. If the conversion obligation is satisfied solely in cash or through payment and delivery of a combination of cash and shares, the amount of cash and shares, if any, due upon conversion will be based on a daily conversion value calculated on a proportionate basis for each trading day in a 40 trading day observation period.

The closing price of the Company’s common stock did not exceed 130% of the $19.24 conversion price, for the required period during the quarter ended March 31, 2018. As a result, the Convertible Notes are not convertible as of March 31, 2018.

The Convertible Notes were accounted for in accordance with ASC Subtopic 470-20, Debt with Conversion and Other Options. Pursuant to ASC Subtopic 470-20, since the Convertible Notes can be settled in cash, shares of common stock or a combination of cash and shares of common stock at the Company’s option, the Company is required to separately account for the liability (debt) and equity (conversion option) components of the instrument. The carrying amount of the liability component of any outstanding debt instrument is computed by estimating the fair value of a similar liability without the conversion option. The amount of the equity component is then calculated by deducting the fair value of the liability component from the principal amount of the convertible debt instrument. The effective interest rate used in determining the liability component of the Convertible Notes was 9.34%. This resulted in the initial recognition of $226.0 million as the liability component net of a $119.0 million debt discount with a corresponding net of tax increase to paid-in capital of $73.3 million, representing the equity component of the Convertible Notes. The underwriting discount of $10.4 million and offering expenses of $0.4 million were allocated between debt issuance costs

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and equity issuance costs in proportion to the allocation of the proceeds. Equity issuance costs of $3.7 million related to the convertible notes were recorded as an offset to additional paid-in capital.

The following is a summary of the liability component of the Convertible Notes as of March 31, 2018 and December 31, 2017 (in thousands):

	March 31, 2018	December 31, 2017
Principal amount of the Convertible Notes	$ 345,000	$ 345,000
Unamortized discount of the liability component	(67,642)	(71,799)
Unamortized debt issuance costs	(3,438)	(3,691)
Total Convertible Notes	$ 273,920	$ 269,510

The debt discount and debt issuance costs are being amortized as interest expense through September 2021. The following is a summary of interest expense for the three months ended March 31, 2018 and 2017 (in thousands):

	Three Months Ended March 31,	
	2018	2017
Stated coupon interest	$ 2,156	$ 2,156
Amortization of debt discount and debt issuance costs	4,410	4,048
Total interest expense Convertible Notes	$ 6,566	$ 6,204

NOTE 10. SHAREHOLDERS' EQUITY

Option Exercises

For the three months ended March 31, 2018, employees exercised options to purchase 120,302 shares of the Company’s common stock with net proceeds to the Company of approximately $0.6 million. For the three months ended March 31, 2017, employees exercised options to purchase 283,797 shares of the Company’s common stock with net proceeds to the Company of approximately $2.6 million.

Restricted Stock Units

For the three months ended March 31, 2018 and March 31, 2017, the Company issued 32,699 shares and zero shares, respectively, of the Company’s common stock due to vesting of restricted stock units.

NOTE 11. INCOME TAXES

On December 22, 2017, the U.S. government enacted the Tax Cuts and Jobs Act (the Tax Act). The Tax Act includes significant changes to the U.S. corporate income tax system including, but not limited to, a federal corporate rate reduction from 35% to 21% and limitations on the deductibility of interest expense and executive compensation. In order to calculate the effects of the new corporate tax rate on our deferred tax balances, ASC 740 Income Taxes (ASC 740) required the re-measurement of our deferred tax balances as of the enactment date of the Tax Act, based on the rates at which the balances were expected to reverse in the future. Due to the Company’s full valuation allowance position, there was no change to the presentation of the deferred tax balances on the financial statements, except for the re-measurement of these deferred tax balances in the income tax footnote. The re-measurement resulted in a one-time reduction in federal & state deferred tax assets as of December 31, 2017 of approximately $25.5 million, which was fully offset by a corresponding change to the Company's valuation allowance.

As of March 31, 2018, our net deferred tax assets are fully offset by a valuation allowance. The valuation allowance is determined in accordance with the provisions of ASC 740, Income taxes, which require an assessment of both negative and positive evidence when measuring the need for a valuation allowance. Based on the weight of available evidence, we recorded a full valuation allowance against our net deferred assets beginning in the fourth quarter of 2016. We have continued to provide a full valuation allowance against our net deferred assets in subsequent quarters. We reassess the need for a valuation allowance on a quarterly basis. If it is determined that a portion or all of the

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valuation allowance is not required, it will generally be a benefit to the income tax provision in the period such determination is made.

In the three months ended March 31, 2018, the Company recorded a benefit from income taxes of approximately $0.3 million that represents an effective tax rate of (1.0%) on income from continuing operations. The difference between the income tax benefit of $0.3 million and the tax at the statutory rate of 21% on current year operations is principally due to the change in valuation allowance. For the three months ended March 31, 2017, the difference between the recorded provision for income taxes and the tax benefit based on the federal statutory rate of 35%, was primarily attributable to the impact of the valuation allowance.

The Company files income tax returns in the United States federal jurisdiction and in various states, and the tax returns filed for the years 1997 through 2016 and the applicable statutes of limitation have not expired with respect to those returns. Because of net operating losses and unutilized R&D credits, substantially all of the Company's tax years remain open to examination. Interest and penalties, if any, related to unrecognized tax benefits, would be recognized as income tax expense by the Company. At March 31, 2018 the Company had approximately $0.9 million of accrued interest and penalties associated with unrecognized tax benefits.

NOTE 12. COMMITMENTS AND CONTINGENCIES

Leases

We have a non-cancelable operating lease for our office buildings and we are obligated to make payments under non-cancelable operating leases for automobiles used by our sales force. Future minimum lease payments under our non-cancelable operating leases at March 31, 2018 were as follows (in thousands):

Year Ending December 31,	Lease Payments
2018 (remainder)	$ 1,887
2019	2,678
2020	2,559
2021	2,360
2022	2,192
Thereafter	632
Total	$ 12,308

In April 2012, the Company entered into an office and laboratory lease agreement to lease approximately 52,500 rentable square feet in Newark, California (Newark Lease) commencing on December 1, 2012. The Company occupied approximately 8,000 additional rentable square feet commencing in July 2015. The lease is due to expire on November 30, 2022.

The Company is relocating its corporate headquarters from Newark, California to Lake Forest, Illinois sometime in mid-2018. The Company began preliminary discussions with the Newark Lease Landlord during the first quarter of 2018 and discussed the options to exit the premises by either subleasing the space or negotiating an exit in the second or the third quarter of 2018.

Effective February 28, 2018, the Company entered into an Office Lease, in Lake Forest, Illinois (Lake Forest Lease) for its corporate headquarters, where the Company will lease approximately 31,000 rentable square feet of space. The Office Lease will commence on the completion of the Company's initial tenant improvements in the space which are expected to be around July 1, 2018, but no later than August 1, 2018. The Lake Forest Lease term is for five years and six months. The Company has the right to renew the term of the Lease for one period of five years, provided that written notice is made to the Landlord no later than twelve months prior to the expiration of the initial term of the Lease. Prior to the Lake Forest Lease Commencement Date, the Company has the right to use temporary space in the Building containing approximately 6,700 rentable square feet.

The Lake Forest Lease initial annual base rent will be $18.00 per rentable square foot and will increase annually by $0.50 per rentable square foot. The lease is a triple net lease, with the Company required to pay its pro rata share of real estate taxes and operating expenses. The Landlord will make available to the Company a tenant improvement allowance

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of $28.00 per square rentable square foot, which the Company may use towards the initial build-out or apply to the payment of rent.

As of March 31, 2018, the aggregate rent payable over the remaining term of the lease agreements was approximately $7.6 million on the Newark Lease and $3.3 million on the Lake Forest Lease, including the Company's option to renew. Deferred rent was approximately $1.4 million as of March 31, 2018 and $1.4 million as of December 31, 2017.

Gross rent expense relating to the office lease agreements for the three months ended March 31, 2018 and 2017, was $0.4 million and $0.3 million, respectively.

The Company has an operating lease agreement with Enterprise FM Trust (Enterprise) for the lease of vehicles to be used by the Company's sales force, with the lease terms ranging from 18 to 48 months. As of March 31, 2018, the aggregate rent payable over the remaining lease term of the vehicle lease agreement was approximately $1.4 million. Rent expense relating to the lease of cars for the three months ended March 31, 2018 and March 31, 2017 was $0.5 million and $0.8 million, respectively.

Legal Matters

Depomed v. NUCYNTA and NUCYNTA ER ANDA Filers

Actavis & Alkem: In July 2013, Janssen Pharma filed patent infringement lawsuits in the U.S. District Court for the District of New Jersey (D.N.J.) against Actavis Elizabeth LLC, Actavis Inc. and Actavis LLC (collectively, Actavis), as well as Alkem Laboratories Limited and Ascend Laboratories, LLC (collectively, Alkem). The patent infringement claims against Actavis and Alkem relate to their respective ANDAs seeking approval to market generic versions of NUCYNTA and NUCYNTA ER before the expiration of U.S. Reissue Patent No. 39,593 (the '593 Patent), U.S. Patent No. 7,994,364 (the '364 Patent) and, as to Actavis only, U.S. Patent No. 8,309,060 (the '060 Patent). In December 2013, Janssen Pharma filed an additional complaint in the D.N.J. against Alkem asserting that newly issued U.S. Patent No. 8,536,130 (the '130 Patent) was also infringed by Alkem's ANDA seeking approval to market a generic version of NUCYNTA ER. In August 2014, Janssen Pharma amended the complaint against Alkem to add additional dosage strengths.

Sandoz & Roxane: In October 2013, Janssen Pharma received a Paragraph IV Notice from Sandoz, Inc. (Sandoz) with respect to NUCYNTA related to the '364 Patent, and a Paragraph IV Notice from Roxane Laboratories, Inc. (Roxane) with respect to NUCYNTA related to the '364 and '593 Patents. In response to those notices, Janssen Pharma filed an additional complaint in the D.N.J. against Roxane and Sandoz asserting the '364 Patent against Sandoz and the '364 and '593 Patents against Roxane. In April 2014, Janssen Pharma and Sandoz entered into a joint stipulation of dismissal of the case against Sandoz, based on Sandoz's agreement not to market a generic version of NUCYNTA

products prior to the expiration of the asserted patents. In June 2014, in response to a new Paragraph IV Notice from Roxane with respect to NUCYNTA ER, Janssen Pharma filed an additional complaint in the D.N.J. asserting the ’364, ’593, and ’130 Patents against Roxane.

Watson: In July 2014, in response to a Paragraph IV Notice from Watson Laboratories, Inc. (Watson) with respect to the NUCYNTA oral solution product and the ’364 and ’593 Patents, Janssen Pharma filed a lawsuit in the D.N.J. asserting the ’364 and ’593 Patents against Watson.

In each of the foregoing actions, the ANDA filers counterclaimed for declaratory relief of non-infringement and patent invalidity. At the time that the actions were commenced, Janssen Pharma was the exclusive U.S. licensee of the patents referred to above. On April 2, 2015, the Company acquired the U.S. rights to NUCYNTA ER and NUCYNTA from Janssen Pharma. As part of the acquisition, the Company became the exclusive U.S. licensee of the patents referred to above. The Company was added as a plaintiff to the pending cases and is actively litigating them.

In September 2015, the Company filed an additional complaint in the D.N.J. asserting the ’130 Patent against Actavis. The ’130 Patent issued in September 2013 and was timely listed in the Orange Book for NUCYNTA ER, but Actavis did not file a Paragraph IV Notice with respect to this patent. In its new lawsuit, the Company claimed that Actavis would infringe or induce infringement of the ’130 Patent if its proposed generic products were approved. In response, Actavis counterclaimed for declaratory relief of non-infringement and patent invalidity, as well as an order requiring the Company to change the corrected use code listed in the Orange Book for the ’130 Patent.

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In February 2016, Actavis, Actavis UT, Roxane and Alkem each stipulated to infringement of the ’593 and ’364 patents. On March 9, 2016, a two-week bench trial on the validity of the three asserted patents and infringement of the ’130 patent commenced. Closing arguments took place on April 27, 2016. On September 30, 2016, the Court issued its final decision. The Court found that the ’593, ’364 patent, and ’130 patents are all valid and enforceable, that Alkem will induce infringement of the ’130 patent, but that Roxane and Actavis will not infringe the ’130 patent.

On April 11, 2017, the Court entered final judgment in favor of the Company on the validity and enforceability of all three patents, on infringement of the ’593 and ’364 Patents by all defendants, and on infringement of the ’130 Patent against Alkem. The judgment includes an injunction enjoining all three defendants from engaging in certain activities with regard to tapentadol (the active ingredient in NUCYNTA), and ordering the effective date of any approval of Actavis, Actavis UT, and Roxane’s ANDAs, and Alkem’s ANDA for NUCYNTA IR to be no earlier than the expiry of the ’364 Patent (June 27, 2025), and the effective date of any approval of Alkem’s ANDA for NUCYNTA ER to be no early than the expiry of the ’130 Patent (September 22, 2028). The period of exclusivity with respect to all four defendants may in the future be extended with the award of pediatric exclusivity.

Notices of appeal were filed by defendants Alkem and Roxane concerning the validity of the ’364 and ’130 patents. The Company filed its own cross-appeal with regard to the Court’s finding that Roxane and Actavis will not infringe the claims of the ’130 Patent. The appeals have been consolidated at the Federal Circuit. Briefing concluded in March 2018. It is estimated that the Federal Circuit will hold oral argument by late summer 2018 and issue a written decision by the end of 2018. The ’593 patent is not the subject of any appeals.

Depomed v. Purdue

The Company has sued Purdue Pharma L.P (Purdue) for patent infringement in a lawsuit filed in January 2013 in the U.S. District Court for the District of New Jersey. The lawsuit arises from Purdue’s commercialization of reformulated OxyContin® (oxycodone hydrochloride controlled-release) in the U.S. and alleges infringement of U.S. Patent Nos. 6,340,475 (the ‘475 Patent) and 6,635,280 (the ‘280 Patent), which expired in September 2016.

On September 28, 2015, the district court stayed the Purdue lawsuit pending the decision of the U.S. Court of Appeals for the Federal Circuit (CAFC) in Purdue’s appeal of the PTAB’s Final Written Decisions described below. On June 30, 2016, the district court lifted the stay based on the CAFC’s opinion and judgment affirming the PTAB’s Final Written Decisions confirming the patentability of the patent claims of the ‘475 and ‘280 Patents Purdue had challenged. On June 10, 2016, the Company filed a motion for leave to file a second amended Complaint to plead willful infringement. On June 21, 2016, Purdue filed an opposition to the Company’s motion for leave to plead willful infringement. On January 31, 2017, the Court granted the Company’s motion for leave to plead willful infringement.

On February 1, 2017, the Company filed a Second Amended Complaint pleading willful infringement. On July 10, 2017, the case was reassigned to Judge Wolfson. On February 15, 2017, Purdue answered the Company’s Second Amended Complaint and pled counterclaims of non-infringement, invalidity, unenforceability and certain affirmative defenses. On September 26, 2017, the case was reassigned to Judge Martinotti. On December 22, 2017, the Court set the close of expert discovery for March 30, 2018. On January 5, 2018, the Court vacated the January 25, 2018 pretrial

conference. No trial dates have been set by the Court, though the Company expects a bench trial on Purdue's claim of inequitable conduct and a jury trial may be scheduled in the second half of 2018.

In response to petitions filed by Purdue, the PTAB instituted IPRs of certain of the claims asserted in the Company's lawsuit against Purdue. In the IPRs initiated by Purdue, in July 2014, the PTAB declined to institute an IPR as to two claims of the '475 patent and two claims of the '280 Patent. The PTAB instituted an IPR as to the other 15 claims of the '475 Patent and as to the other ten claims of the '280 Patent asserted against Purdue. In July 2015, the PTAB issued Final Written Decisions confirming the patentability of all claims at issue. In March 2016, following Purdue's appeal of the PTAB's decisions, the CAFC affirmed the PTAB's Final Written Decisions.

Depomed v. Strides Pharma Inc. and Strides Pharma Global Pte Limited

On May 5, 2017, the Company filed suit in the U.S. District Court for the District of New Jersey against Strides Pharma Inc. and Strides Pharma Global Pte Limited (collectively, Strides) based on Strides' filing of an ANDA to market a generic version of ZIPSOR prior to the expiration of U.S. Patent Nos. 7,662,858; 7,884,095; 7,939,518; 8,110,606; 8,623,920; and 9,561,200 (the patents-in-suit). By letter dated March 27, 2017, Strides informed the Company that it had filed an ANDA for a generic version of ZIPSOR with Paragraph IV certifications against each of

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the patents-in-suit. The Company's filing of the complaint against Strides resulted in an automatic 30-month stay of FDA approval of Strides' ANDA, lasting until September 2019.

On August 11, 2017, the Company and the defendants reached a settlement of the case that permits Strides to begin selling their generic version of ZIPSOR in September 2022, or earlier in certain circumstances. In accordance with applicable legal requirements, the Company and Strides submitted the ZIPSOR settlement agreement to the United States Federal Trade Commission and United States Department of Justice for review. The ZIPSOR settlement agreement provides for a full settlement and release by both the Company and Strides of all claims that were or could have been asserted in the litigation and that arise out of the issues that were the subject of the litigation or Strides' generic version of ZIPSOR.

Previously, in July 2013, the Company filed suit against Banner Pharmacaps Inc. (Banner) and Watson Laboratories, Inc. (Watson) based on Banner's filing of an ANDA for a generic version of ZIPSOR. The Company and the defendants reached a settlement of the case that permits Watson to begin selling their generic version of ZIPSOR on March 24, 2022, or earlier under certain circumstances. The Company believes that Banner and Watson may be entitled to 180-day exclusivity with respect to generic ZIPSOR.

Securities Class Action Lawsuit

On August 23, 2017, the Company, its current chief executive officer and president, its former chief executive officer and president, and its current chief financial officer were named as defendants in a purported federal securities law class action filed in the United States District Court for the Northern District of California (Huang v. Depomed et al., No. 3:17-cv-04830-JST, N.D. Cal.). The action alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended, and Rule 10b-5 relating to certain prior disclosures of the Company about its business, compliance, and operational policies; and practices concerning the sales and marketing of its opioid products. The plaintiff, who seeks to represent a class consisting of all purchasers of Company common stock between February 26, 2015 and August 7, 2017, contends that the conduct supporting the alleged violations affected the value of Company common stock and is seeking damages and other relief. On December 8, 2017, the "Depomed Investor Group" was appointed lead plaintiff. On February 6, 2018, the lead plaintiff filed an amended complaint that asserted the same claims arising out of the same and similar disclosures against the Company and the same individuals as were involved in the original complaint. The Company and the individuals filed a motion to dismiss the amended complaint on April 9, 2018. The lead plaintiff must oppose the motion by June 8, 2018. The Company and the individuals must then file a reply in support of their motion to dismiss by July 23, 2018. The Company believes that the action is without merit and intends to contest it vigorously.

In addition, three shareholder derivative actions were filed on behalf of the Company and purport to assert claims by the Company against its officers and directors for breach of fiduciary duty, arising out of the same factual allegations as the class action. Two of these actions were filed in the Northern District of California, the first on November 10, 2017 (Solak v. Higgins et al., No. 3:17-cv-06546-JST) and the second on November 15, 2017 (Ross v. Fogarty et al.,

No. 3:17-cv-06592-JST). The third derivative action was filed in the Superior Court of California, Alameda County (Singh v. Higgins, et al., RG17877280) on September 29, 2017. On December 7, 2017, the plaintiffs in Solak v. Higgins, et al. voluntarily dismissed the first federal derivative action. And, on January 18, 2018 and January 23, 2018, respectively, the remaining federal and state derivative actions were stayed pending the resolution of the motion to dismiss in the securities class action. The Company believes that these actions are without merit and intends to contest them vigorously.

Opioid-Related Request and Subpoenas

In March 2017, the Company, and a number of other pharmaceutical companies, received a request for information from the ranking minority member of the United States Senate Committee on Homeland Security and Governmental Affairs related to the promotion of opioids. The Company has voluntarily furnished information responsive to such request.

The Company, like a number of other pharmaceutical companies, has received subpoenas or civil investigative demands in connection with our prior sales and marketing of opioid products. We have received subpoenas or civil investigative demands from the Attorneys General of Kentucky, Maryland, Missouri, Montana, New Jersey and Washington seeking documents and information in connection with our prior sales and marketing of opioid products. We

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are cooperating with each of the foregoing states in their investigations. We have also received subpoenas from the U.S. Department of Justice (DOJ) seeking documents and information in connection with our prior sales and marketing of opioid products. We are cooperating with the DOJ in its investigation. The Company also from time to time receives and complies with subpoenas from governmental authorities related to investigations primarily directed at third parties, including health care practitioners, pursuant to which the Company's records related to agreements with and payments made to those third parties, among other items, are produced.

Multidistrict Opioid Litigation

A number of pharmaceutical manufacturers, distributors and other industry participants have been named in numerous lawsuits around the country brought by various groups of plaintiffs, including city and county governments, hospitals and others. In general, the lawsuits assert claims arising from defendants' manufacturing, distributing, marketing and promoting of FDA-approved opioid drugs. The specific legal theories asserted vary from case to case, but most of the lawsuits include federal and state statutory claims as well as claims arising under state common law. Plaintiffs seek various forms of damages, injunctive and other relief and attorneys' fees and costs.

For such cases filed in or removed to federal court, the Judicial Panel on Multi-District Litigation issued an order in December 2017, establishing a Multi-District Litigation court (MDL Court) in the Northern District of Ohio (In re National Prescription Opiate Litigation, Case No. 1:17-MD-2804). Since that time, more than 600 such cases that were originally filed in U.S. District Courts, or removed to federal court from state court, have been transferred to the MDL Court. The Company is currently involved in five lawsuits that have been transferred to the MDL Court. Plaintiffs may file additional lawsuits in which the Company may be named. Plaintiffs in these cases are municipalities, health clinics and health insurance providers who assert federal and state statutory claims and state common law claims, such as conspiracy, nuisance, fraud, negligence or deceptive trade practices. In these cases, plaintiffs seek a variety of forms of relief, including actual damages to compensate for alleged past and future costs to provide care and services to persons with opioid-related addiction or related conditions, injunctive relief to prohibit alleged deceptive marketing practices and abate an alleged nuisance, establishment of a compensation fund, punitive damages, attorneys' fees and costs. These lawsuits are in the earliest stages of proceedings, and the Company intends to defend itself vigorously in these matters.

State Opioid Litigation

Related to the cases in the MDL Court noted above, there have been over 100 similar lawsuits filed in state courts around the country, in which various groups of plaintiffs assert opioid-drug related claims against similar groups of defendants. The Company is named in two such cases, one in Arkansas and one in Pennsylvania. Plaintiffs may file additional lawsuits in which the Company may be named. In these cases, plaintiffs are asserting state common law and statutory claims against the defendants similar in nature to the claims asserted in the MDL cases. Plaintiffs are seeking past and future damages, injunctive relief, and punitive and statutory treble damages. These lawsuits are likewise in their earliest stages, and the Company intends to defend itself vigorously in these matters.

General

The Company cannot reasonably predict the outcome of the legal proceedings described above, nor can the Company estimate the amount of loss, range of loss or other adverse consequence, if any, that may result from these proceedings or the amount of any gain in the event we prevail in litigation involving a claim for damages. As such the Company is not currently able to estimate the impact of the above litigation on its financial position or results of operations.

The Company may from time to time become party to actions, claims, suits, investigations or proceedings arising from the ordinary course of our business, including actions with respect to intellectual property claims, breach of contract claims, labor and employment claims and other matters. The Company may also become party to further litigation in federal and state courts relating to opioid drugs. Although actions, claims, suits, investigations and proceedings are inherently uncertain and their results cannot be predicted with certainty, other than the matters set forth above, the Company is not currently involved in any matters that the Company believes may have a material adverse effect on its business, results of operations or financial condition. However, regardless of the outcome, litigation can have an adverse impact on the Company because of associated cost and diversion of management time.

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NOTE 13. ACQUISITIONS

Asset Purchase Agreement with Slán

On November 7, 2017, the Company entered into an Asset Purchase Agreement (the Asset Purchase Agreement) with Slán Medicinal Holdings Limited (Slán) under which the Company acquired a license to market the specialty drug, cosyntropin in the United States and Canada. The term of the License Agreement runs from November 7, 2017, through the end of the 10-year period following the first commercial sale of an approved product (Licensed Product), but the Company may terminate the License Agreement if the FDA determines that a Licensed Product is not approvable in the U.S. Under the terms of the Agreement, Slán is responsible for clinical and regulatory expenses associated with cosyntropin prior to its first approval by the U.S. Food and Drug Administration. Upon approval, the Company will be responsible for marketing and selling cosyntropin for the first seven years following the first commercial sale of a Licensed Product in the U.S., and Slán will be responsible for selling the Licensed Product during the remaining three years of the 10-year period.

The acquisition of cosyntropin was treated as an asset acquisition under the applicable guidance contained with U.S. GAAP. The fair value of the license to market cosyntropin was estimated to be approximately $24.9 million which, in accordance with the applicable accounting rules, was recorded as “acquired in process research and development” during the fourth quarter of 2017, as cosyntropin is still under development and the rights the Company acquired were deemed to have no alternative future use.

As consideration for this acquisition, the Company provided the seller all of the rights and obligations, as defined under the arrangement, associated with Lazanda and together with $5.0 million in cash to Slán. The divestiture of Lazanda was treated as a disposition of a business for accounting purposes and resulted in a gain of approximately $17.1 million which was recorded as “gain on divestiture of Lazanda” in the Company’s 2017 consolidated statements of operations. The Company determined that the divestiture of Lazanda does not qualify for reporting as discontinued operations as the divestiture does not constitute on its own a strategic shift that will have a major effect on Depomed’s operations and financial results.

The Cebranopadol Acquisition

On November 17, 2015, the Company entered into a definitive agreement to acquire the U.S. and Canadian rights to cebranopadol and its related follow-on compound from Grünenthal. The acquisition was completed on December 30, 2015.

Under the terms of the acquisition agreement, Depomed entered into a settlement agreement with Endo Pharmaceuticals, Inc., a subsidiary of Endo International Plc (Endo) to resolve Depomed's ongoing patent litigation against Endo for alleged infringement of three of the Company’s patents by Endo's OPANA® ER product (the Settlement). As the formulator of OPANA® ER, Grünenthal indemnified Endo for certain intellectual property matters, including the Company’s ongoing patent infringement lawsuit against Endo. The settlement agreement granted Endo a non-exclusive patent license in the United States, and a covenant not to sue outside the United States, for the currently marketed form of OPANA® ER. In addition, the Company provided Grünenthal with a limited covenant not to sue under certain of the Company’s Acuform® drug delivery patents with specific drug substances as well as $25 million in cash. The Company also agreed to pay Grünenthal royalties on net sales and one-time net sales milestones. There are no clinical, regulatory or approval contingent milestone payments.

The cebranopadol acquisition was treated as an asset acquisition under the applicable guidance contained with U.S. GAAP. Accordingly, the total purchase consideration of $54.9 million was expensed to research and development expenses. The total expense of $54.9 million consists of $25.0 million paid in cash upon the closing of the acquisition and $29.9 million reflecting a one-time accounting adjustment to recognize the total non-cash fair value of each of the elements of the Settlement reached with Endo. The $29.9 million was recorded as income within “Non-cash gain on settlement agreement” and as an additional expense within “acquired in-process research and development” in the Company’s 2015 consolidated statements of operations. Significant judgments were used in determining the estimated fair values assigned to the elements of the Settlement, such as but not limited to, the probability of the Company succeeding in its litigation against Endo had the litigation not been resolved, estimates of royalty rates and any damages that may have been awarded by the court, the timing of such an award and estimates of appropriate discount rates used to

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present value these expected future net cash flows. An actual judgment awarded by the court may have differed materially from the amounts recorded.

In January 2018, the Company gave 120 days' written notice of termination to Grünenthal of the cebranopadol license agreement.

The NUCYNTA Acquisition

On January 15, 2015, the Company, entered into an asset purchase agreement pursuant to which the Company acquired from Janssen and its affiliates the U.S. rights to the NUCYNTA franchise of pharmaceutical products (the NUCYNTA U.S. Product Rights) as well as certain related assets for $1.05 billion in cash (the Purchase Price).

The NUCYNTA franchise includes NUCYNTA ER (tapentadol) extended release tablets indicated for the management of pain, including neuropathic pain associated with diabetic peripheral neuropathy (DPN), severe enough to require daily, around-the-clock, long-term opioid treatment, NUCYNTA (tapentadol), an immediate release version of tapentadol, for management of moderate to severe acute pain in adults, and NUCYNTA (tapentadol) oral solution, an approved oral form of tapentadol that has not been commercialized (collectively, the Products).

Upon the consummation of the transaction on April 2, 2015, the Company acquired (i) rights to commercialize the Products in the United States, and (ii) certain other assets relating to the Products, including finished goods product inventory and certain manufacturing equipment. In addition, Janssen Pharma assigned to the Company all of its rights and obligations under the License Agreement (U.S.) (the License Agreement) by and among Janssen Pharma, Janssen Research & Development, LLC and Grünenthal GmbH (Grünenthal) pursuant to which Janssen has a royalty-bearing license to certain Grünenthal patents and other intellectual property rights covering the commercialization of the Products in the United States.

In connection with the transaction, the Company assumed responsibility for the ongoing legal proceedings relating to certain of the Grünenthal patents licensed under the License Agreement and Janssen Pharma's clinical obligations relating to the Products and will be responsible for the associated post acquisition costs. Other than as set forth in the Asset Purchase Agreement, Janssen Pharma retained all liabilities relating to the Products associated with Janssen Pharma's commercialization of the Products prior to the consummation of the transaction.

In connection with the Transaction, the Company, Janssen Pharma and certain affiliates of Janssen also entered into (i) supply agreements pursuant to which Janssen Pharma will manufacture and supply the Products to the Company until the Company, or its contract manufacturer, begins commercial production of the Products, following which the

Company will manufacture and supply Janssen Pharma for its requirements for NUCYNTA outside of the United States and (ii) a supply agreement pursuant to which an affiliate of Janssen will manufacture and supply the Company with the active pharmaceutical ingredient contained in the Products.

In connection with the consummation of the transaction, on April 2, 2015, the Company sold an aggregate of $575.0 million principal amount of the Senior Notes for gross proceeds of approximately $562.0 million. The Company used $550.0 million of the net proceeds received upon the sale of the Senior Notes to fund a portion of the Purchase Price paid to Janssen Pharma.

Pursuant to ASC Topic 805, Business Combinations, the Transaction was determined to be a business combination and was accounted for using the acquisition method of accounting. The following table presents a summary of the purchase price consideration for the Transaction:

(in thousands)	
Cash Paid	$ 1,050,000
Rebates payable by Seller	(9,977)
Total Purchase Consideration	$ 1,040,023

The rebates payable by Janssen Pharma represent a reduction to the total purchase consideration. The fair value of the rebates payable by Janssen Pharma was determined based on estimates that take into consideration the terms of agreements with customers, historical rebates taken, and the estimated amount of time it takes the product to flow through the distribution channel. The actual amount of rebates paid by Janssen Pharma, determined in the fourth quarter

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of 2015, was approximately $0.5 million lower than the Company's estimate of $10.5 million recorded as of the acquisition date. Consequently, the total purchase consideration and the fair value of the NUCYNTA U.S. Product Rights was increased by $0.5 million.

Under the acquisition method of accounting, we have recognized net tangible and intangible assets acquired based upon their respective estimated fair values as of the acquisition date. The table below shows the fair values assigned to the assets acquired:

(in thousands)	
NUCYNTA U.S. Product Rights	$ 1,019,978
Inventories	11,590
Manufacturing Equipment	8,455
	$ 1,040,023

The fair value of inventories acquired included a step-up in the value of NUCYNTA inventories of $5.9 million that was fully amortized to cost of sales in 2015 as the acquired inventories were sold. The Company incurred non-recurring transaction costs of $12.3 million in 2015 with respect to the NUCYNTA Acquisition which were recorded in "Selling, general and administrative expense" within the Company's Consolidated Statement of Operations.

NUCYNTA U.S. Product Rights

The valuation of the NUCYNTA U.S. Product Rights was based on management's estimates, information and reasonable and supportable assumptions. This estimated fair value was determined using the income approach under the discounted cash flow method. Significant assumptions used in valuing the NUCYNTA U.S. Product Rights included revenue projections based on assumptions relating to pricing and reimbursement rates, market size and market penetration rates, general and administrative expenses, sales and marketing expenses, research and development expenses for clinical and regulatory support and developing an appropriate discount rate. If the Company's assumptions are not correct, there could be an impairment loss or, in the case of a change in the estimated useful life of the asset, a change in amortization expense. The NUCYNTA U.S. Product Rights intangible asset is amortized using the straight-line method over an estimated useful life of approximately ten years. The estimated useful life was determined based on the period of time over which the NUCYNTA U.S. Product Rights are expected to contribute to the Company's future cash flows.

NOTE 14. INTANGIBLE ASSETS

The gross carrying amounts and net book values of our intangible assets were as follows (in thousands):

	March 31, 2018				December 31, 2017		
Product rights	Remaining Useful Life (In years)	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
NUCYNTA	7.7	$ 1,019,978	$ (290,165)	$ 729,813	$ 1,019,978	$ (266,590)	$ 753,388
CAMBIA	5.7	51,360	(22,039)	29,321	51,360	(20,755)	30,605
Zipsor	4.0	27,250	(17,955)	9,295	27,250	(17,370)	9,880
Total		$ 1,098,588	$ (330,159)	$ 768,429	$ 1,098,588	$ (304,715)	$ 793,873

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Based on finite-lived intangible assets recorded as of March 31, 2018, and assuming the underlying assets will not be impaired and that we will not change the expected lives of the assets, future amortization expenses were estimated as follows (in thousands):

Year Ending December 31,	Estimated Amortization Expense
2018 (remainder)	$ 76,330
2019	101,774
2020	101,774
2021	101,774
2022	99,969
Thereafter	286,808
Total	$ 768,429

NOTE 15. RESTRUCTURING CHARGES

In June 2017, the Company announced a limited reduction-in-force in order to streamline operations and achieve operating efficiencies, the activities related to that reduction-in-force were completed during the third quarter of 2017. In December 2017, the Company initiated a company-wide restructuring plan following the entry into the Commercialization Agreement with Collegium. This plan focused on a reduction of the Company's pain sales force during the first quarter of 2018, a reduction of the staff at its headquarters office by mid-2018 and a move from its headquarters facility in Newark, California to Lake Forest, Illinois sometime in mid-2018.

The following table summarizes the total expenses recorded related to the 2017 restructuring and one-time termination cost activities by type of activity and the locations recognized within the consolidated statements of operations as restructuring costs (in thousands):

	Three Months Ended March 31,	
	2018	2017
Employee compensation costs	$ 8,779	$ —
Other exit costs	238	—
Total restructuring costs	$ 9,017	$ —

Selected information relating to accrued restructuring, severance costs and one-time termination costs is as follows (in thousands):

	Employee compensation costs	Other exit costs	Total
Balance at December 31, 2017	$ 9,483	$ —	$ 9,483
Net accruals	8,779	238	9,017
Non-cash reductions	(258)	—	(258)
Cash paid	(11,184)	(238)	(11,422)
Balance at March 31, 2018	$ 6,820	$ -	$ 6,820

As of March 31, 2018, the full $6.8 million accrued restructuring liability balance was classified as a current liability in the Condensed Consolidated Balance Sheet. The Company has incurred $18.5 million in related restructuring costs since the announcement of the plan in December 2017 through March 31, 2018. The Company expects to incur additional related restructuring costs of $9.0 million to $12.0 million through June 30, 2019.

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NOTE 16. OUT OF PERIOD ADJUSTMENT

During the three months ended March 31, 2017, the Company identified that it had understated the amount payable for the Branded Prescription Drug fee (BPD) relating to net sales of the NUCYNTA franchise since its acquisition in the second quarter of 2015. Accordingly, the Company recorded an adjustment during the three months ended March 31, 2017 to increase its BPD accrual relating to the net sales of the NUCYNTA franchise in the cumulative amount of $3.4 million of which $1.4 million and $2.0 million related to the years ended December 31, 2015 and 2016, respectively. This adjustment resulted in an increase in loss per share by $0.05 in the three months ended March 31, 2017. In accordance with the relevant guidance, management evaluated the materiality of the error from a qualitative and quantitative perspective. Based on such evaluation, we concluded that correcting the cumulative error would not be material to the expected full year results for 2017, and correcting the error would not have had a material impact on any individual prior period financial statements or affect the trend of financial results.

NOTE 17. SUBSEQUENT EVENTS

The following subsequent events occurred in May 2018:

The Company amended its existing licensing agreement with Applied Pharma Research S.A. to in-license a new presentation of Cambia. The Company expects to pay an initial fee of $1.25 million with royalties and milestones payable based on certain sales thresholds. The Company expects to file for FDA approval of this new Cambia presentation in 2019 and, if approved, this presentation would provide patent protection through at least 2026.

The Company also entered into a new co-promotion relationship with Allegis Pharmaceuticals, LLC (Allegis) for Zipsor. Under the terms of the agreement, beginning in June 2018, Allegis will supplement the Company’s existing sales force outreach by adding approximately 30 new sales reps that focus exclusively on primary care physicians in targeted geographic regions.

The Company’s shareholders approved a change in the Company's state of incorporation from California to Delaware (the Reincorporation). The Reincorporation would be effectuated pursuant to the terms of a merger agreement providing for the Company to merge into a newly formed, wholly-owned subsidiary of the Company incorporated in the State of Delaware. The shareholders also approved a proposal to change the name of the Company after Reincorporation to Assertio Therapeutics, Inc. The Company expects that these changes will be implemented in the third quarter of 2018.

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

FORWARD-LOOKING INFORMATION

Statements made in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this Quarterly Report on Form 10-Q that are not statements of historical fact are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). We have based these forward-looking statements on our current expectations and projections about future events. Our actual results could differ materially from those discussed in, or implied by, these forward-looking statements. Forward-looking statements are identified by words such as "believe," "anticipate," "expect," "intend," "plan," "will," "may" and other similar expressions. In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances are forward-looking statements. Forward-looking statements include, but are not necessarily limited to, those relating to:

- the commercial success and market acceptance of our products;
- the success of Collegium Pharmaceutical, Inc. (Collegium) in commercializing NUCYNTA® ER and NUCYNTA®;
- the reversal or any successful appeal of the court's favorable ruling in our patent infringement litigation against the filers of Abbreviated New Drug Applications (each, an ANDA) to market generic versions of NUCYNTA ER and NUCYNTA in the United States (U.S.);
- any additional patent infringement or other litigation, investigation or proceeding that may be instituted related to us or any of our products, product candidates or products we may acquire;
- our ability to generate sufficient cash flow from our business to make payments on our indebtedness and our compliance with the terms and conditions of the agreements governing our indebtedness;
- our and our collaborative partners' compliance or non-compliance with legal and regulatory requirements related to the development or promotion of pharmaceutical products in the U.S.;
- our plans to acquire, in-license or co-promote other products;
- the results of our research and development efforts including clinical studies relating to our product candidates, including cosyntropin;
- submission, acceptance and approval of regulatory filings;
- our ability to raise additional capital, if necessary;
- our ability to successfully develop and execute our sales and marketing strategies;
- our collaborative partners' compliance or non-compliance with obligations under our collaboration agreements;
- the outcome of our ongoing patent infringement litigation against Purdue Pharma L.P. (Purdue);
- the outcome of our opioid-related investigations and litigation;
- the successful execution of our restructuring plan that was announced in December 2017; and
- our ability to attract and retain key executive leadership following our restructuring and office relocation.

Factors that could cause actual results or conditions to differ from those anticipated by these and other forward-looking statements include those more fully described in the “RISK FACTORS” section and elsewhere in this Quarterly Report on Form 10-Q. Except as required by law, we assume no obligation to update any forward-looking statement publicly, or to revise any forward-looking statement to reflect events or developments occurring after the date of this Quarterly Report on Form 10-Q, even if new information becomes available in the future. Thus, you should not assume that our silence over time means that actual events are bearing out as expressed or implied in any such forward-looking statement.

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COMPANY OVERVIEW

Depomed is a specialty pharmaceutical company focused on pain and other central nervous system (CNS) conditions. Our current specialty pharmaceutical business includes the following three products which we market in the United States (U.S.):

- Gralise® (gabapentin), a once daily product for the management of postherpetic neuralgia (PHN), that we launched in October 2011.

- CAMBIA® (diclofenac potassium for oral solution), a non-steroidal anti-inflammatory drug for the acute treatment of migraine attacks, that we acquired in December 2013.

- Zipsor® (diclofenac potassium) liquid filled capsules, a non-steroidal anti-inflammatory drug for the treatment of mild to moderate acute pain, that we acquired in June 2012.

In January 2018, pursuant to the terms of a Commercialization Agreement we entered into with Collegium Pharmaceutical, Inc. (Collegium) in December 2017, we granted Collegium the right to commercialize the NUCYNTA® franchise of pain products in the U.S. Pursuant to the Commercialization Agreement, Collegium assumed all commercialization responsibilities for the NUCYNTA franchise effective January 9, 2018, including sales and marketing. We will receive a royalty on all NUCYNTA revenues based on certain net sales thresholds, with a minimum royalty of $132.0 million for the year ended December 31, 2018 and $135.0 million per year for the years ended December 31, 2019 to December 31, 2021, subject to certain conditions. Additionally, we retained certain rights to co-promote NUCYNTA products, subject to providing advanced notice to Collegium. The NUCYNTA franchise includes two products currently marketed in the U.S. by Collegium:

- NUCYNTA® ER (tapentadol extended release tablets), a product for the management of pain severe enough to require daily, around the clock, long term opioid treatment, including neuropathic pain associated with diabetic peripheral neuropathy (DPN) in adults, and for which alternate treatment options are inadequate; and

- NUCYNTA® IR (NUCYNTA) (tapentadol), an immediate release version of tapentadol for the management of moderate to severe acute pain in adults.

In November 2017, we entered into definitive agreements with Slán Medicinal Holdings Limited and certain of its affiliates (Slán) pursuant to which we acquired Slán’s rights to market the specialty drug cosyntropin (Synthetic ACTH Depot) in the U.S. and Canada, and Slán acquired our rights to Lazanda® (fentanyl) nasal spray. We believe cosyntropin can be second-to-market behind Mallinckrodt plc's marketed product, H-P Acthar gel. We expect Slán to file a New Drug Application (NDA) for cosyntropin in late 2018 with a goal of a potential launch in the second half of 2019 or early 2020, if the product is approved.

We actively seek to expand our product portfolio through acquiring or in licensing commercially available products or late stage product candidates that may be marketed and sold effectively through our sales and marketing capability.

We also have royalty and milestone producing license arrangements based on our proprietary Acuform® gastroretentive drug delivery technology, including with Ironwood Pharmaceuticals, Inc. (Ironwood).

Strategy

Our commercial strategy is based on three pillars: Maintain, Grow and Build.

We intend to “Maintain” our NUCYNTA franchise of pain products through our commercialization arrangement with Collegium. In January 2018, pursuant to the terms of a Commercialization Agreement we entered into with Collegium in December 2017, we granted Collegium the right to commercialize the NUCYNTA franchise of pain products in the U.S. Pursuant to the Commercialization Agreement, Collegium assumed all commercialization responsibilities for the NUCYNTA franchise effective January 9, 2018, including sales and marketing. We will receive a royalty on all NUCYNTA revenues based on certain net sales thresholds, with a minimum royalty of $135.0 million per year during the first four years of the agreement, subject to certain conditions. Both we and Collegium may terminate the

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agreement under certain circumstances. We can terminate the agreement if aggregate net sales of the NUCYNTA products fall below certain thresholds or within the first year upon the payment of a termination fee. Collegium may terminate at any time after the first anniversary of the transaction by giving 12 months' notice and, if the termination date is prior to the fourth anniversary of the transaction, by paying us a $25.0 million termination fee.

We intend to "Grow" our neurology and non-opioid pain franchises, through organic and inorganic growth. As of September 2017, we increased the size of our neurology field force to 90 representatives and, in doing so, doubled our call plan targets. We believe our increased field force supports Gralise, Cambia and Zipsor, three promotionally sensitive products, and allows us the flexibility to add new neurology products.

We intend to "Build" a portfolio of high-value products positioned to address the needs of patients, physicians and payers. In November 2017 we acquired the exclusive rights to market cosyntropin in the U.S. and Canada. We will seek to bring additional specialty products into this portfolio.

In connection with our entry into the Commercialization Agreement with Collegium, we eliminated our pain sales force and announced our intent to relocate our headquarters and reduce our headquarters' staff. Excluding restructuring charges we expect these actions will significantly reduce our operating expenses in future periods, further enabling us to implement our strategy.

OUR BUSINESS OPERATIONS

As of March 31, 2018, our revenues were generated primarily from the following commercialized products.

Gralise (Gabapentin)

Gralise is our proprietary, once daily formulation of gabapentin indicated for management of PHN, a persistent pain condition caused by nerve damage during a shingles, or herpes zoster, viral infection. We made Gralise commercially available in October 2011, following its U.S. Food and Drug Administration (FDA) approval in January 2011. The FDA has granted Orphan Drug exclusivity for PHN. Gralise product sales were $14.8 million and $17.6 million for the three months ended March 31, 2018 and 2017, respectively.

CAMBIA (Diclofenac Potassium for Oral Solution)

CAMBIA is a non-steroidal anti-inflammatory drug (NSAID) indicated for the acute treatment of migraine attacks with or without aura in adults 18 years of age or older. We acquired CAMBIA in December 2013 from Nautilus Neurosciences, Inc. (Nautilus).

We began shipping and recognizing product sales on CAMBIA in December 2013. Our CAMBIA product sales were $6.4 million and $7.2 million for the three months ended March 31, 2018 and 2017, respectively.

Zipsor (Diclofenac Potassium) Liquid Filled Capsules

Zipsor is an NSAID indicated for relief of mild to moderate acute pain in adults. Zipsor uses proprietary ProSorb® delivery technology to deliver a finely dispersed, rapidly absorbed formulation of diclofenac. We acquired Zipsor on June 21, 2012 from Xanodyne Pharmaceuticals, Inc. (Xanodyne).

Our Zipsor® product sales were $4.7 million and $4.7 million for the three months ended March 31, 2018 and 2017, respectively.

NUCYNTA ER (Tapentadol Extended Release Tablets)

NUCYNTA ER is an extended release version of tapentadol that is indicated for the management of pain severe enough to require daily, around the clock, long term opioid treatment, including neuropathic pain associated with DPN in adults, and for which alternate treatment options are inadequate. We acquired the U.S. rights to NUCYNTA ER from Janssen Pharmaceuticals, Inc. (Janssen Pharma) and began shipping and recognizing product sales on NUCYNTA ER in April 2015. We began commercial promotion of NUCYNTA ER in June 2015.

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NUCYNTA (Tapentadol)

NUCYNTA is an immediate release version of tapentadol that is indicated for the management of moderate to severe acute pain in adults. We acquired the U.S. rights to NUCYNTA from Janssen Pharma and began shipping and recognizing product sales on NUCYNTA in April 2015. We began commercial promotion of NUCYNTA in June 2015.

In January 2018, pursuant to the terms of a Commercialization Agreement we entered into with Collegium in December 2017, we granted Collegium the right to commercialize the NUCYNTA franchise of pain products in the U.S. Pursuant to the Commercialization Agreement, Collegium assumed all commercialization responsibilities for the NUCYNTA franchise effective January 9, 2018, including sales and marketing. We will receive a royalty on all NUCYNTA revenues based on certain net sales thresholds, with a minimum royalty of $132.0 million for the year ended December 31, 2018 and $135.0 million per year for the years ended December 31, 2019 to December 31, 2021, subject to certain conditions. Both we and Collegium may terminate the agreement under certain circumstances. We may terminate the agreement if aggregate net sales of the NUCYNTA products fall below certain thresholds or within the first year upon the payment of a termination fee. Collegium may terminate at any time after the first anniversary of the transaction by giving 12 months' notice and, if the termination date is prior to fourth anniversary of the transaction, by paying us a $25.0 million termination fee.

NUCYNTA ER and NUCYNTA product sales were $18.1 million and $56.9 million for the three months ended March 31, 2018 and 2017, respectively. Sales in the first quarter of 2018, reflect the period January 1 to January 8, prior to the closing of the Collegium Agreement.

Lazanda (Fentanyl) Nasal Spray

Lazanda nasal spray is an intranasal fentanyl drug used to manage breakthrough pain in adults (18 years of age and older) who are already routinely taking other opioid pain medicines around the clock for cancer pain. We acquired Lazanda in July 2013 from Archimedes Pharma US Inc. and its affiliated companies (collectively, Archimedes). In November 2017, we entered into agreements with Slán pursuant to which Slán acquired our rights to Lazanda. The $0.2 million recorded in net sales of Lazanda in the first quarter of 2018 reflects an adjustment to previously recorded sales reserves compared to $3.9 million for the three months end March 31, 2017.

Product Candidates

In November 2017, we entered into agreements with Slán pursuant to which we obtained the marketing rights to cosyntropin. We believe cosyntropin can be second-to-market behind Mallinckrodt plc's marketed product, H-P Acthar gel. We expect Slán to file an NDA for cosyntropin in late 2018.

In December 2015, we entered into a license agreement with Grünenthal GmbH (Grünenthal) pursuant to which we acquired the U.S. and Canadian rights to cebranopadol, a product candidate for the treatment of moderate to severe chronic nociceptive and neuropathic pain. In January 2018, we gave Grünenthal 120 days' written notice of termination of the cebranopadol license agreement.

Segment and Customer Information

We operate in one operating segment and has operations solely in the United States. To date, all of the Company's revenues from product sales are related to sales in the United States. The Company has recognized license and royalty revenue from license agreements in the territories of the United States, Canada, and South Korea.

Collaboration and License Agreement with Ironwood Pharmaceuticals, Inc.

In July 2011, we entered into a collaboration and license agreement with Ironwood granting Ironwood a license for worldwide rights to certain patents and other intellectual property rights to our Acuform drug delivery technology for IW 3718, an Ironwood product candidate under evaluation for refractory GERD. We have received $3.4 million under the agreement, including a contingent milestone payment of $1.0 million in March 2014 as a result of the initiation of clinical trials relating to IW 3718 by Ironwood. We will receive additional contingent milestone payments upon the occurrence of certain development milestones and royalties on net sales of the product if approved, including a $5.0 million contingent milestone payment if Ironwood commences Phase 3 clinical trials for IW-3718.

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RESTRUCTURING

In June 2017, we announced a limited reduction-in-force in order to streamline operations and achieve operating efficiencies. In December 2017, we continued our restructuring plans by initiating a company-wide restructuring designed to help position the Company for sustainable, long-term growth that we believe will align our staff and office locations to fit our commercial strategy. Pursuant to our restructuring plans in February 2018, we eliminated our pain sales force, consisting of approximately 230 sales representative and 25 manager positions, and began the process of relocating our corporate headquarters from Newark, California to Lake Forest, Illinois. In connection with the relocation of the headquarters, we will significantly reduce our office staff and reduce our headquarters office space by approximately 50%. See note 15 to the unaudited condensed consolidated financial statements for further information about our restructuring costs.

CRITICAL ACCOUNTING POLICIES

Critical accounting policies are those that require significant judgment and/or estimates by management at the time that the financial statements are prepared such that materially different results might have been reported if other assumptions had been made. We consider certain accounting policies related to revenue recognition, accrued liabilities and use of estimates to be critical policies. These estimates form the basis for making judgments about the carrying value of assets and liabilities. There have been no changes to our critical accounting policies, other than those listed below, since we filed our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the SEC on March 1, 2018 (the 2017 Form 10-K). The description of our critical accounting policies is incorporated herein by reference to our 2017 Form 10-K.

Recently Adopted Accounting Pronouncements - Revenue Recognition

The Company accounts for revenue arising from contracts and customers in accordance with Accounting Standards Update (ASU or Update) No. 2014-09, Revenue from Contracts with Customers (ASC 606), which was adopted on January 1, 2018 using the modified retrospective transition method. There was no adjustment to the Company’s opening balance of accumulated deficit resulting from the adoption of this guidance.

Under ASC 606, the Company recognizes revenue when its customer obtains control of promised goods or services, in an amount that reflects the consideration which the Company expects to receive in exchange for those goods or services. To determine revenue recognition for arrangements that the Company determines are within the scope of ASC 606, the Company performs the following five step model: (i) identify the contract(s) with a customer; (ii) identify the performance obligations in the contract; (iii) determine the transaction price; (iv) allocate the transaction

price to the performance obligations in the contract; and (v) recognize revenue when (or as) the Company satisfies a performance obligation. The Company only applies the five-step model to contracts when it is probable that Company will collect the consideration it is entitled to in exchange for the goods or services it transfers to the customer. At contract inception, once the contract is determined to be within the scope of ASC 606, the Company assesses the goods or services promised within each contract and determines those that are performance obligations and assesses whether each promised good or service is distinct. The Company then recognizes as revenue the amount of the transaction price that is allocated to the respective performance obligation when (or as) the performance obligation is satisfied.

The Company derives revenue from the sale of its products, royalties and license fees under its Commercialization Agreement with Collegium, and from license fees, milestones and royalties earned on license and collaborative arrangements. See Note 1 to the unaudited condensed consolidated financial statements for further information about our accounting policies.

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RESULTS OF OPERATIONS

Three Months Ended March 31, 2018 and 2017.

Revenue

Total revenues by products are summarized in the following table:

	Three Months Ended March 31,	
	2018	2017
Product sales, net		
Gralise	$ 14,827	$ 17,600
CAMBIA	6,416	7,190
Zipsor	4,746	4,651
Total neurology product sales, net	25,989	29,441
NUCYNTA products (1)	18,145	56,919
Lazanda (2)	220	3,925
Total product sales, net	44,354	90,285
Commercialization agreement:		
Commercialization rights and facilitation services	28,095	—
Revenue from transfer of inventory	55,705	—
Royalties	250	162
Total revenues	$ 128,404	$ 90,447

(1) The Company licensed the commercial rights to sell NUCYNTA to Collegium on January 9, 2018. Nucynta product sales for the three months ended March 31, 2018 reflects the Company selling NUCYNTA between January 1st and January 8th and also includes a $12.5 million benefit related to the release of sales reserves for which the Company is no longer financially responsible for.

(2) The Company divested Lazanda in November 2017. Product sales for the three months ended March 31, 2018 relates to sales reserve estimate adjustments.

Product Sales

Gralise. The decrease in Gralise product sales during the three months ended March 31, 2018 as compared to 2017 was primarily due to lower prescription demand and higher managed care rebates.

CAMBIA. The decrease in CAMBIA product sales during the three months ended March 31, 2018 as compared to 2017 was primarily a result of lower prescription demand.

Zipsor. The increase in Zipsor product sales during the three months ended March 31, 2018 as compared to 2017 was a result of price increases offset, in part, by lower prescription demand.

We expanded the sales force promoting Gralise, CAMBIA and Zipsor from 40 to 90 sales representatives in September 2017, and we do not expect to see any material impact of this increase until the second half of 2018.

NUCYNTA. Net sales in the first quarter of 2018 reflect the period of January 1 to January 8 prior to closing of the Collegium Commercialization Agreement and the release of approximately $12.5 million of rebate reserves that Collegium assumed pursuant to the terms of the Commercialization Agreement. The Company will not record NUCYNTA product net sales during the remainder of the term of the Commercialization Agreement.

During the three months ended March 31, 2017, the we identified that we had understated the amount payable for the Branded Prescription Drug fee (BPD) relating to net sales of the NUCYNTA franchise since its acquisition in the second quarter of 2015. Accordingly, the we recorded an adjustment during the three months ended March 31, 2017 to increase the BPD accrual relating to the net sales of the NUCYNTA franchise in the cumulative amount of $3.4 million of which $1.4 million and $2.0 million related to the years ended December 31, 2015 and 2016, respectively. This adjustment resulted in an increase in loss per share by $0.05 in the three months ended March 31, 2017. In accordance

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with the relevant guidance, management evaluated the materiality of the error from a qualitative and quantitative perspective. Based on such evaluation, we concluded that correcting the cumulative error would not be material to the expected full year results for 2017, and correcting the error would not have had a material impact on any individual prior period financial statements or affect the trend of financial results.

Lazanda. In November 2017, we entered into definitive agreements with Slán pursuant to which we acquired Slán's rights to market cosyntropin in the U.S. and Canada, and Slán acquired our rights to Lazanda nasal spray CII. We ceased recording revenues and related costs associated with Lazanda after November 7, 2017, product sales for the three months ended March 31, 2018 reflect an adjustment to previously recorded sales reserve estimates.

Commercialization agreement revenues. Pursuant to the Commercialization Agreement, Collegium assumed all commercialization responsibilities for the NUCYNTA franchise effective January 9, 2018, including sales and marketing. For 2018 and subsequent years we expect to recognize royalty revenue from the Commercialization Agreement based on net sales of NUCYNTA and NUCYNTA ER. We are entitled to a royalty of 58% of net sales up to $233.0 million in any calendar year; 25% of net sales from $233.0 million to $258.0 million in any calendar year; and 17.5% of net sales above $258.0 million in any calendar year, with a minimum royalty of $132.0 million for the year ended December 31, 2018 and $135.0 million per year for the years ended December 31, 2019 to December 31, 2021, subject to certain conditions. From and after January 1, 2022, we are entitled to a royalty of 58% of annual net sales of NUCYNTA of up to $233.0 million; 25% of net sales from $233.0 million to $258.0 million; and 17.5% of net sales above $258.0 million. Both we and Collegium may terminate the agreement under certain circumstances.

The Company determined the total transaction price to be $553 million, which consists of $537 million in total annual minimum royalty payments, the $10.0 million upfront fee, and a $6.2 million payment for NUCYNTA finished goods inventory at cost. In accordance with the relevant Accounting Standard, the Company allocated the total transaction price to the Company's performance obligations under the Commercialization Agreement over the deemed contract term of four years which begins on the effective date of January 9th, 2018 and lasts through December 31, 2021.

Revenue in the first quarter of 2018 reflects $28.1 million attributable to royalty income for the quarter and $55.7 million attributable the one-time sale of inventory to Collegium at closing. The amount attributable to the sale of inventory represents the stand-alone selling price of that inventory and was recognized in full in the three months ended March 31, 2018 as our performance obligation was completed in January 2018. We will not recognize any future revenue with respect to the inventory sold to Collegium. We expect to recognize total revenues of approximately $178.0 million for 2018 and $125.1 million per year for the years ending December 31, 2019, to 2021 as a result of accounting for the minimum royalty payments due from Collegium. Any amounts receivable in excess of the minimum royalties due till December 31, 2021 will be recognized during the period that NUCYNTA net sales by Collegium exceed $233.0 million. Royalties receivable after January 1, 2022 will be recognized based on NUCYNTA net sales recorded by Collegium.

Pharmacy Benefit Manager. During the three months ended March 31, 2017, we established a reserve with respect to a dispute with a pharmacy benefit manager (PBM) over rebates relating to NUCYNTA ER, NUCYNTA and Gralise. The dispute relates to rebate claims submitted with respect to the year ended December 31, 2015 and the first half of 2016. As of December 31, 2016, we established a reserve for $1.0 million with respect to these claims, and had determined the likely amount payable on settlement would not be material to the consolidated financial statements. However, as a result of further communication with the PBM during the three months ended March 31, 2017, it became clear that our failure to pay the disputed amount would adversely impact our ability to maintain a favorable position on the PBM's formulary. Accordingly, despite our belief that the claims in dispute were invalid, we increased the reserve against this matter by $4.7 million which was an offset to net sales for the three months ended March 31, 2017. We paid this amount in the fourth quarter of 2017.

Royalties

Royalties are primarily comprised of royalties from Aealez Pharmaceuticals, Inc. on net sales of CAMBIA in Canada and royalties from Janssen Pharma on net sales of NUCYNTA ER in Canada and Japan.

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License and other revenue

Janssen Pharmaceuticals, Inc. In August 2012, we entered into a license agreement with Janssen Pharma that granted Janssen Pharma a non-exclusive license to certain patents and other intellectual property rights to the Company's Acuform drug delivery technology for the development and commercialization of tapentadol extended release products, including NUCYNTA ER (tapentadol extended release tablets).We receive low single digit royalties on net sales of NUCYNTA ER in Canada and Japan.

Ironwood Pharmaceuticals, Inc. In July 2011, we entered into a collaboration and license agreement with Ironwood granting Ironwood a license for worldwide rights to certain patents and other intellectual property rights to our Acuform drug delivery technology for IW 3718, an Ironwood product candidate under evaluation for refractory GERD. We will receive contingent milestone payments upon the occurrence of certain development milestones and royalties on net sales of the product if approved, including a $5.0 million contingent milestone payment if Ironwood commences Phase 3 clinical trials for IW-3718.

Cost of Sales

Cost of sales consists of costs of the active pharmaceutical ingredient, contract manufacturing and packaging costs, royalties payable to third parties, inventory write downs, amortization of inventory write-ups associated with business acquisitions, product quality testing, internal employee costs related to the manufacturing process, distribution costs and shipping costs related to our product sales. Cost of sales excludes the amortization of intangible assets described separately below under "Amortization of Intangible Assets." Total cost of sales for the three months ended March 31, 2018 and 2017, was as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Cost of Sales	$ 12,044	$ 17,774
Dollar change from prior year	(5,730)	(5,575)
Percentage change from prior year	(32.2) %	(24.5) %

Cost of sales decreased during the three months ended March 31, 2018 as compared to 2017 primarily due to the reduction in NUCYNTA and Lazanda net product sales. Pursuant to the terms of our Commercialization Agreement with Collegium, effective January 9, 2018, we no longer record product sales of NUCYNTA and NUCYNTA ER and as a result no longer incur or record the cost of sales of such products. The cost of sales related to the net sales of NUCYNTA and NUCYNTA ER were $3.6 million. The cost of sales during the three months ended March 31, 2018 includes $6.2 million related to the cost of inventory transferred to Collegium on closing of the Commercialization

Agreement. Furthermore, following the divestiture of Lazanda in November 2017, we no longer record Lazanda product sales or related cost of sales.

We acquired the U.S. rights to NUCYNTA from Janssen Pharmaceuticals, Inc. (Janssen) in April 2015. As part of that transaction, we also acquired the related royalty obligations for NUCYNTA to Grünenthal, the originator of tapentadol. Pursuant to the terms of the commercialization agreement, Collegium is now responsible for those royalty obligations. However, as a condition of giving its consent to the commercialization agreement with Collegium, Grünenthal amended the terms of the original royalty agreement to require us to pay a minimum royalty of $34.0 million per year on net sales of NUCYNTA greater than $180.0 million and equal to, or less than, $243.0 million for each of the years ended December 31, 2018 through 2021. In return for this agreement to pay minimum royalties, we received the right to share royalties with Grünenthal on net sales of NUCYNTA above $243.0 million during the same period. We are obligated to cover any shortfall between the minimum royalty amount of $34.0 million and the amounts paid to Grünenthal by Collegium for each of the years ended December 31, 2018 through 2021. Under the terms of this amended royalty agreement, the maximum amount that we could be obligated to pay is $8.8 million per year for each of the years ended December 31, 2018 through 2021. We continue to review the net sales of NUCYNTA by Collegium and will recognize an estimated liability once the minimum threshold of $180.0 million is reached. We expect to recognize any such amounts within cost of sales.

We review the net sales of NUCYNTA by Collegium and recognizes an estimated liability for the amount it believes is likely to be paid for the year. As this estimation process requires a significant amount of judgment and is

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based on expected net sales of NUCYNTA by Collegium, the liability recorded as of a reporting period may not necessarily be reflective of the amount ultimately due to Grünenthal for the year.

The cost of sales for Gralise, CAMBIA and Zipsor, combined for the three months ended March 31, 2018 was approximately 8%. We expect cost of sales as a percentage of net sales over the remainder of 2018 will average approximately 8% for Gralise, CAMBIA, and Zipsor, combined.

Research and Development Expenses

Our research and development expenses currently include salaries, clinical trial costs, consultant fees, supplies, manufacturing costs for research and development programs and allocations of corporate costs. It is extremely difficult to predict the scope and magnitude of future research and development expenses for our product candidates in research and development, as it is extremely difficult to determine the nature, timing and extent of clinical trials and studies and the FDA's requirements for a particular drug. As potential products proceed through the development process, each step is typically more extensive, and therefore more expensive, than the previous step. Therefore, success in development generally results in increasing expenditures until actual product approval. Total research and development expenses for the three months ended March 31, 2018 and 2017 were as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Research and development expenses	$ 1,528	$ 5,084
Dollar change from prior year	(3,556)	(865)
Percentage change from prior year	(69.9) %	(14.5) %

Research and development expenses during the three months ended March 31, 2018 decreased as compared to 2017 primarily as a result of a reduction in the development costs associated with cebranopadol, completion of certain portions of our ongoing pediatric trials for NUCYNTA during the second quarter of 2017, and delays in the next steps of those pediatric trials. In January of 2018, we gave to Grünenthal 120 days' written notice of termination of the cebranopadol license agreement and consequently, do not expect to incur any significant costs relating to cebranopadol in 2018.

We expect research and development expenses in 2018 to decrease as compared to 2017 levels. 2018 research and development expenses will consist primarily of pediatric studies relating to NUCYNTA.

Selling, General and Administrative Expenses

Selling, general and administrative expenses primarily consist of personnel, contract personnel, marketing and promotion expenses associated with our commercial products, personnel expenses to support our administrative and operating activities, facility costs, and professional expenses, such as legal fees. Total selling, general and administrative expenses were as follows:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Selling, general and administrative expenses	$ 29,033	$ 48,519
Dollar change from prior year	(19,486)	(4,040)
Percentage change from prior year	(40.2) %	(7.7) %

The decrease in selling, general and administrative expense during the three months ended March 31, 2018 as compared to 2017 was primarily due to the reduction in our sales force following the restructuring plan announced in December 2017 and the elimination of all commercialization efforts relating to NUCYNTA following the Commercialization Agreement with Collegium. Selling, general and administrative expenses in 2017 include a $3.4 million adjustment booked in the three months ended March 31, 2017 related to an increase in estimates associated with the branded prescription drug fee of which $1.4 million and $2.0 million related to the years ended December 31, 2015 and 2016, respectively.

In December 2017, in connection with the signing of the Commercialization Agreement with Collegium we announced the termination of our pain sales force during the first quarter of 2018, consisting of approximately 255 sales

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representative and sales manager positions, and our plan to significantly reduce our office staff and reduce our headquarters office space by approximately 50%. As a result, we expect selling, general and administrative expenses, excluding restructuring charges, in 2018 to be significantly lower than 2017.

Amortization of Intangible Assets

	Three Months Ended March 31,	
(in thousands)	2018	2017
Amortization of intangible assets - NUCYNTA	$ 23,575	$ 23,576
Amortization of intangible assets - CAMBIA	1,284	1,284
Amortization of intangible assets - Lazanda	—	291
Amortization of intangible assets - Zipsor	585	584
Total	$ 25,444	$ 25,735

The reduction in amortization expense during the three months ended March 31, 2018 as compared to 2017 was due to the divestiture of Lazanda to Slán in November 2017, where we exchanged our interest in Lazanda for exclusive distribution rights to cosyntropin in the United States and Canada. Consequently, no amortization expense was recorded relating to Lazanda subsequent to its divestiture.

Restructuring Charges

	Three Months Ended March 31,	
	2018	2017
Employee compensation costs	$ 8,779	$ —
Other exit costs	238	—
Total restructuring costs	$ 9,017	$ —

During the first quarter of 2018 we continued to execute the restructuring plan announced in December 2017. We completed the previously announced termination of our pain sales force during the first quarter of 2018, consisting of approximately 255 sales representative and sales manager positions. We expect to significantly reduce our office staff by the end of the second quarter of 2018. We expect to relocate our corporate headquarters from Newark, California to Lake Forest, Illinois by mid-2018 which will reduce our headquarters office space requirement by 50%, During the first quarter of 2018, we entered into an Office Lease pursuant to which we will lease approximately 31,000 rentable square feet of space in Lake Forest, Illinois. The Lease will commence on the earlier of the completion of the Company’s initial tenant improvements in the space or July 1, 2018, but no later than August 1, 2018. We will therefore, incur overlapping lease expense for a portion of 2018.

For the three months ended March 31, 2018 and 2017, restructuring expenses and one-time termination costs were $9.0 million, and zero. To date we have incurred $18.5 million in related restructuring costs since the announcement of the plan in December 2017 through March 31, 2018. The Company expects to incur additional related restructuring costs of $9.0 million to $12.0 million through June 30, 2019.

Other Income and Expense

Other income and expense as of March 31, 2018 and 2017 was comprised of:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest and other income	$ 229	$ 250
Interest expense	(18,068)	(20,124)
Total other expense	$ (17,839)	$ (19,874)

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The interest expense was comprised of:

	Three Months Ended March 31,	
(in thousands)	2018	2017
Interest payable on Senior Notes	$ 10,441	12,766
Interest payable on Convertible Notes	2,156	2,156
Amortization of debt discounts and issuance costs relating to Senior Notes and Convertible Notes	5,418	4,650
Changes in fair value of contingent consideration	40	531
Other	13	21
Total interest expense	$ 18,068	$ 20,124

We prepaid and retired $100.0 million of principal of the Senior Notes in April 2017 and $10.0 million of principal of the Senior Notes in November 2017. The decrease in interest expense in 2018 as compared to 2017 is due to these principal prepayments, offset in part by the impact of increasing interest rates in 2018. The increase in amortization of debt discounts and issuance costs was primarily due to the modification of the prepayment schedule for our Senior Notes.

On April 2, 2015, we issued $575.0 million aggregate principal amount of senior secured notes (the Senior Notes) for aggregate gross proceeds of approximately $562.0 million pursuant to a Note Purchase Agreement dated March 12, 2015, among us and Deerfield Private Design Fund III, L.P., Deerfield Partners, L.P., Deerfield International Master Fund, L.P., Deerfield Special Situations Fund, L.P., Deerfield Private Design Fund II, L.P., Deerfield Private Design International II, L.P., BioPharma Secured Investments III Holdings Cayman LP, Inteligo Bank Ltd. and Phemus Corporation (collectively, the Purchasers) and Deerfield Private Design Fund III, L.P., as collateral agent. We used $550.0 million of the net proceeds received upon the sale of the Senior Notes to fund a portion of the Purchase Price paid to Janssen Pharma in connection with the NUCYNTA acquisition. We incurred debt issuance costs of $0.5 million during 2015. In November 2017, the Company prepaid and retired $10.0 million of the Senior Notes and paid a $0.4 million prepayment fee. In April 2017, the Company prepaid and retired $100.0 million of the Senior Notes and paid a $4.0 million prepayment fee.

In December 2017 we amended our Note Purchase Agreement for our Senior Notes, modifying the repayment schedule, paying a $3.0 million amendment fee which will offset future prepayment fees, replaced the net sales covenant with an EBITDA covenant, and received a waiver to allow the Commercialization Agreement with Collegium to proceed. We are required to make a scheduled principal repayment of secured indebtedness of $57.5 million in April 2018 followed by a $25.0 million scheduled principal repayment in October 2018 pursuant to the terms of the original and the amended Note Purchase Agreement.

We intend to refinance the balance of our outstanding Senior Notes in the second half of 2018. Any such prepayment and refinancing will be subject to a prepayment fee of 4% of the principal amount of the Senior Notes prepaid and refinanced. In addition, we will also accelerate the recognition of the balance of the unamortized debt discount and the debt issuance costs as of the date of any refinancing.

On September 9, 2014, we issued and sold $345.0 million aggregate principal amount of convertible senior notes in a public offering (the Convertible Notes). The convertible debt offering resulted in net proceeds of $334.2 million after deducting the underwriting discount and offering expenses of $10.4 million and $0.4 million, respectively.

Income Tax Provision

In the three months ended March 31, 2018, we recorded a benefit from income taxes of approximately $0.3 million that represents an effective tax rate of (1.0%) on income from continuing operations. The difference between the income tax benefit of $0.3 million and the tax at the statutory rate of 21% on current year operations is principally due to the change in valuation allowance. For the three months ended March 31, 2017, the difference between the recorded provision for income taxes and the tax benefit based on the federal statutory rate of 35%, was primarily attributable to the impact of the valuation allowance.

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Non-GAAP Financial Measures

To supplement our financial results presented on a U.S. generally accepted accounting principles, or GAAP, basis, we have included information about non GAAP adjusted earnings, non GAAP adjusted earnings per share and non-GAAP adjusted EBITDA, non GAAP financial measures, as useful operating metrics. We believe that the presentation of these non GAAP financial measures, when viewed with our results under GAAP and the accompanying reconciliation, provides supplementary information to analysts, investors, lenders, and our management in assessing the Company's performance and results from period to period. We use these non GAAP measures internally to understand, manage and evaluate the Company's performance, and in part, in the determination of bonuses for executive officers and employees. These non GAAP financial measures should be considered in addition to, and not a substitute for, or superior to, net income or other financial measures calculated in accordance with GAAP. Non GAAP adjusted earnings and non GAAP adjusted earnings per share are not based on any standardized methodology prescribed by GAAP and represent GAAP net income (loss) and GAAP earnings (loss) per share adjusted to exclude amortization, IPR&D and non-cash adjustments related to product acquisitions, stock based compensation expense, non-cash interest expense related to debt, costs associated with the special meeting requests made by an activist investor and CEO transition, costs associated with an attempted debt refinancing, restructuring costs, adjustments associated with non-recurring legal settlements and disputes, and to adjust for the tax effect related to each of the non-GAAP adjustments. Non GAAP adjusted EBITDA is not based on any standardized methodology prescribed by GAAP and represents GAAP net income (loss) adjusted to exclude interest income, interest expense, amortization, IPR&D and non-cash adjustments related to product acquisitions, stock based compensation expense, depreciation, taxes, transaction costs, restructuring costs, adjustments related to non-recurring legal settlements and disputes, costs associated with an attempted debt refinancing, the special meeting requests made by an activist investor, and CEO transition. Non GAAP financial measures used by us may be calculated differently from, and therefore may not be comparable to, non GAAP measures used by other companies.

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Reconciliation of GAAP Net Income (Loss) to Non-GAAP Adjusted Earnings

The following table reconciles our GAAP net income (loss) to non-GAAP adjusted earnings for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31,	
	2018 (unaudited)	2017
(in thousands, except share and per share amounts)		
GAAP net income (loss)	$ 33,824	$ (26,741)
Non-cash adjustment to commercialization agreement revenues (1)	(52,486)	—
Non-cash adjustment to commercialization agreement cost of sales (1)	6,200	—
Release of NUCYNTA sales reserves (2)	(10,711)	
Non-cash interest expense on debt	5,418	4,650
Intangible amortization related to product acquisitions	25,444	25,735
Managed care dispute reserve	—	4,742
Contingent consideration related to product acquisitions	(202)	(4,469)
Restructuring and other costs (3)	8,330	2,276
Stock based compensation	1,976	3,556
Valuation allowance on deferred tax assets	—	7,568
Income tax effect of non-GAAP adjustments (4)	3,615	(12,884)
Non-GAAP adjusted earnings	$ 21,408	$ 4,433
Add interest expense of convertible debt, net of tax (5)	1,703	—
Numerator	$ 23,111	$ 4,433
Shares used in calculation (5)	81,877	64,294
Non-GAAP adjusted earnings per share	$ 0.28	$ 0.07

(1) Adjustment to non-cash value assigned to inventory transferred to Collegium.
(2) $12.5 million benefit from the release of sales reserves for which the Company is no longer financially responsible, net of $1.7 million in royalties payable to Grünenthal.
(3) Restructuring and other costs represents non-recurring costs associated with the Company’s restructuring and headquarters relocation, and CEO transition.
(4) Calculated by taking the pre-tax non-GAAP adjustments and applying the statutory tax rate. Expected cash taxes were zero for the three months ended March 31, 2018 and March 31, 2017.
(5) The Company uses the if-converted method to compute diluted earnings per share with respect to its convertible debt.

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Reconciliation of GAAP Net Income (Loss) to Non-GAAP Adjusted EBITDA

The following table reconciles the Company's GAAP net income (loss) to non-GAAP adjusted EBITDA for the three months ended March 31, 2018 and 2017:

	Three Months Ended March 31,	
	2018 (unaudited)	2017
(in thousands)		
GAAP net income (loss)	$ 33,824	$ (26,741)
Non-cash adjustment to commercialization agreement revenues (1)	(52,486)	—
Non-cash adjustment to commercialization agreement cost of sales (1)	6,200	—
Release of NUCYNTA sales reserves (2)	(10,711)	—
Managed care dispute reserve	—	4,742
Intangible amortization related to product acquisitions	25,444	25,735
Contingent consideration related to product acquisitions	(202)	(4,469)
Stock based compensation	1,976	3,556
Interest income	(94)	(204)
Interest expense	18,015	19,572
Depreciation	1,475	626
Provision for income taxes	(325)	202
Restructuring and other costs (3)	8,330	2,276
Transaction costs	361	—
Non-GAAP adjusted EBITDA	$ 31,807	$ 25,295

(1) Adjustment for the non-cash value assigned to inventory transferred to Collegium.
(2) $12.5 million benefit from the release of sales reserves for which the Company is no longer financially responsible, net of $1.7 million in royalties payable to Grünenthal.
(3) Restructuring and other costs represents non-recurring costs associated with the Company's restructuring and headquarters relocation, and CEO transition.

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LIQUIDITY AND CAPITAL RESOURCES

(in thousands)	March 31, 2018	December 31, 2017
Cash, cash equivalents and short-term investments	$ 101,693	$ 128,089

The decrease in cash, cash equivalents and short-term investments during the three months ended March 31, 2018 is primarily attributable to the payment in the quarter of six months of Nucynta product royalties and six months of interest on our convertible notes and changes in working capital items. These payments were partially off-set by the cash generated from operations during the three months ended March 31, 2018.

We may incur operating losses in future years. We believe that our existing cash and investment balances and cash we expect to generate from operations will be sufficient to fund our operations, and to meet our existing obligations for the foreseeable future, including our obligations under the Senior Notes and the Convertible Notes. We base this expectation on our current operating plan and the anticipated impact of the cash expected to be received from Collegium pursuant to the Commercialization Agreement, which may change as a result of many factors, including:

- payments from Collegium pursuant to our Commercialization Agreement;
- acquisitions or licenses of complementary businesses, products, technologies or companies;
- sales of our marketed products;
- expenditures related to our commercialization of Gralise, CAMBIA, and Zipsor;
- expenditures related to our product candidates;
- the timing of our NUCYNTA pediatric clinical trials;
- milestone and royalty revenue we receive under our collaborative development arrangements;
- interest and principal payments on our current and future indebtedness;
- our ability to refinance the Convertible Notes in 2021;
- financial terms of definitive license agreements or other commercial agreements we may enter into; and
- changes in the focus and direction of our business strategy and/or research and development programs.

The inability to raise any additional capital that may be required to fund our future operations or product acquisitions and strategic transactions which we may pursue could have a material adverse effect on our company.

The following table summarizes our cash flow activities (in thousands):

(in thousands)	Three Months Ended March 31, 2018	2017
Cash (used in) provided by operating activities	$ (26,975)	$ 16,006
Cash provided by investing activities	1,424	52,411
Cash provided by financing activities	360	1,684
Net (decrease) increase in cash and cash equivalents	$ (25,191)	$ 70,101

Cash Flows from Operating Activities

Cash (used in) provided by operating activities declined during the three months ended March 31, 2018 as compared to the same period in 2017 primarily due to a reduction in our accounts payable and other accrued liabilities balances and the accrued rebates, returns and discounts balances following the commercialization agreement with Collegium.

Cash Flows from Investing Activities

The reduction in cash provided by investing activities during the three months ended March 31, 2018 primarily relates to the reduction in our investments. Cash provided by investing activities during the three months ended March 31, 2017 primarily related to the maturities of marketable securities.

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Cash Flows from Financing Activities

The reduction in cash used in financing activities during the three months ended March 31, 2018 as compared to the same period in 2017 primarily relates to lower proceeds from stock option exercises during the three months ended March 31, 2018.

Contractual Obligations

As of March 31, 2018, our aggregate contractual obligations as shown in the following table were as follows:

(in thousands)	1 Year	2 - 3 Years	4 - 5 Years	More than 5 Years	Total
Senior Notes—principal	$ 107,500	$ 195,000	$ 62,500	$ —	$ 365,000
Senior Notes—interest	36,758	37,354	2,169	—	76,281
Convertible Debt—principal	—	—	345,000	—	345,000
Convertible Debt—interest	8,625	17,250	4,313	—	30,188
Operating leases(1)	2,562	5,201	4,069	476	12,308
Purchase commitments	16,948	—	—	—	16,948
Total	$ 172,393	$ 254,805	$ 418,051	$ 476	$ 845,725

(1) Amounts represent payments under a non-cancelable office and laboratory lease and under an operating lease for vehicles used by our sales force.

As of March 31, 2018, we had non-cancelable purchase orders and minimum purchase obligations of approximately $16.9 million under our manufacturing agreements related to Gralise, CAMBIA and Zipsor. The amounts disclosed only represent minimum purchase requirements. Actual purchases are expected to exceed these amounts.

In April 2012, the Company entered into an office and laboratory lease agreement to lease approximately 52,500 rentable square feet in Newark, California (Newark Lease) commencing on December 1, 2012. The Company occupied approximately 8,000 additional rentable square feet commencing in July 2015. The lease is due to expire on November 30, 2022.

We are relocating our corporate headquarters from Newark, California to Lake Forest, Illinois sometime in mid-2018. We have had preliminary discussions with our Newark Lease Landlord in the first quarter of 2018 and discussed our options to exit the premises by either subleasing the space or negotiating an exit.

Effective February 28, 2018, the Company entered into an Office Lease, in Lake Forest, Illinois (Lake Forest Lease, where the Company will lease approximately 31,000 rentable square feet of space. The completion of the Company's initial tenant improvements in the space which are expected to be around July 1, 2018, but no later than August 1, 2018. The Lake Forest Lease term is for five (5) years and six (6) months. The Company has the right to renew the term of the Lease for one (1) period of five (5) years, provided that written notice is made to the Landlord no later than twelve (12) months prior to the expiration of the initial term of the Lease. Prior to the Lease Commencement Date, the Company has the right to use temporary space in the Building containing approximately 6,700 rentable square feet.

The Lake Forest Lease initial annual base rent will be $18.00 per rentable square foot of the Premises and will increase annually by $0.50. The lease is a triple net lease, with the Company required to pay its pro rata share of real estate taxes and operating expenses. The Landlord will make available to the Company a tenant improvement allowance of $28.00 per square rentable square foot, which the Company may use towards the initial build-out or apply to the payment of rent.

Off-Balance Sheet Arrangements

None.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in the sources and effects of our market risk compared to the disclosures in Item 7A of our Annual Report on the 2017 Form 10-K.

Interest Rate Risk. We are subject to interest rate fluctuation exposure through our borrowings under the Senior Secured Credit Facility and our investment in money market accounts which bear a variable interest rate. Borrowings under the Senior Secured Credit Facility bear interest at a rate equal to the three month LIBOR plus 9.75% per annum, subject to a 1.0% LIBOR floor and certain thresholds. Current LIBOR rates are above the 1.0% LIBOR floor, and the interest rate on our borrowings under the Senior Secured Credit Facility is currently 12.07% per annum. An increase in the three month LIBOR of 100 basis points above the current three month LIBOR rates would increase our interest expense by approximately $3.2 million for 2018, assuming we timely make the scheduled principal payments. As of March 31, 2018, we had $345 million aggregate principal amount of convertible senior notes outstanding, which are fixed rate instruments.

The goals of our investment policy are the preservation of capital, fulfillment of liquidity needs and fiduciary control of cash. To achieve our goal of maximizing income without assuming significant market risk, we maintain our excess cash and cash equivalents in money market funds and short term corporate debt securities. Because of the short term maturities of our cash equivalents, we do not believe that a decrease in interest rates would have any material negative impact on the fair value of our cash equivalents.

Foreign Currency Risk. We have not had any significant transactions in foreign currencies, nor did we have any significant balances that were due or payable in foreign currencies at December 31, 2017. Accordingly, significant changes in foreign currency rates would not have a material impact on our financial position and results of operations.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

An evaluation was performed under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this quarterly report. Based on that evaluation, our management, including our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective.

We review and evaluate the design and effectiveness of our disclosure controls and procedures on an ongoing basis to improve our controls and procedures over time and to correct any deficiencies that we may discover in the future. Our goal is to ensure that our senior management has timely access to all material financial and non-financial information concerning our business. While we believe the present design of our disclosure controls and procedures is effective to achieve our goal, future events affecting our business may cause us to significantly modify our disclosure controls and procedures.

Changes in Internal Controls

There were no changes in our internal controls over financial reporting during the three months ended March 31, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II — OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

For a description of our material pending legal proceedings, see Note 12 “Commitments and Contingencies - Legal Matters” of the Notes to unaudited condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q, which is incorporated herein by reference.

ITEM 1A. RISK FACTORS

The risk factors presented below amend and restate the risk factors previously disclosed in our 2017 Form 10-K.

The following factors, along with those described above under “MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS — LIQUIDITY AND CAPITAL RESOURCES” should be reviewed carefully, in conjunction with the other information contained in this Form 10-Q and our financial statements. These factors, among others, could cause actual results to differ materially from those currently anticipated and contained in forward-looking statements made in this Form 10-Q and presented elsewhere by our management from time to time. See “Part I, Item 2—Forward-Looking Information.”

We rely on Collegium Pharmaceutical Inc. to commercialize NUCYNTA and NUCYNTA ER and their failure to successfully commercialize these products could have a material adverse effect on our business, financial condition and results of operations.

In December 2017, we entered into a commercialization agreement with Collegium pursuant to which Collegium assumed, effective as of January 9, 2018, responsibility for the sales and marketing of NUCYNTA and NUCYNTA ER. Collegium will pay us royalties based on net sales of NUCYNTA and NUCYNTA ER. Although we have retained certain rights to promote NUCYNTA and NUCYNTA ER to physicians that Collegium does not call on, we do not have any immediate plans to exercise such rights. As a result, the commercial success of NUCYNTA and NUCYNTA ER will depend almost entirely on Collegium’s commercialization efforts.

As a company, Collegium has a limited history of selling and marketing pharmaceutical products. Collegium’s ability to successfully commercialize and generate revenues from NUCYNTA and NUCYNTA ER, our largest selling product, depends on a number of factors, including, but not limited to, Collegium’s ability to:

· develop and execute its sales and marketing strategies for NUCYNTA and NUCYNTA ER;

- achieve, maintain and grow market acceptance of, and demand for, NUCYNTA and NUCYNTA ER;
- obtain and maintain adequate coverage, reimbursement and pricing from managed care, government and other third-party payers;
- maintain and manage the necessary sales, marketing, manufacturing, managed markets, and other capabilities and infrastructure that are required to successfully integrate and commercialize NUCYNTA and NUCYNTA ER;
- obtain adequate supply of NUCYNTA and NUCYNTA ER; and
- comply with applicable legal and regulatory requirements.

Additional factors that may affect the success of our commercialization arrangement with Collegium include the following:

- Collegium may prioritize the commercialization of their other products, including Xtampza, over NUCYNTA and NUCYNTA ER;
- Collegium may pursue higher-priority programs, or change the focus of its marketing programs;
- Collegium may acquire or develop alternative products;
- Collegium may in the future choose to devote fewer resources to NUCYNTA and NUCYNTA ER;
- changes in laws and regulations applicable to, and scrutiny of, the pharmaceutical industry, including the opioid market;
- market acceptance of NUCYNTA and NUCYNTA ER may fail to increase or may decrease;
- the outcome of the appeal of the court's ruling in our litigation against the ANDA filers seeking to prevent such

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ANDA filers from marketing a generic version of NUCYNTA and NUCYNTA ER in the U.S.;
- Collegium may experience financial difficulties;
- Collegium may fail to comply with its obligations under our commercialization agreement; or
- Collegium's involvement in governmental investigations and inquires or lawsuits and the disposition of such proceedings.

Any of the preceding factors could affect Collegium's commitment to, and ability to perform, its obligations under the commercialization agreement, which, in turn, could adversely affect the commercial success of NUCYNTA and NUCYNTA ER. Any failure by Collegium to successfully commercialize NUCYNTA and NUCYNTA ER could have a material adverse effect on our business, financial condition and results of operations.

If our commercialization agreement with Collegium terminates, we may not succeed in commercializing NUCYNTA and NUCYNTA ER on our own or through an alternative commercialization partner.

Our agreement with Collegium grants each party specified termination rights, including if certain minimum performance criteria are unmet. Further, Collegium may terminate the agreement at any time and for any reason after the first anniversary by providing us 12 months' notice. Alternatively, if Collegium is unsuccessful in its commercialization of NUCYNTA and NUCYNTA ER we may seek to terminate the agreement. If the agreement is terminated for any reason, we may either perform commercialization activities relating to NUCYNTA and NUCYNTA ER on our own or search for another commercialization partner, either of which would result in us incurring greater expenses and could cause a disruption in the commercialization of the products while we expand our commercial operations or seek an alternative commercialization partner, which disruption could lead to a loss of market share and decreased demand for the products. If we elect to increase our expenditures to fund commercialization activities on our own, we may need to obtain additional capital, which may not be available to us on acceptable terms, or at all, or which may not be possible due to our other financing arrangements.

If we do not successfully commercialize Gralise, CAMBIA, and Zipsor, our business, financial condition and results of operations will be materially and adversely affected.

In October 2011, we began commercial sales of Gralise. In June 2012, we acquired Zipsor and began commercial promotion of Zipsor in July 2012. In December 2013, we acquired CAMBIA and began commercial promotion of CAMBIA in February 2014. In addition to the risks discussed elsewhere in this section, our ability to successfully commercialize and generate revenues from Gralise, CAMBIA and Zipsor, depends on a number of factors, including, but not limited to, our ability to:

- develop and execute our sales and marketing strategies for our products;
- achieve, maintain and grow market acceptance of, and demand for, our products;
- obtain and maintain adequate coverage, reimbursement and pricing from managed care, government and other third-party payers;
- maintain, manage or scale the necessary sales, marketing, manufacturing, managed markets, and other capabilities and infrastructure that are required to successfully integrate and commercialize our products;
- obtain adequate supply of our products;
- maintain and extend intellectual property protection for our products; and
- comply with applicable legal and regulatory requirements.

If we are unable to successfully achieve or perform these functions, we will not be able to maintain or increase our product revenues and our business, financial condition and results of operations will be materially and adversely affected.

We depend on third parties that are single source suppliers to manufacture our products. If these suppliers are unable to manufacture and supply our products, or if there is insufficient availability of our products or the raw materials necessary to manufacture our products, our business will suffer.

We have one qualified supplier for the active pharmaceutical ingredient in each of NUCYNTA ER, NUCYNTA, CAMBIA, Zipsor and Gralise. An affiliate of Janssen Pharma is currently the sole supplier of NUCYNTA ER pursuant to a manufacturing supply agreement we entered into with such entity in April 2015. Halo Pharmaceutical, Inc. (Halo) is

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the sole supplier of NUCYNTA pursuant to a manufacturing supply agreement we entered into with Halo in June 2017. Patheon Puerto Rico Inc. (Patheon) is our sole supplier for Gralise pursuant to a manufacturing and supply agreement we entered into with Patheon in September 2011. Catalent Ontario Limited is our sole supplier for Zipsor pursuant to a manufacturing agreement we assumed in connection with our acquisition of Zipsor in June 2012. MiPharm, S.p.A is our sole supplier for CAMBIA pursuant to a manufacturing and supply agreement that we assumed in connection with our acquisition of CAMBIA in December 2013. We do not have, and we do not intend to establish in the foreseeable future, internal commercial scale manufacturing capabilities. Rather, we intend to use the facilities of third parties to manufacture products for commercialization and clinical trials. Our dependence on third parties for the manufacture of our products and our product candidates may adversely affect our ability to obtain such products on a timely or competitive basis, if at all. Any stock out, or failure to obtain sufficient supplies of NUCYNTA or NUCYNTA ER, or the necessary active pharmaceutical ingredients, excipients or components necessary to manufacture NUCYNTA or NUCYNTA ER, would adversely affect Collegium's ability to commercialize such products, which would adversely affect our results of operations and financial condition. Any stock out, or failure to obtain sufficient supplies of Gralise, CAMBIA, or Zipsor, or the necessary active pharmaceutical ingredients, excipients or components from our suppliers would adversely affect our business, results of operations and financial condition.

Hurricanes Irma and Maria caused significant devastation and damage throughout Puerto Rico in 2017, including widespread flooding and power loss. As a result, we experienced delays in the manufacture, packaging and delivery of certain dosage strengths of NUCYNTA ER in fourth quarter of 2017 and the first quarter of 2018. We and Collegium may continue to experience further outages in the future. Any delay in the manufacture, packaging or delivery of NUCYNTA and NUCYNTA ER, whether due to the manufacturing facility at which NUCYNTA and NUCYNTA ER are produced not being fully operational for an extended period of time or otherwise, could adversely affect the ability of Collegium to commercialize such products, which could adversely affect our results of operations and financial condition. In addition, if our contract manufacturer is unable to deliver a certain percentage of ordered quantities of NUCYNTA ER for a period of two months or longer in calendar year 2018, then we may be required to make a payment to Collegium to ensure that it receives a minimum level of gross profit for 2018, in which case we would not be ensured a minimum amount of royalties from Collegium for 2018.

The manufacturing process for pharmaceutical products is highly regulated, and regulators may shut down manufacturing facilities that they believe do not comply with regulations. We, our third-party manufacturers and our suppliers are subject to numerous regulations, including current FDA regulations governing manufacturing processes, stability testing, record keeping, product serialization and quality standards. Similar regulations are in effect in other countries. Our third-party manufacturers and suppliers are independent entities who are subject to their own unique operational and financial risks which are out of our control. If we or any third-party manufacturer or supplier fails to perform as required or fails to comply with the regulations of the FDA and other applicable governmental authorities, our ability to deliver adequate supplies of our products to our customers on a timely basis, or to continue our clinical trials could be adversely affected. The manufacturing processes of our third party manufacturers and suppliers may also be found to violate the proprietary rights of others. To the extent these risks materialize and adversely affect such third-party manufacturers' performance obligations to us, and we are unable to contract for a sufficient supply of required products on acceptable terms, or if we encounter delays and difficulties in our relationships with manufacturers or suppliers, our business, results of operation and financial condition could be adversely affected.

If generic manufacturers use litigation and regulatory means to obtain approval for generic versions of our products, our business will be materially and adversely affected.

Under the Federal Food, Drug and Cosmetics Act (FDCA), the FDA can approve an ANDA for a generic version of a branded drug without the ANDA applicant undertaking the clinical testing necessary to obtain approval to market a new drug. In place of such clinical studies, an ANDA applicant usually needs only to submit data demonstrating that its product has the same active ingredient(s) and is bioequivalent to the branded product, in addition to any data necessary to establish that any difference in strength, dosage, form, inactive ingredients or delivery mechanism does not result in different safety or efficacy profiles, as compared to the reference drug.

The FDCA requires an applicant for a drug that relies, at least in part, on the patent of one of our branded drugs to notify us of their application and potential infringement of our patent rights. Upon receipt of this notice we have 45 days to bring a patent infringement suit in federal district court against the company seeking approval of a product covered by one of our patents. The discovery, trial and appeals process in such suits can take several years. If such a suit is commenced, the FDCA provides a 30-month stay on the FDA’s approval of the competitor’s application. Such litigation

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is often time-consuming and quite costly and may result in generic competition if the patents at issue are not upheld or if the generic competitor is found not to infringe such patents. If the litigation is resolved in favor of the applicant or the challenged patent expires during the 30-month stay period, the stay is lifted and the FDA may thereafter approve the application based on the standards for approval of ANDAs.

We have been involved in patent litigation lawsuits against filers of ANDAs (the Filers) seeking to market generic versions of NUCYNTA and NUCYNTA ER before the expiration of the patents listed in the Patent and Exclusivity Information Addendum of FDA's publication, Approved Drug Products with Therapeutic Equivalence Evaluations (commonly known as the Orange Book) for these two products. A two-week bench trial was completed on April 27, 2016. On September 30, 2016, the Court issued its opinion finding all three of the Orange Book patents valid and enforceable. On April 11, 2017, the Court entered a final judgment, which included an injunction enjoining the Filers from engaging in certain activities with regard to tapentadol (the active ingredient in NUCYNTA) and ordering the effective date of any approval of Actavis, Actavis UT, and Roxane's ANDAs, and Alkem's ANDA for NUCYNTA IR to be no earlier than the expiry of the '364 Patent (June 27, 2025), and the effective date of any approval of Alkem's ANDA for NUCYNTA ER to be no early than the expiry of the '130 Patent (September 22, 2028). The foregoing periods of exclusivity may in the future be extended with the award of pediatric exclusivity. The Court's final judgment remains subject to the results of the appeals filed by the parties.

Any introduction of one or more products generic to NUCYNTA ER, NUCYNTA, Gralise, CAMBIA, or Zipsor, whether as a result of an ANDA or otherwise, would harm our business, financial condition and results of operations. The filing of the ANDAs described above, or any other ANDA or similar application in respect to any of our products, could have an adverse impact on our stock price. Moreover, if the patents covering our products are not upheld in litigation or if a generic competitor is found not to infringe these patents, the resulting generic competition would have a material adverse effect on our business, financial condition and results of operations.

If we or our commercialization partner are unable to negotiate acceptable pricing or obtain adequate reimbursement for our products from third-party payers, our business will suffer.

Sales of our products depend significantly on the availability of acceptable pricing and adequate reimbursement from third-party payers such as:

- government health administration authorities;
- private health insurers;
- health maintenance organizations;
- managed care organizations;
- pharmacy benefit management companies; and
- other healthcare-related organizations.

If reimbursement is not available for our products or product candidates, demand for our products may be limited. Further, any delay in receiving approval for reimbursement from third party payers could have an adverse effect on our future revenues.

Third-party payers frequently require pharmaceutical companies to negotiate agreements that provide discounts or rebates from list prices and that protect the payers from price increases above a specified annual limit. We and our commercialization partner have agreed to provide such discounts and rebates to certain third-party payers. We expect increasing pressure to offer larger discounts and rebates or discounts and rebates to a greater number of third-party payers to maintain acceptable reimbursement levels for and access to our products for patients at co-pay levels that are reasonable and customary. Consolidation among large third party payers may increase their leverage in negotiations with pharmaceutical companies. If we or our commercialization partner are forced to provide additional discounts and rebates to third party payers to maintain acceptable access to our products for patients, our results of operations and financial condition could be adversely affected. If third-party payers do not accurately and timely report the eligibility and utilization of our products under their plans, our reserves for rebates or other amounts payable to third party payers may be lower than the amount we are invoiced and we may be required to dispute the amount payable, which would adversely affect our business, financial condition and results of operations. For example, we have had, and continue to have, disputes with managed care providers over rebates related to our products. Even when rebate claims made by such managed care providers are without merit, we may be forced to pay such disputed amounts to the extent our failure to do so could otherwise adversely impact our business, such as our ability to maintain a favorable position on such provider’s

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formulary. In addition, if competitors reduce the prices of their products, or otherwise demonstrate that they are better or more cost effective than our products, this may result in a greater level of reimbursement for their products relative to our products, which would reduce sales of our products and harm our results of operations. The process for determining whether a third-party payer will provide coverage for a product may be separate from the process for setting the price or reimbursement rate that such third-party payer will pay for the product once coverage is approved. Third-party payers may limit coverage to specific products on an approved list, or formulary, which might not include all of the approved products for a particular indication, including one or more of our products. Any third-party payer decision not to approve pricing for, or provide adequate coverage and reimbursement of, our products, including by reducing, limiting or denying reimbursement for new products or excluding products that were previously eligible for reimbursement, would limit the market acceptance and commercial prospects of our products and harm our business, financial condition and results of operations. In addition, any third-party payer decision to impose restrictions, limitations or conditions on prescribing or reimbursement of our products, including on the dosing or duration of prescriptions for our products, would harm our business, financial condition and results of operations.

There have been, and there will continue to be, legislative, regulatory and third-party payer proposals to change the healthcare system in ways that could impact our ability to commercialize our products profitably. We anticipate that the federal and state legislatures and the private sector will continue to consider and may adopt and implement healthcare policies, such as the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act (the ACA), intended to curb rising healthcare costs. These cost containment measures may include: controls on government-funded reimbursement for drugs; new or increased requirements to pay prescription drug rebates to government health care programs; controls on healthcare providers; challenges to or limits on the pricing of drugs, including pricing controls or limits or prohibitions on reimbursement for specific products through other means; requirements to try less expensive products or generics before a more expensive branded product; and public funding for cost effectiveness research, which may be used by government and private third-party payers to make coverage and payment decisions. In California, voters rejected Proposition 61 in November 2016, a ballot initiative that would have prohibited the state from buying prescription drugs from a drug manufacturer at a price over the lowest price paid for such drug by U.S. Department of Veterans Affairs. Although Proposition 61 was defeated, these and other cost containment or price control measures, if adopted at the federal or state level, could significantly decrease the price that we or our commercialization partner receive for our products and any product that we may develop or acquire, which would harm our business, financial condition and results of operations.

Changes in laws and regulations applicable to, and investigations of, the pharmaceutical industry, including the opioid market, may adversely affect our business, financial condition and results of operations.

The manufacture, marketing, sale, promotion and distribution of our products are subject to comprehensive government regulation. Changes in laws and regulations applicable to the pharmaceutical industry could potentially affect our business. For instance, federal, state and local governments have recently given increased attention to the public health issue of opioid abuse. In 2016, the Centers for Disease Control (CDC) issued national, non-binding guidelines on the prescribing of opioids, providing recommended considerations for primary care providers when prescribing opioids, including specific considerations and cautionary information about opioid dosage increases and morphine milligram equivalents (MME). Certain third-party payers are, or are considering, adopting some or all of these CDC guidelines to limit access to high doses of opioids. Recently, CVS Pharmacy announced it would only fill first time opioid prescriptions for acute pain for a seven day supply. In July 2017, the Pharmaceutical Care

Management Association, a trade association representing pharmacy benefit managers, wrote a letter to the commissioner of FDA in which it expressed support for, among other things, the CDC guidelines and a seven-day limit on the supply of opioids for acute pain. In addition, states, including the Commonwealths of Massachusetts and Virginia and the States of New York, Ohio, Arizona, Maine, New Hampshire, Vermont, Rhode ISláND, Colorado, Wisconsin, Alabama, South Carolina, Washington and New Jersey, have either recently enacted, intend to enact, or have pending legislation or regulations designed to, among other things, limit the duration and quantity of initial prescriptions of immediate release forms of opiates, mandate the use by prescribers of prescription drug databases and mandate prescriber education. Also, at the state and local level, a number of states and cities have brought separate lawsuits against various pharmaceutical companies marketing and selling opioid pain medications, alleging misleading or otherwise improper promotion of opioid drugs to physicians and consumers. In addition, the attorneys general from several states have announced the launch of a joint investigation into the marketing and sales practices of drug companies that market opioid pain medications. These and other similar initiatives and actions, whether taken by governmental authorities or other industry stakeholders, may result in the reduced prescribing and use of opioids, including NUCYNTA and NUCYNTA ER,

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which could adversely affect the ability of Collegium to commercialize NUCYNTA and NUCYNTA ER, and in turn adversely affect our business, financial condition and results of operations.

At the federal level, the White House Office of National Drug Control Policy (ONDCP) and the National Institutes of Health are coordinating efforts between the FDA, the U.S. Drug Enforcement Agency (DEA), the U.S. Department of Health and Human Services and pharmaceutical industry groups to research and develop effective non-opioid pain relievers. The DEA continues to increase its efforts to hold manufacturers, distributors, prescribers and pharmacies accountable through various enforcement actions as well as the implementation of compliance practices for controlled substances. Further, the FDA is requiring “black-box” warnings on immediate release opioids highlighting the risk of misuse, abuse, addiction, overdose and death as well as implementing a Risk Evaluation and Mitigation Strategies (REMS) for immediate release opioids. Many elected officials, including President Trump, have called for the DEA to restrict the amount of opioids that can be manufactured in the U.S. The DEA also recently proposed reducing the quota for controlled substances to be manufactured in the U.S. in 2018. In March 2017, President Trump announced the creation of a commission, through ONDCP, to make recommendations to the president on how to best combat opioid addiction and abuse. In August 2017, the commission issued a preliminary report calling on President Trump to officially declare the crisis of opioid abuse a national emergency. On October 26, 2017, President Trump declared the opioid crisis a “national public health emergency”. The commission’s final report was released in early November 2017. These and other changes and potential changes in laws, regulations and industry and regulatory practices including those that have the effect of reducing the overall market for opioids or reducing the prescribing of opioids, could adversely affect Collegium’s ability to commercialize NUCYNTA and NUCYNTA ER and in turn adversely affect our business, financial condition and results of operations.

Heightened attention on the problems associated with the abuse of opioids could adversely affect Collegium’s ability to commercialize NUCYNTA and NUCYNTA ER, which would adversely affect our financial condition and results of operations.

In recent years, there has been increased public attention on the public health issue of opioid abuse. The ability of drug abusers to discover previously unknown ways to abuse and misuse opioid products; public inquiries and governmental investigations into prescription drug abuse; litigation and heightened regulatory activity regarding the sales, marketing, distribution or storage of opioid products, among other things, could cause additional unfavorable publicity regarding the use and misuse of opioids, which could have a material adverse effect on opioid products, the reputation of the opioid manufacturers and the ability of our commercialization partner to successfully commercialize NUCYNTA and NUCYNTA ER. Such negative publicity could reduce the potential size of the market for NUCYNTA and NUCYNTA ER, and decrease the revenues Collegium is able to generate from their sale, which in turn would adversely affect our financial condition and results of operations. Additionally, such increased scrutiny of opioids generally, whether focused on NUCYNTA and NUCYNTA ER or otherwise, could have the effect of negatively impacting relationships with healthcare providers and other members of the healthcare community, reducing the overall market for opioids or reducing the prescribing and use of NUCYNTA and NUCYNTA ER.

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Governmental investigations and inquiries, regulatory actions and lawsuits brought against us by government agencies and private parties with respect to our historical commercialization of opioids could adversely affect our business, financial condition and results of operations.

As a result of the greater public awareness of the public health issue of opioid abuse, there has been increased scrutiny of, and investigation into, the commercial practices of opioid manufacturers generally by federal, state and local regulatory and governmental agencies, as well as increased legal action brought by private parties. For example, we are currently involved in multiple lawsuits asserting state common law and statutory claims related to opioid-drug related injuries that the plaintiffs claim to have suffered. Such litigation and related matters are described in Note 12 “Commitments and Contingencies - Legal Matters” of the Notes to unaudited Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q. Additionally, we were named as a defendant in a case brought by the City of Chicago against a number of pharmaceutical companies marketing and selling opioid pain medications, alleging misleading or otherwise improper promotion of opioid drugs to physicians and consumers. This case against us was dismissed. We received a letter from Senator Claire McCaskill, the Ranking Member on the U.S. Senate Committee on Homeland Security and Governmental Affairs, requesting certain information from the Company regarding its prior commercialization of opioid products. We voluntarily furnished information responsive to Sen. McCaskill’s requests. We received subpoenas or civil investigative demands from the Attorneys General of Kentucky, Maryland, Missouri, Montana, New Jersey and Washington seeking documents and information regarding our prior sales and marketing of opioid products. We are cooperating with each of the foregoing states in their investigations. We received subpoenas from the U.S. Department of Justice (DOJ) seeking documents and information regarding our prior sales and marketing of opioid products. We are cooperating with the DOJ in its investigation. We also from time to time receive and comply with subpoenas from governmental authorities related to investigations primarily directed at third parties, including health care practitioners, pursuant to which our records related to agreements with and payments made to those third parties, among other items, are produced. These matters are described in Note 12 “Commitments and Contingencies - Legal Matters” of the Notes to unaudited Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

These and other governmental investigations or inquiries, as well as lawsuits, in which we are and may become involved may result in additional claims and lawsuits being brought against us by governmental agencies or private parties. It is not possible at this time to predict the outcome of the opioid-related lawsuits mentioned above, any governmental investigations or inquiries of us or any lawsuits or regulatory responses that may result from such investigations or inquiries or otherwise. However, the initiation of any investigation, inquiry or lawsuit relating to us, or any assertion, claim or finding of wrongdoing by us, could:

- adversely affect our business, financial condition and results of operations;
- result in reputational harm and reduced market acceptance and demand for our products;
- harm our and our commercial partner’s ability to market our products;
- cause us to incur significant liabilities, costs and expenses; and
- cause our senior management to be distracted from execution of our business strategy.

To the extent governmental investigations and inquiries or lawsuits similar to those matters described above are, or may be, initiated against Collegium, such proceedings, and any assertion, claim or finding of wrongdoing by Collegium, could adversely affect Collegium's ability to commercialize NUCYNTA or NUCYNTA ER and in turn adversely affect our business, results of operations and financial condition.

Furthermore, governmental regulators could take measures that could have a negative effect on our business and our products. For example, in 2017 Endo Pharmaceuticals, Inc. voluntarily withdrew, at the FDA's request, OPANA ER from the market due to the FDA's view that the risks associated with the use of the product outweighed the potential benefits. Any negative regulatory request or action taken by a regulatory agency, including the FDA, with respect to NUCYNTA or NUCYNTA ER would adversely affect Collegium's ability to commercialize NUCYNTA and NUCYNTA ER and in turn adversely affect our business, results of operations and financial condition.

We may incur significant liability if it is determined that we are promoting or have in the past promoted the "off-label" use of drugs.

Companies may not promote drugs for "off-label" use—that is, uses that are not described in the product's labeling and that differ from those approved by the FDA. Physicians may prescribe drug products for off-label uses, and such off-

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label uses are common across some medical specialties. Although the FDA and other regulatory agencies do not regulate a physician's choice of treatments, the FDCA and FDA regulations restrict communications on the subject of off-label uses of drug products by pharmaceutical companies. The Office of Inspector General of the U.S. Department of Health and Human Services (OIG), the FDA, and the DOJ all actively enforce laws and regulations prohibiting promotion of off-label use and the promotion of products for which marketing clearance has not been obtained. Such liabilities would harm our business, financial condition and results of operations as well as divert management's attention from our business operations and damage our reputation.

We and our commercial partner may be unable to compete successfully in the pharmaceutical industry.

Tapentadol, the active pharmaceutical ingredient in NUCYNTA and NUCYNTA ER, is a proprietary opioid analgesic that is marketed in the U.S. by our commercialization partner Collegium. NUCYNTA and NUCYNTA ER compete with a number of branded and generic products that are widely used to treat moderate to severe pain, including neuropathic pain associated with DPN, and acute pain, respectively. These products include OxyContin® (oxycodone hydrochloride extended-release tables), which is owned by Purdue, is approved for marketing in the U.S. for the management of pain severe enough to require daily, around-the-clock, long-term opioid treatment and for which alternative treatment options are inadequate. OxyContin® has achieved significant levels of market acceptance. Unlike NUCYNTA ER, a number of long-acting opioids have product labelling related to their abuse deterrent properties, which may put NUCYNTA ER at a competitive disadvantage. There are also a number of branded and generic short and long acting opioids, including oxycodone, oxymorphone, fentanyl patch, morphine, buprenorphine patch, tramadol, hydrocodone and hydromorphone, which have received approval and are marketed in the U.S. for the treatment of moderate to severe pain, including chronic and acute pain. More opioid development and launches of both generics and brands are expected to continue. For example, Butrans (promoted by Purdue) has been facing generic entrants since June 2017. In addition, Pfizer's new opioid Troxyca ER was approved in 2016, but has not yet launched. Teva's Vantrela ER was approved in 2017, but has not yet launched. Inspirion received approval for MorphaBond™ ER (morphine sulfate) and RoxyBond (oxycodone HCL). MorphaBond launched in the fourth quarter of 2017 and RoxyBond is expected to launch in the first quarter of 2018. Lyrica (pregabalin), which is marketed by Pfizer, is approved for marketing in the U.S. for the treatment of neuropathic pain associated with DPN. Pfizer also received approval on October 13, 2017 to market Lyrica CR (pregabalin extended-release tablets), a once-daily treatment for the management of DPN and PHN. Branded and generic versions of duloxetine and lidocaine have also been approved for marketing in the U.S. for the treatment of neuropathic pain associated with DPN. There are a number of other products and treatments prescribed for, or under development for, the management of chronic and acute pain, including neuropathic pain associated with DPN, which are now or may become competitive with NUCYNTA and NUCYNTA ER.

Branded gabapentin is currently sold by Pfizer as Neurontin for adjunctive therapy for partial onset epileptic seizures and for PHN. Pfizer's basic U.S. patents relating to Neurontin have expired, and numerous companies have received approval to market generic versions of the immediate release product. In addition to receiving approval for marketing to treat neuropathic pain associated with DPN, Lyrica (pregabalin), has also been approved for marketing in the U.S. for the treatment of post herpetic pain, fibromyalgia, adjunctive therapy for partial onset epileptic seizures, and nerve pain associated with spinal cord injury and has captured a significant portion of the market. Pfizer received approval on October 13, 2017 to market Lyrica CR (pregabalin extended-release tablets), a once-daily treatment for the management of DPN and PHN. Arbor Pharmaceuticals, LLC's Horizant (gabapentin enacarbil extended-release

tablets) is approved for the management of PHN and Restless Leg Syndrome. There are other products prescribed for or under development for PHN which are now or may become competitive with Gralise.

Diclofenac, the active pharmaceutical ingredient in Zipsor, is an NSAID that is approved in the U.S. for the treatment of mild to moderate pain in adults, including the symptoms of arthritis. Both branded and generic versions of diclofenac are marketed in the U.S. Zipsor competes against other drugs that are widely used to treat mild to moderate pain in the acute setting. In addition, a number of other companies are developing NSAIDs in a variety of dosage forms for the treatment of mild to moderate pain and related indications. Other drugs are in clinical development to treat acute pain.

An alternate formulation of diclofenac is the active ingredient in CAMBIA that is approved in the U.S. for the acute treatment of migraines in adults. CAMBIA competes with a number of triptans that are used to treat migraines and certain other headaches. Pfizer’s Relpax patent expired in December 2016, and generic entrants began in July 2017. Currently, seven triptans are available and sold in the U.S. (almotriptan, eletriptan, frovatriptan, naratriptan, rizatriptan,

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sumatriptan and zolmitriptan). Branded competitors include Zomig nasal, Onzetra, Xsail Zembrace, SymTouchTM and Treximet, which is a fixed-dose combination product containing sumatriptan plus naproxen. There are other products prescribed for or under development for the treatment of migraines that are now or may become competitive with CAMBIA, including CGRP products which may launch in 2018.

Competition in the pharmaceutical industry is intense and we expect competition to increase. Competing products currently under development or developed in the future may prove superior to our products and may achieve greater commercial acceptance. Most of our principal competitors have substantially greater financial, sales, marketing, personnel and research and development resources than we or Collegium do.

Pharmaceutical marketing is subject to substantial regulation in the U.S. and any failure by us or our commercial and collaborative partners to comply with applicable statutes or regulations could adversely affect our business.

All marketing activities of Collegium associated with NUCYNTA and NUCYNTA ER, and of us associated with Gralise, CAMBIA, and Zipsor, as well as marketing activities related to any other products that we may acquire, or for which we or our collaborative partners obtain regulatory approval, are and will be subject to numerous federal and state laws governing the marketing and promotion of pharmaceutical products. The FDA regulates post-approval promotional labeling and advertising to ensure that they conform to statutory and regulatory requirements. In addition to FDA restrictions, the marketing of prescription drugs is subject to laws and regulations prohibiting fraud and abuse under government healthcare programs. For example, the federal healthcare program anti-kickback statute prohibits giving things of value to induce the prescribing or purchase of products that are reimbursed by federal healthcare programs, such as Medicare and Medicaid. In addition, federal false claims laws prohibit any person from knowingly presenting, or causing to be presented, a false claim for payment to the federal government. Under this law, in recent years, the federal government has brought claims against drug manufacturers alleging that certain marketing activities caused false claims for prescription drugs to be submitted to federal programs. Many states have similar statutes or regulations that apply to items and services reimbursed under Medicaid and other state programs, and, in some states, such statutes or regulations apply regardless of the payer.

Governmental authorities may also seek to hold us responsible for any failure of our commercialization or collaborative partners to comply with applicable statutes or regulations. If we, or our commercial or collaborative partners, fail to comply with applicable FDA regulations or other laws or regulations relating to the marketing of our products, we could be subject to criminal prosecution, civil penalties, seizure of products, injunctions and exclusion of our products from reimbursement under government programs, as well as other regulatory or investigatory actions against our product candidates, our commercial or collaborative partners or us.

If we engage in strategic transactions that fail to achieve the anticipated results and synergies, our business will suffer.

We may seek to engage in strategic transactions with third parties, such as product or company acquisitions, strategic partnerships, joint ventures, divestitures or business combinations. We may face significant competition in seeking potential strategic partners and transactions, and the negotiation process for acquiring any product or engaging in strategic transactions can be time-consuming and complex. Engaging in strategic transactions, such as our acquisition in 2015 of the U.S. rights to NUCYNTA and NUCYNTA ER, and our completion in 2018 of the commercialization arrangement covering NUCYNTA and NUCYNTA ER with Collegium, may require us to incur non-recurring and other charges, increase our near- and long-term expenditures, pose integration challenges and fail to achieve the anticipated results or synergies or distract our management and business, which may harm our business.

As part of an effort to acquire a product or company or to enter into other strategic transactions, we conduct business, legal and financial due diligence with the goal of identifying, evaluating and assessing material risks involved in the transaction. Despite our efforts, we ultimately may be unsuccessful in ascertaining, evaluating and accurately assessing all such risks and, as a result, might not realize the intended advantages of the transaction. We may also assume liabilities and legal risks in connection with a transaction, including those relating to activities of the seller prior to the consummation of the transaction and contracts that we assume. Failure to realize the expected benefits from acquisitions or strategic transactions that we may consummate, or that we have completed, such as the acquisition in 2015 of the U.S. rights to NUCYNTA and NUCYNTA ER, and the recently completed commercialization arrangement covering NUCYNTA and NUCYNTA ER with Collegium, whether as a result of identified or unidentified risks,

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integration difficulties, regulatory setbacks, governmental investigations, litigation or other events, could adversely affect our business, results of operations and financial condition.

Our failure to generate sufficient cash flow from our business to make payments on our debt would adversely affect our business, financial condition and results of operations.

We have incurred significant indebtedness in the aggregate principal amount of $710.0 million at March 31, 2018 under the senior secured notes we issued in April 2015 (the Senior Notes) and the convertible notes we issued in September 2014 (the Convertible Notes). Our ability to make scheduled payments of the principal of, to pay interest on or to refinance the Convertible Notes, the Senior Notes and any additional debt obligations we may incur depends on our future performance, which is subject to economic, financial, competitive and other factors that may be beyond our control. Our business may not generate cash flow from operations in the future sufficient to service our debt and to make necessary capital expenditures. If we are unable to generate such cash flow, we may be required to adopt one or more alternatives, such as selling assets, restructuring debt or obtaining additional equity capital on terms that may be onerous or highly dilutive. Our ability to refinance our indebtedness will depend on the capital markets and our financial condition at such time. We may not be able to engage in any of these activities or engage in these activities on commercially reasonable or acceptable terms, which could result in a default on our obligations, including the Convertible Notes and the Senior Notes.

In addition, our significant indebtedness, combined with our other financial obligations and contractual commitments, could have other important consequences to our business. For example, it could:

- make it more difficult for us to meet our payment and other obligations under the Convertible Notes, the Senior Secured Notes or our other indebtedness;
- result in an event of default if we fail to comply with the financial and other covenants contained in the Note Purchase Agreement, which event of default could result in all of our debt becoming immediately due and payable;
- make us more vulnerable to adverse changes in general economic, industry and competitive conditions and adverse changes in government regulation;
- subject us to the risk of increased sensitivity to interest rate increases on our indebtedness with variable interest rates, including the Senior Notes;
- require the dedication of a substantial portion of our cash flow from operations to service our indebtedness, thereby reducing the amount of our cash flow available for other purposes, including working capital, clinical trials, research and development, business development activities, capital expenditures and other general corporate purposes;
- prevent us from raising funds necessary to repurchase the Convertible Notes in the event we are required to do so following a “fundamental change,” as specified in the indenture governing the Convertible Notes, to repurchase the Senior Notes in the event we are required to do so following a “major transaction” or as required in the event that the principal amount outstanding under the Convertible Notes as of March 31, 2021 is greater than $100.0 million, as specified in the Note Purchase Agreement or to settle conversions of the Convertible Notes in cash;
- result in dilution to our existing shareholders as a result of the conversion of the Convertible Notes into shares of common stock;
- limit our flexibility in planning for, or reacting to, changes in our business and our industry;

- put us at a disadvantage compared to our competitors who have less debt; and
- limit our ability to borrow additional amounts for working capital and other general corporate purposes, including funding possible acquisitions of, or investments in, additional products, technologies and companies.

Any of these factors could adversely affect our business, financial condition and results of operations. In addition, if we incur additional indebtedness, the risks related to our business and our ability to service or repay our indebtedness would increase.

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We may not have the ability to raise the funds necessary to settle conversions of the Convertible Notes in cash, to repurchase the Convertible Notes upon a fundamental change or to repurchase the Senior Notes upon a major transaction put or as required in the event that the principal amount outstanding under the Convertible Notes as of March 31, 2021 is greater than $100.0 million.

Holders of the Convertible Notes will have the right to require us to repurchase all or a portion of their Convertible Notes upon the occurrence of certain events, including events deemed to be a “fundamental change,” at a repurchase price equal to 100% of the principal amount of the outstanding Convertible Notes to be repurchased, plus accrued and unpaid interest, if any. Upon conversion of the Convertible Notes, unless we elect to deliver solely shares of our common stock to settle such conversion (other than paying cash in lieu of delivering any fractional share), we will be required to make cash payments in respect of the Convertible Notes being converted.

Furthermore, holders of the Senior Notes will have the right to require us to repurchase all of their Senior Notes (i) if the principal amount outstanding under the Convertible Notes as of March 31, 2021 is greater than $100.0 million, at a repurchase price equal to 100% of the principal amount of the outstanding Senior Notes to be repurchased, plus accrued and unpaid interest, if any, or (ii) upon the occurrence of certain events deemed to be a “major transaction” at a repurchase price equal to: (a) 100% of the principal amount of the outstanding Senior Notes to be repurchased, plus (b) accrued and unpaid interest, if any, plus (c) a prepayment premium, which may be substantial.

However, we may not have enough available cash or be able to obtain financing at the time we are required to make repurchases of Convertible Notes or Senior Notes or pay cash with respect to Convertible Notes being converted. In addition, our ability to repurchase or to pay cash upon conversion of the Convertible Notes may be limited by law, regulatory authority or agreements governing our future indebtedness. An event of default under the indenture governing the Convertible Notes, including our failure to repurchase Convertible Notes when required by the indenture governing the Convertible Notes, would constitute a default under the Note Purchase Agreement. In addition, an event of default under the Note Purchase Agreement, including our failure to repurchase Senior Notes when the repurchase is required by the Note Purchase Agreement, would constitute a default under the indenture governing the Convertible Notes. Moreover, the occurrence of a fundamental change under the indenture governing the Convertible Notes or a major transaction under the Note Purchase Agreement could constitute an event of default under either the indenture governing the Convertible Notes or the Note Purchase Agreement, as applicable and any agreements that may govern any future indebtedness. Following an event of default, if the payment of our outstanding indebtedness were to be accelerated after any applicable notice or grace periods, we may not have sufficient funds to repay such indebtedness.

Acquisition of new and complementary businesses, products and technologies is a key element of our corporate strategy. If we are unable to successfully identify and acquire such businesses, products or technologies, our business growth and prospects will be limited.

Since June 2012, we have acquired NUCYNTA, NUCYNTA ER, CAMBIA, and Zipsor, exclusively in-licensed the right to develop and commercialize cebranopadol, and in-licensed the right to market cosyntropin. An important element of our business strategy is to actively seek to acquire products or companies and to in-license or seek co-promotion rights to additional products. We cannot be certain that we will be able to successfully identify, pursue and complete any further acquisitions or whether we would be able to successfully integrate any acquired business, product or technology or retain any key employees. If we are unable to enhance and broaden our product offerings, our business and prospects will be limited.

If we are unable to successfully integrate any business, product or technology we may acquire, our business, financial condition and operating results will suffer.

Integrating any business, product or technology we acquire is expensive, time consuming and can disrupt and adversely affect our ongoing business, including product sales, and distract our management. Our ability to successfully integrate any business, product or technology we acquire depends on a number of factors, including, but not limited to, our ability to:

- minimize the disruption and distraction of our management and other employees, including our sales force, in connection with the integration of any acquired business, product or technology;
- maintain and increase sales of our existing products;

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- establish or manage the transition of the manufacture and supply of any acquired product, including the necessary active pharmaceutical ingredients, excipients and components;
- identify and add the necessary sales, marketing, manufacturing, regulatory and other related personnel, capabilities and infrastructure that are required to successfully integrate any acquired business, product or technology;
- manage the transition and migration of all commercial, financial, legal, clinical, regulatory and other pertinent information relating to any acquired business, product or technology;
- comply with legal, regulatory and contractual requirements applicable to any acquired business, product or technology;
- obtain and maintain adequate coverage, reimbursement and pricing from managed care, government and other third-party payers with respect to any acquired product; and
- maintain and extend intellectual property protection for any acquired product or technology.

If we are unable to perform the above functions or otherwise effectively integrate any acquired businesses, products or technologies, our business, financial condition and operating results will suffer.

Health care reform could increase our expenses and adversely affect the commercial success of our products.

The ACA includes numerous provisions that affect pharmaceutical companies. For example, the ACA seeks to expand healthcare coverage to the uninsured through private health insurance reforms and an expansion of Medicaid. The ACA also imposes substantial costs on pharmaceutical manufacturers, such as an increase in liability for rebates paid to Medicaid, new drug discounts that must be offered to certain enrollees in the Medicare prescription drug benefit and an annual fee imposed on all manufacturers of brand prescription drugs in the U.S. The ACA also requires increased disclosure obligations and an expansion of an existing program requiring pharmaceutical discounts to certain types of hospitals and federally subsidized clinics and contains cost-containment measures that could reduce reimbursement levels for pharmaceutical products. The ACA also includes provisions known as the Physician Payments Sunshine Act, which require manufacturers of drugs, biologics, devices and medical supplies covered under Medicare and Medicaid to record any transfers of value to physicians and teaching hospitals and to report this data to the Centers for Medicare and Medicaid Services for subsequent public disclosure. Similar reporting requirements have also been enacted on the state level domestically, and an increasing number of countries worldwide either have adopted or are considering similar laws requiring transparency of interactions with health care professionals. Failure to report appropriate data may result in civil or criminal fines and/or penalties. These and other aspects of the ACA, including regulations that may be imposed in connection with the implementation of the ACA, such as the 340B Program, could increase our expenses and adversely affect our ability to successfully commercialize our products and product candidates.

Many members of Congress and President Trump have pledged to repeal the ACA. In January 2017, the House and Senate passed a budget resolution that authorizes congressional committees to draft legislation to repeal all or portions of the ACA and permits such legislation to pass with a majority vote in the Senate. President Trump also recently issued an executive order in which he stated that it is his administration’s policy to seek the prompt repeal of the ACA and directed executive departments and federal agencies to waive, defer, grant exemptions from, or delay the implementation of burdensome provisions of the ACA to the maximum extent permitted by law. Although several attempts to repeal and replace the ACA failed to pass both houses of Congress, there is still uncertainty with respect to

the impact President Trump's administration and the Congress may have, if any, and any changes will likely take time to unfold. Any new laws or regulations that have the effect of imposing additional costs or regulatory burden on pharmaceutical manufacturers, or otherwise negatively affect the industry, could adversely affect our ability to successfully commercialize our products and product candidates. In addition, President Trump has indicated that reducing the price of prescription drugs will be a priority of his administration. The implementation of any price controls or caps on prescription drugs, whether at the federal level or state level, could adversely affect our business, operating results and financial condition.

If we or our collaborative partners are unable to obtain or maintain regulatory approval for our products, our raw materials or product candidates, we will be limited in our ability to commercialize our products, and our business will suffer.

The regulatory process is expensive and time consuming. Even after investing significant time and expenditures on clinical trials, we may not obtain regulatory approval of our product candidates. Data obtained from clinical trials are susceptible to varying interpretations, which could delay, limit or prevent regulatory approval, and the FDA may not

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agree with our methods of clinical data analysis or our conclusions regarding safety and/or efficacy. Significant clinical trial delays could impair our ability to commercialize our products and could allow our competitors to bring products to market before we do. In addition, changes in regulatory policy for product approval during the period of product development and regulatory agency review of each submitted new application may cause delays or rejections. Even if we receive regulatory approval, this approval may entail limitations on the indicated uses for which we can market a product.

Further, with respect to our approved products, once regulatory approval is obtained, a marketed product and its manufacturer are subject to continual review. The discovery of previously unknown problems with a product or manufacturer may result in restrictions on the product, manufacturer or manufacturing facility, including withdrawal of the product from the market. Manufacturers of approved products are also subject to ongoing regulation and inspection, including compliance with FDA regulations governing current Good Manufacturing Practices (cGMP) or Quality System Regulation (QSR). The FDCA, the Controlled Substances Act of 1970 (CSA) and other federal and foreign statutes and regulations govern and influence the testing, manufacturing, packing, labeling, storing, record keeping, safety, approval, advertising, promotion, sale and distribution of our products. In addition, we and our partners are also subject to ongoing DEA regulatory obligations, including annual registration renewal, security, recordkeeping, theft and loss reporting, periodic inspection and annual quota allotments for the raw material for commercial production of our products. The failure to comply with these regulations could result in, among other things, warning letters, fines, injunctions, civil penalties, recall or seizure of products, total or partial suspension of production, non-renewal of marketing applications or authorizations or criminal prosecution, which could adversely affect our business, results of operations and financial condition.

We are also required to report adverse events associated with our products to the FDA and other regulatory authorities. Unexpected or serious health or safety concerns could result in labeling changes, recalls, market withdrawals or other regulatory actions. Recalls may be issued at our discretion or at the discretion of the FDA or other empowered regulatory agencies. For example, in June 2010, we instituted a voluntary class 2 recall of 52 lots of our 500mg Glumetza product after chemical traces of 2,4,6-tribromoanisole (TBA) were found in the product bottle.

We may incur product liability losses and other litigation liability.

We are or may be involved in various legal proceedings, lawsuits and certain government inquiries and investigations, including with respect to, but not limited to, patent infringement, product liability, personal injury, antitrust matters, securities class action lawsuits, breach of contract, Medicare and Medicaid reimbursement claims, opioid-related matters, promotional practices and compliance with laws relating to the manufacture and sale of controlled substances. For example, we, along with other opioid manufacturers and, often, distributors, have been named in lawsuits related to the manufacturing, distribution, marketing and promotion of opioids. In addition, we have also received various subpoenas and requests for information related to the distribution, marketing and sale of our opioid products. Such litigation and related matters are described in Note 12 “Commitments and Contingencies - Legal Matters” of the Notes to Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q. If any of these legal proceedings, inquiries or investigations were to result in an adverse outcome, the impact could have a material adverse effect on our competitive position, business, financial condition, results of operations and cash

flows.

We have obtained product liability insurance for sales of our products and clinical trials currently underway, but:

- we may be unable to maintain product liability insurance on acceptable terms;
- we may be unable to obtain product liability insurance for future trials;
- we may be unable to obtain product liability insurance for future products; or
- our insurance may not provide adequate protection against potential liabilities (including pending and future claims relating to opioid litigation), if at all.

Our inability to obtain or maintain adequate insurance coverage at an acceptable cost could prevent or inhibit the commercialization of our products. Collegium's inability to obtain or maintain adequate insurance coverage with regard to its commercialization of NUCYNTA and NUCYNTA ER could prevent or inhibit Collegium's commercialization of NUCYNTA and NUCYNTA ER and in turn adversely affect our business, results of operations and financial condition. Defending a lawsuit could be costly and significantly divert management's attention from conducting our business. If third parties were to bring a successful product liability or other claims, or series of claims, against us, or Collegium

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relating to NUCYNTA and NUCYNTA ER, for uninsured liabilities or in excess of our insured liability limits, or Collegium's insured liability limits with respect to NUCYNTA and NUCYNTA ER, respectively, our business, results of operations and financial condition could be adversely affected.

Any failure by us or our commercialization or collaborative partners to comply with applicable statutes or regulations relating to controlled substances could adversely affect our business.

Each of NUCYNTA and NUCYNTA ER are opioid analgesics that contain tapentadol. Tapentadol is a regulated "controlled substance" under the CSA. The CSA establishes, among other things, certain registration, production quotas, security, recordkeeping, reporting, import, export and other requirements administered by the DEA. The DEA regulates controlled substances as Schedule I, II, III, IV or V substances, with Schedule II substances being the pharmaceutical products that present the highest risk of abuse. Tapentadol is listed by the DEA as a Schedule II substance under the CSA. The manufacture, shipment, storage, sale and use, among other things, of controlled substances that are pharmaceutical products are subject to a high degree of regulation. For example, generally all Schedule II substance prescriptions must be written and signed by a physician, physically presented to a pharmacist and may not be refilled without a new prescription.

The DEA also conducts periodic inspections of certain registered establishments that handle controlled substances. Facilities that conduct research, manufacture, distribute, import or export controlled substances must be registered to perform these activities and have the security, control and inventory mechanisms required by the DEA to prevent drug loss and diversion. Failure to maintain compliance, particularly non-compliance resulting in loss or diversion, can result in regulatory action that could adversely affect our business, results of operations and financial condition. The DEA may seek civil penalties, refuse to renew necessary registrations, or initiate proceedings to restrict, suspend or revoke those registrations and in certain circumstances, violations could lead to criminal proceedings against us or our manufacturing and distribution partners, and our respective employees, officers and directors.

In addition to federal regulations, many individual states also have controlled substances laws. Although state controlled substances laws generally mirror federal law, because the states are separate jurisdictions they may separately schedule our products. Any failure by us or our partners to obtain separate state registrations, permits or licenses in order to be able to obtain, handle and distribute tapentadol or to meet applicable regulatory requirements could lead to enforcement and sanctions by the states in addition to those from the DEA or otherwise arising under federal law and could adversely affect our business, results of operations and financial condition.

Limitations on the production of Schedule II substances in the U.S. could limit the ability of Collegium to successfully commercialize NUCYNTA and NUCYNTA ER.

The availability and production of all Schedule II substances, including tapentadol, is limited by the DEA through a quota system that includes a national aggregate quota, production quotas for individual manufacturers and procurement quotas that authorize the procurement of specific quantities of Schedule II controlled substances for use in drug product manufacturing. The DEA annually establishes an aggregate quota for total tapentadol production in the U.S. based on the DEA's estimate of the quantity needed to meet commercial and scientific need. The aggregate quota of tapentadol that the DEA allows to be produced in the U.S. annually is allocated among applicable individual drug manufacturers, which must submit applications at least annually to the DEA for individual production quotas. In turn, our third party manufacturers of NUCYNTA and NUCYNTA ER have to obtain a procurement quota to source tapentadol for the production of NUCYNTA and NUCYNTA ER.

The DEA requires substantial evidence and documentation of expected legitimate medical and scientific needs before assigning quotas for these activities. The DEA may adjust aggregate production quotas and individual production and procurement quotas from time to time during the year, although the DEA has substantial discretion in whether or not to make such adjustments. Based on a variety of factors, including public policy considerations, the DEA may set the aggregate quota lower for tapentadol than the total amount requested by individual manufacturers. Although through our manufacturing partner we are permitted to ask the DEA to increase our manufacturer's procurement quota after it is initially established, we cannot be certain that the DEA would act favorably upon such a request. In addition, our manufacturers obtain a procurement quota for tapentadol for all tapentadol products manufactured at their facility, which is allocated to NUCYNTA and NUCYNTA ER, as applicable, at the manufacturer's discretion. If the available quota of tapentadol is insufficient to meet commercial demand or clinical needs, our business, results of operations and financial condition could be adversely affected. Further, during the 2016 presidential campaign, President Trump called for the

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DEA to restrict the amount of opioids that can be manufactured in the U.S. The DEA also recently proposed reducing the quota for controlled substances to be manufactured in the U.S. in 2018. Additionally, the DEA has proposed various changes to its process for setting production and procurement quota. Any delay or refusal by the DEA or our manufacturers in establishing the production or procurement quota or granting sufficient production or procurement quota to meet commercial demand, or any reduction by the DEA or our manufacturer in the allocated quota for tapentadol, could adversely affect the ability of Collegium to commercialize NUCYNTA and NUCYNTA ER and in turn adversely affect our business, results of operations and financial condition.

The FDA-mandated Risk Evaluation and Mitigation Strategy program may limit the commercial success of NUCYNTA ER and potentially NUCYNTA.

NUCYNTA ER is subject to a FDA-mandated Risk Evaluation and Mitigation Strategy (REMS) protocol that requires enrollment and participation in the REMS program to prescribe, dispense or distribute such products for outpatient use. Many physicians, health care practitioners and pharmacies are unwilling to enroll and participate in the REMS programs. As a result, there are relatively few prescribers and dispensers of products subject to REMS protocols. In addition, the FDA recently mandated a REMS protocol for NUCYNTA. If Collegium is not able to successfully promote NUCYNTA ER and NUCYNTA to participants in the applicable REMS program, our business, results of operations and financial condition could be adversely affected.

The market price of our common stock historically has been volatile. Our results of operations may fluctuate and affect our stock price.

The trading price of our common stock has been, and is likely to continue to be, volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control. From December 31, 2015 through March 31, 2018, our stock price has ranged from $4.31 to $27.02 per share.

Factors affecting our operating results and that could adversely affect our stock price include:

- the degree of commercial success and market acceptance of NUCYNTA and NUCYNTA ER achieved by Collegium;
- the degree of commercial success and market acceptance of Gralise, CAMBIA and Zipsor achieved by us;
- the current and future market conditions for short-acting and long-acting opioids;
- filings and other regulatory or governmental actions, investigations or proceedings related to our products and product candidate and those of our commercialization and collaborative partners;
- the reversal or any appeal of the court’s favorable ruling in our patent infringement litigation against the filers of ANDAs for NUCYNTA and NUCYNTA ER;
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developments concerning proprietary rights, including patents, infringement allegations, inter party review proceedings and litigation matters;
- legal and regulatory developments in the U.S.;
- actions taken by industry stakeholders affecting the market for our products;
- our ability to generate sufficient cash flow from our business to make payments on our indebtedness;
- our and our commercialization and collaborative partners' compliance or non-compliance with legal and regulatory requirements and with obligations under our collaborative agreements;
- our ability to successfully develop and execute our sales and marketing strategies;
- our plans to acquire, in-license or co-promote other products, compounds or acquire or combine with other companies, and our degree of success in realizing the intended advantages of, and mitigating any risks associated with, any such transaction;
- our ability to successfully commercialize cosyntropin if regulatory approval is obtained;
- adverse events related to our products, including recalls;
- interruptions of manufacturing or supply, or other manufacture or supply difficulties;
- variations in revenues obtained from commercialization and collaborative agreements, including contingent milestone payments, royalties, license fees and other contract revenues;
- adverse events or circumstances related to our peer companies or our industry or the markets for our products;
- adoption of new technologies by us or our competitors;
- the outcome of our patent infringement litigation against Purdue;

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- the outcome of our opioid-related investigations and litigation;
- the outcome and impact of a proxy contest initiated by an activist shareholder;
- our compliance with the terms and conditions of the agreements governing our indebtedness;
- decisions by collaborative partners to proceed or not to proceed with subsequent phases of a collaboration or program;
- sales of large blocks of our common stock or the dilutive effect of our Convertible Notes; and
- variations in our operating results, earnings per share, cash flows from operating activities, deferred revenue, and other financial metrics and non-financial metrics, and how those results are measured, presented and compare to analyst expectations.

As a result of these factors, our stock price may continue to be volatile and investors may be unable to sell their shares at a price equal to, or above, the price paid. Any significant drops in our stock price could give rise to shareholder lawsuits, which are costly and time consuming to defend against and which may adversely affect our ability to raise capital while the suits are pending, even if the suits are ultimately resolved in our favor.

In addition, if the market for pharmaceutical stocks or the stock market in general experiences uneven investor confidence, the market price of our common stock could decline for reasons unrelated to our business, operating results or financial condition. For example, if one or more securities or industry analysts downgrades our stock or publishes an inaccurate research report about our company, the market price for our common stock would likely decline. The market price of our common stock might also decline in reaction to events that affect other companies within, or outside, our industry even if these events do not directly affect us.

We have incurred operating losses in the past and may incur operating losses in the future.

To date, we have recorded revenues from product sales, license fees, royalties, collaborative research and development arrangements and feasibility studies. In 2017, 2016 and 2015 we incurred net losses of $102.5 million. $88.7 million and $75.7 million, respectively. We expect to incur operating losses in 2018 and may continue to incur operating losses in future years. Any such losses may have an adverse impact on our total assets, shareholders' equity and working capital.

Our existing capital resources may not be sufficient to fund our future operations or product acquisitions and strategic transactions that we may pursue.

We fund our operations primarily through revenues from product sales and do not have any committed sources of capital. To the extent that our existing capital resources and revenues from ongoing operations are insufficient to fund our future operations, or product acquisitions and strategic transactions that we may pursue, we will have to raise additional funds through the sale of our equity securities, through additional debt financing, from development and

licensing arrangements or from the sale of assets. We may be unable to raise such additional capital on favorable terms, or at all. If we raise additional capital by selling our equity or convertible debt securities, the issuance of such securities could result in dilution of our shareholders' equity positions.

We have significant amounts of intangible assets which depend upon future positive cash flows to support the values recorded in our balance sheet. We may have an increased risk of future impairment charges should actual financial results differ materially from our projections.

Our consolidated balance sheet contains significant amounts of intangible assets representing the product rights which we have acquired over the last few years. We review the carrying value of our intangible assets when indicators of impairment are present. Conditions that could indicate impairment of intangible assets include, but are not limited to, a significant adverse change in market conditions, significant competing product launches by our competitors and the legal or regulatory environment.

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In performing our impairment tests, we utilize our future projections of cash flows. Projections of future cash flows are inherently subjective and reflect assumptions that may or may not ultimately be realized. Significant assumptions utilized in our projections include, but are not limited to, our evaluation of the market opportunity for our products, the current and future competitive landscape and resulting impacts to product pricing, future regulatory actions, planned strategic initiatives and the realization of benefits associated with our existing patents. Given the inherent subjectivity and uncertainty in projections, we could experience significant unfavorable variances in future periods or revise our projections downward. This would result in an increased risk that our intangible assets may be impaired. If an impairment were recognized, this could have a material adverse effect on our financial condition and results of operations.

Our customer concentration may materially adversely affect our financial condition and results of operations.

We and our commercialization partners sell a significant amount of our products to a limited number of independent wholesale drug distributors. Three of our wholesale distributors represented 30%, 30% and 24% for the three months ended March 31, 2018 and 36%, 27% and 26% for the year ended December 31, 2017, of our product shipments. If we, or our commercialization partners, were to lose the business of one or more of these distributors, if any of these distributors failed to fulfill their obligations, if any of these distributors experienced difficulty in paying us or our commercialization partners on a timely basis, or if any of these distributors negotiated lower pricing terms, it could have a material adverse effect on our competitive position, business, financial condition, results of operations and cash flows.

Our product revenues have historically been lower in the first quarter of the year as compared to the fourth quarter of the preceding year, which may cause our stock price to decline.

Our product revenues have historically been lower in the first quarter of the year as compared to the fourth quarter of the preceding year. We believe this arises primarily as a result of wholesalers’ reductions of inventory of our products in the first quarter and annual changes in health insurance plans that occur at the beginning of the calendar year.

In 2013, 2014, 2015, and 2016, our wholesalers ended the calendar year with higher levels of inventory of our products than at the end of the first quarter of the following year. As a result, in the first quarters of 2014, 2015, 2016 and 2017, net sales were lower than would otherwise have been the case as a result of the reduction of product inventory at our wholesalers. Any material reduction by our wholesalers of their inventory of our products in the first quarter of any calendar year as compared to the fourth quarter of the preceding calendar year, could adversely affect our operating results and may cause our stock price to decline.

Many health insurance plans and government programs reset annual limits on deductibles and out-of-pocket costs at the beginning of each calendar year and require participants to pay for substantially all of the costs of medical services

and prescription drug products until such deductibles and annual out-of-pocket cost limits are met. In addition, enrollment in high-deductible health insurance plans has increased significantly in recent years. As a result of these factors, patients may delay filling or refilling prescriptions for our products or substitute less expensive generic products until such deductibles and annual out-of-pocket cost limits are met. Any reduction in the demand for our products, including those marketed by our commercialization partners as a result of the foregoing factors or otherwise, could adversely affect our business, operating results and financial condition.

Our commercialization and collaborative arrangements may give rise to disputes over commercial terms, contract interpretation and ownership or protection of our intellectual property and may adversely affect the commercial success of our products.

We currently have a commercialization agreement with Collegium. We currently have collaboration or license arrangements with a number of companies, including Grünenthal, Janssen Pharma and Ironwood. In addition, we have in the past and may in the future enter into other commercialization or collaborative arrangements, some of which have been based on less definitive agreements, such as memoranda of understanding, material transfer agreements, options or feasibility agreements. We may not execute definitive agreements formalizing these arrangements.

Commercialization and collaborative relationships are generally complex and may give rise to disputes regarding the relative rights, obligations and revenues of the parties, including the ownership of intellectual property and associated rights and obligations, especially when the applicable collaborative provisions have not been fully negotiated

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and documented. Such disputes can delay collaborative research, development or commercialization of potential products, and can lead to lengthy, expensive litigation or arbitration. The terms of such arrangements may also limit or preclude us from developing products or technologies developed pursuant to such collaborations. Additionally, the commercialization or collaborative partners under these arrangements might breach the terms of their respective agreements or fail to maintain, protect or prevent infringement of the licensed patents or our other intellectual property rights by third parties. Moreover, negotiating commercialization and collaborative arrangements often takes considerably longer to conclude than the parties initially anticipate, which could cause us to enter into less favorable agreement terms that delay or defer recovery of our development costs and reduce the funding available to support key programs. Any failure by our commercialization or collaborative partners to abide by the terms of their respective agreements with us, including their failure to accurately calculate, report or pay any royalties payable to us, may adversely affect our results of operations.

We may be unable to enter into future commercialization or collaborative arrangements on acceptable terms, which could harm our ability to develop and commercialize our current and potential future products and technologies. Other factors relating to collaborations that may adversely affect the commercial success of our products include:

- any parallel development by a commercialization or collaborative partner of competitive technologies or products;
- arrangements with commercialization or collaborative partners that limit or preclude us from developing products or technologies;
- premature termination of a commercialization or collaboration agreement; or
- failure by a commercialization or collaborative partner to devote sufficient resources to the development and commercial sales of products using our current and potential future products and technologies.

Our commercialization or collaborative arrangements do not necessarily restrict our commercialization or collaborative partners from competing with us or restrict their ability to market or sell competitive products. Our current and any future commercialization or collaborative partners may pursue existing or other development-stage products or alternative technologies in preference to those being commercialized or developed in collaboration with us. Our commercialization or collaborative partners may also terminate their relationships with us or otherwise decide not to proceed with development or commercialization of our products.

We may be unable to protect our intellectual property and may be liable for infringing the intellectual property of others.

Our success will depend in part on our ability to obtain and maintain patent protection for our products and technologies, and to preserve our trade secrets. Our policy is to seek to protect our proprietary rights by, among other methods, filing patent applications in the U.S. and foreign jurisdictions to cover certain aspects of our technology. We hold issued U.S. patents and have patent applications pending in the U.S. In addition, we are pursuing patent applications relating to our technologies in the U.S. and abroad. We have also applied for patents in numerous foreign countries. Some of those countries have granted our applications and other applications are still pending. Our pending patent applications may lack priority over other applications or may not result in the issuance of patents. Even if

issued, our patents may not be sufficiently broad to provide protection against competitors with similar technologies and may be challenged, invalidated or circumvented, which could limit our ability to stop competitors from marketing related products or may not provide us with competitive advantages against competing products. We also rely on trade secrets and proprietary know-how, which are difficult to protect. We seek to protect such information, in part, by entering into confidentiality agreements with employees, consultants, collaborative partners and others before such persons or entities have access to our proprietary trade secrets and know-how. These confidentiality agreements may not be effective in certain cases, due to, among other things, the lack of an adequate remedy for breach of an agreement or a finding that an agreement is unenforceable. In addition, our trade secrets may otherwise become known or be independently developed by competitors.

Our ability to develop our technologies and to make commercial sales of products using our technologies also depends on not infringing other patents or intellectual property rights. We are not aware of any such intellectual property claims directly against us. The pharmaceutical industry has experienced extensive litigation regarding patents and other intellectual property rights. Patents issued to third parties relating to sustained release drug formulations or particular pharmaceutical compounds could in the future be asserted against us, although we believe that we do not infringe any valid claim of any patents. However, in February 2018 Purdue sued Collegium for infringement of three patents owned

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by Purdue that were issued in January 2018 and expire in 2022 arising from Collegium's commercialization of the NUCYNTA franchise of products. Although we are not a defendant in the suit, Purdue has identified the Company as an infringer of the patents due to the Company's manufacture of the products. If claims concerning any of our products were to arise and it was determined that these products infringe a third party's proprietary rights, we or our commercial partners could be subject to substantial damages for past infringement or could be forced to stop or delay activities with respect to any infringing product, unless we or our commercial partner, as applicable, can obtain a license, or our product may need to be redesigned so that it does not infringe upon such third party's patent rights, which may not be possible or could require substantial funds or time. Such a license may not be available on acceptable terms, or at all. Even if we, our collaborators or our licensors were able to obtain a license, the rights may be nonexclusive, which could give our competitors access to the same intellectual property. In addition, any public announcements related to litigation or interference proceedings initiated or threatened against us, even if such claims are without merit, could cause our stock price to decline.

From time to time, we may become aware of activities by third parties that may infringe our patents. Infringement of our patents by others may reduce our market shares (if a related product is approved) and, consequently, our potential future revenues and adversely affect our patent rights if we do not take appropriate enforcement action. We may need to engage in litigation to enforce any patents issued or licensed to us or to determine the scope and validity of third-party proprietary rights. For instance, we have previously been engaged in ANDA litigation involving NUCYNTA, NUCYNTA ER and NUCYNTA oral solution as well as Gralise and Zipsor. It is possible our issued or licensed patents may not be held valid by a court of competent jurisdiction or the PTAB. Whether or not the outcome of litigation or the PTAB proceeding is favorable to us, the litigation and the proceedings may take significant time, may be expensive and may divert management's attention from other business concerns. We may also be required to participate in derivation proceedings or other post-grant proceedings declared by the U.S. Patent and Trademark Office for the purposes of, respectively, determining the priority of inventions in connection with our patent applications or determining validity of claims in our issued patents. Adverse determinations in litigation or proceedings at the U.S. Patent and Trademark Office could adversely affect our business, results of operations and financial condition and could require us to seek licenses which may not be available on commercially reasonable terms, or at all, or subject us to significant liabilities to third parties. If we need but cannot obtain a license, we may be prevented from marketing the affected product.

We are subject to risks associated with NDAs submitted under Section 505(b)(2) of the Food, Drug and Cosmetic Act.

The products we develop or acquire generally are or will be submitted for approval under Section 505(b)(2) of the FDCA, which was enacted as part of the Drug Price Competition and Patent Term Restoration Act of 1984, otherwise known as the Hatch-Waxman Act. Section 505(b)(2) permits the submission of an NDA where at least some of the information required for approval comes from studies not conducted by or for the applicant and for which the applicant has not obtained a right of reference. For instance, the NDA for Gralise relies on the FDA's prior approval of Neurontin, the immediate release formulation of gabapentin initially approved by the FDA.

For NDAs submitted under Section 505(b)(2) of the FDCA, the patent certification and related provisions of the Hatch-Waxman Act apply. In accordance with the Hatch-Waxman Act, such NDAs may be required to include

certifications, known as “Paragraph IV certifications,” that certify any patents listed in the Orange Book publication in respect to any product referenced in the 505(b)(2) application are invalid, unenforceable and/or will not be infringed by the manufacture, use or sale of the product that is the subject of the 505(b)(2) application. Under the Hatch-Waxman Act, the holder of the NDA which the 505(b)(2) application references may file a patent infringement lawsuit after receiving notice of the Paragraph IV certification. Filing of a patent infringement lawsuit triggers a one-time automatic 30-month stay of the FDA’s ability to approve the 505(b)(2) application. Accordingly, we may invest a significant amount of time and expense in the development of one or more products only to be subject to significant delay and patent litigation before such products may be commercialized, if at all. A Section 505(b)(2) application may also not be approved until any non-patent exclusivity, such as exclusivity for obtaining approval of a new chemical entity, listed in the Orange Book for the referenced product has expired. The FDA may also require us to perform one or more additional clinical studies or measurements to support the change from the approved product. The FDA may then approve the new formulation for all or only some of the indications sought by us. The FDA may also reject our future Section 505(b)(2) submissions and may require us to file such submissions under Section 501(b)(1) of the FDCA, which could be considerably more expensive and time consuming.

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The development of drug candidates such as cosyntropin, is inherently difficult and uncertain, and we cannot be certain that any of our product candidates or those of our collaborative partners will be approved for marketing or, if approved, will achieve market acceptance.

Clinical development is a long, expensive and uncertain process and is subject to delays and failures. As a condition to regulatory approval, each product candidate must undergo extensive and expensive preclinical studies and clinical trials to demonstrate to a statistically significant degree that the product candidate is safe and effective. The results at any stage of the development process may lack the desired safety, efficacy or pharmacokinetic characteristics. Positive or encouraging results of prior clinical trials are not necessarily indicative of the results obtained in later clinical trials, as has occurred in the past in certain of our Phase 3 trials. Further, product candidates in later clinical trials may fail to show the desired safety and efficacy despite having progressed in development. In addition, data obtained from pivotal clinical trials are susceptible to varying interpretations, which could delay, limit or prevent regulatory approval.

Product candidates, such as cosyntropin, are subject to the risk that any or all of them may be found to be ineffective or unsafe, or otherwise may fail to receive necessary regulatory clearances. The FDA or other applicable regulatory agencies may determine that our data is not sufficiently compelling to warrant marketing approval and require us to engage in additional clinical trials or provide further analysis, which may be costly and time-consuming. A number of companies in the pharmaceutical industry, including us, have suffered significant setbacks in clinical trials, even in advanced clinical trials after showing positive results in preclinical studies or earlier clinical trials. If our current or future product candidates fail at any stage of development, they will not receive regulatory approval, we will not be able to commercialize them and we will not receive any return on our investment in those product candidates.

Other factors could delay or result in the termination of our current and future clinical trials and related development programs, including:

- negative or inconclusive results;
- patient noncompliance with the protocol;
- adverse medical events or side effects among patients during the clinical trials;
- FDA inspections of our clinical operations;
- failure to meet FDA preferred or recommended clinical trial design, end points or statistical power;
- failure to comply with good clinical practices;
- failure of our third party clinical trial vendors to comply with applicable regulatory laws and regulations;
- compliance with applicable laws and regulations;
- inability of our third party clinical trial vendors to satisfactorily perform their contractual obligations, comply with applicable laws and regulations or meet deadlines;
- delays or failures in obtaining clinical materials and manufacturing sufficient quantities of the product candidate for use in our clinical trials
- delays or failures in recruiting qualified patients to participate in our clinical trials; and
- actual or perceived lack of efficacy or safety of the product candidate.

We are unable to predict whether any product candidates, including cosyntropin, will receive regulatory clearances or be successfully manufactured or marketed. Further, due to the extended testing and regulatory review process required before marketing clearance can be obtained, the time frame for commercializing a product is long and uncertain. Even if cosyntropin and any other product candidates receive regulatory clearance, these products may not achieve or maintain market acceptance. If it is discovered that our or our collaborators' products or technologies could have adverse effects or other characteristics that indicate they may be ineffective as therapeutics, our product development efforts and our business could be significantly harmed.

Even assuming our or our collaborative partners' products obtain regulatory approval, successful commercialization requires:

- market acceptance;
- a cost-effective commercial scale production; and
- reimbursement under private or governmental health plans.

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Any material delay or failure in the governmental approval process and/or the successful commercialization of our potential products or those of our collaborative partners could adversely impact our business, financial condition and results of operations.

We and our collaborative partners customarily depend on third party contract research organizations, clinical investigators and clinical sites to conduct clinical trials with regard to product candidates, and if they do not perform their regulatory, legal and contractual obligations, or successfully enroll patients in and manage our clinical trials, we and our collaborative partners may not be able to obtain regulatory approvals for product candidates, including cosyntropin.

We and our collaborative partners customarily rely on third party contract research organizations and other third parties to assist us in designing, managing, monitoring and otherwise conducting clinical trials. We and our collaborative partners do not control these third parties and, as a result, we and our collaborative partners may be unable to control the amount and timing of resources that they devote to our or our collaborative partners' clinical trials.

Although we and our collaborative partners rely on third parties to conduct clinical trials, we and our collaborative partners are responsible for confirming that each clinical trials is conducted in accordance with its general investigational plan and protocol, as well as the FDA's and other applicable regulatory agencies' requirements, including good clinical practices, for conducting, recording and reporting the results of clinical trials to ensure that the data and results are credible and accurate and that the trial participants are adequately protected. If we, contract research organizations or other third parties assisting us or our collaborative partners with clinical trials fail to comply with applicable good clinical practices, the clinical data generated in such clinical trials may be deemed unreliable and the FDA, or other applicable regulatory agencies, may require us or our collaborative partners to perform additional clinical trials before approving any marketing applications with regard to product candidates. We cannot be certain that, upon inspection, the FDA or other applicable regulatory agencies will determine that any of our clinical trials or our collaborative partners comply with good clinical practices. In addition, clinical trials must be conducted with product produced under the FDA's cGMP regulations and similar regulations outside of the U.S. Our or our collaborative partners' failure, or the failure of our product manufacturers, to comply with these regulations may require the repeat or redesign of clinical trials, which would delay the regulatory approval process.

We and our collaborative partners also customarily rely on clinical investigators and clinical sites to enroll patients and other third parties to manage clinical trials and to perform related data collection and analysis. If clinical investigators and clinical sites fail to enroll a sufficient number of patients in such clinical trials or fail to enroll them on the planned schedule, these trials may not be completed or completed as planned, which could delay or prevent us or our collaborative partners from obtaining regulatory approvals for product candidates.

Agreements with clinical investigators and clinical sites for clinical testing and for trial management services place substantial responsibilities on these parties, which could result in delays in, or termination of, clinical trials if these

parties fail to perform as expected. If these clinical investigators, clinical sites or other third parties do not carry out their contractual duties or obligations or fail to meet expected deadlines, or if the quality or accuracy of the clinical data they obtain is compromised due to their failure to adhere to clinical protocols or for other reasons, clinical trials may be extended, delayed or terminated, and we and our collaborative partners may be unable to obtain regulatory approval for, or successfully commercialize, product candidates.

We have recently experienced a significant transition in our Board of Directors and executive management.

We recently experienced significant changes in our Board of Directors and executive management team. If our newly appointed directors, Chief Executive Officer and executive officers are not able to timely develop, implement and execute successful business strategies and plans to maintain and increase our product revenues, our business, financial condition and results of operations will be materially and adversely affected. Moreover, the changes to our Board of Directors and executive management team may result in disruption to the operation of our business. While our newly appointed Chief Executive Officer has significant industry-related experience, he has not previously worked together with some of the other members of our executive management team and it may take time for the team to become fully integrated. Any delay in the integration of our Board of Directors or executive management team could affect our ability to develop, implement and execute our business strategies and plans, which could have a material adverse effect on our business, financial condition and results of operations.

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Further, as a result of the changes to our Board of Directors and executive management, the future business strategies and plans of the Company may differ materially from those we previously pursued. If our business strategies and plans, including our recent commercialization arrangement with Collegium, cause disruption in our business or operations or do not achieve the level of success or results we anticipate, our business, financial condition and results of operations will be materially and adversely affected.

Our ability to successfully manage our transition to our new headquarters could result in a material adverse effect on our business or operations if we underestimate the costs of the transition, experience delays or quality issues with our manufacturing, or if internal measures to mitigate these risks are not effective.

On December 4, 2017, the Company announced its plan to relocate its corporate headquarters to a different state and reduce its staff. The transition may involve unanticipated delays, which could materially impact our desired commercial timelines, and we cannot be certain that we will be able to move into our new headquarters without any material interruption to our business. There may also be additional costs and delays associated with relocation to the new headquarters and such costs may exceed our projections.

Furthermore, we may face significant challenges in relocating our principal executive office to a different state, including difficulties in retaining and attracting officers, key personnel and other employees and challenges in maintaining the continuity of our operations. Employees who are not relocating to our new headquarters will be terminated throughout the first half of 2018 and as a result, may be distracted as they search for new employment. Management may also be required to devote substantial time to relocating our corporate headquarters and related matters, which could otherwise be devoted to focusing on ongoing business operations and other initiatives and opportunities. Any such difficulties could have an adverse effect on our business, results of operations or financial condition.

Our success is dependent in large part upon the continued services of our executive management with whom we do not have employment agreements.

Our success is dependent in large part upon the continued services of members of our executive management team, and on our ability to attract and retain key management and operating personnel, especially in light of our announced headquarters relocation. We do not have agreements with any of our executive officers that provide for their continued employment with us. We may have difficulty filling open senior commercial, scientific and financial positions. Management, scientific and operating personnel are in high demand in our industry and are often subject to competing offers. The loss of the services of one or more members of management or key employees or the inability to hire additional personnel as needed could result in delays in the research, development and commercialization of our products and potential product candidates.

Our financial results are impacted by management's assumptions and use of estimates.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Estimates are used when accounting for amounts recorded in connection with acquisitions, including initial fair value determinations of assets and liabilities as well as subsequent fair value measurements. Additionally, estimates are used in determining items such as sales discounts and returns, depreciable and amortizable lives, share-based compensation assumptions, fair value of contingent consideration and taxes on income. Although management believes these estimates are based upon reasonable assumptions within the bounds of its knowledge of the Company's business and operations, actual results could differ materially from these estimates.

If we are unable to satisfy regulatory requirements relating to internal controls, our stock price could suffer.

Section 404 of the Sarbanes-Oxley Act of 2002 requires companies to conduct a comprehensive evaluation of the effectiveness of their internal control over financial reporting. At the end of each fiscal year, we must perform an evaluation of our internal control over financial reporting, include in our annual report the results of the evaluation and have our external auditors also publicly attest to the effectiveness of our internal control over financial reporting.

Our ability to produce accurate financial statements and comply with applicable laws, rules and regulations is largely dependent on our maintenance of internal control and reporting systems, as well as on our ability to attract and

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retain qualified management and accounting personnel to further develop our internal accounting function and control policies. If we fail to effectively establish and maintain such reporting and accounting systems or fail to attract and retain personnel who are capable of designing and operating such systems, these failures will increase the likelihood that we may be required to restate our financial results to correct errors or that we will become subject to legal and regulatory infractions, which may entail civil litigation and investigations by regulatory agencies including the SEC. In addition, if material weaknesses are found in our internal controls in the future, if we fail to complete future evaluations on time or if our external auditors cannot attest to the effectiveness of our internal control over financial reporting, we could fail to meet our regulatory reporting requirements and be subject to regulatory scrutiny and a loss of public confidence in our internal controls, which could have an adverse effect on our stock price or expose us to litigation or regulatory proceedings, which may be costly or divert management attention.

Changes in fair value of contingent consideration assumed as part of our acquisitions could adversely affect our results of operations.

Contingent consideration obligations arise from the Zipsor and CAMBIA acquisitions and relate to the potential future contingent milestone payments and royalties payable under the respective agreements. The contingent consideration is initially recognized at its fair value on the acquisition date and is re-measured to fair value at each reporting date until the contingency is resolved with changes in fair value recognized in earnings. The estimates of fair values for the contingent consideration contain uncertainties as it involves assumptions about the probability assigned to the potential milestones and royalties being achieved and the discount rate. Significant judgment is employed in determining these assumptions as of the acquisition date and for each subsequent period. Updates to assumptions could have a significant impact on our results of operations in any given period.

The conditional conversion feature of the Convertible Notes, if triggered, may adversely affect our financial condition and operating results.

In the event the conditional conversion feature of the Convertible Notes is triggered, holders of Convertible Notes will be entitled to convert the Convertible Notes at any time during specified periods at their option. If one or more holders elect to convert their Convertible Notes, unless we elect to satisfy our conversion obligation by delivering solely shares of our common stock (other than paying cash in lieu of delivering any fractional share), we would be required to settle a portion or all of our conversion obligation in cash, which could adversely affect our liquidity. In addition, even if holders do not elect to convert their Convertible Notes, we could be required under applicable accounting rules to reclassify all or a portion of the outstanding principal of the Convertible Notes as a current rather than long-term liability, which would result in a material reduction of our net working capital.

The accounting method for convertible debt securities that may be settled in cash, such as the Convertible Notes could have a material effect on our reported financial results.

In May 2008, FASB issued FASB Staff Position No. APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement), which has subsequently been codified as Accounting Standards Codification 470-20, Debt with Conversion and Other Options (ASC 470-20). Under ASC 470-20, an entity must separately account for the liability and equity components of the convertible debt instruments (such as the Convertible Notes) that may be settled entirely or partially in cash upon conversion in a manner that reflects the issuer's economic interest cost. The effect of ASC 470-20 on the accounting for the Convertible Notes is that the equity component is required to be included in the additional paid-in capital within shareholders' equity on our consolidated balance sheet at the issuance date and the value of the equity component would be treated as debt discount for purposes of accounting for the debt component of the Convertible Notes. As a result, we have been required to record a greater amount of non-cash interest expense as a result of the accretion of the discounted carrying value of the Convertible Notes to their face amount over the term of the notes. We will report lower net income (or larger net losses) in our financial results because ASC 470-20 requires interest to include both the accretion of the debt discount and the instrument's non-convertible coupon interest rate, which adversely affects our reported or future financial results and may adversely affect the trading price of our common stock.

In addition, if the Convertible Notes become convertible, we are required under applicable accounting rules to reclassify all or a portion of the outstanding principal of the Convertible Notes as a current rather than a long-term liability, which would result in a material reduction of our net working capital. Finally, we use the if-converted method

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to compute diluted earnings per share with respect to our convertible debt, which could be more dilutive than assuming the debt would be settled in cash.

Any of these factors could cause a decrease in the market price of our common stock.

Our business could be negatively affected as a result of any future proxy fight or the actions of activist shareholders.

On October 17, 2016, we and Starboard Value LP (Starboard) entered into a settlement agreement pursuant to which, among other things, (i) three independent directors appointed by Starboard joined our Board of Directors, (ii) we amended our bylaws to move the window for shareholders director nominations and other shareholder proposals for consideration at the 2017 annual meeting of shareholders to March 15, 2017 through April 15, 2017 and (iii) Starboard agreed to withdraw its request for the Special Meeting scheduled to be held on November 15, 2016. On March 28, 2017, we and Starboard entered into a cooperation and support agreement pursuant to which, among other things, two additional independent directors appointed by Starboard joined our Board of Directors and the parties agreed to certain standstill commitments.

Another proxy contest or related activities with Starboard or other activist shareholders, could adversely affect our business for a number of reasons, including, but not limited to the following:

- responding to proxy contests and other actions by activist stockholders can be costly and time-consuming, disrupting our operations and diverting the attention of management and our employees;
- perceived uncertainties as to our future direction may result in the loss of potential business opportunities and may make it more difficult to attract and retain qualified personnel, business partners, customers and others important to our success, any of which could negatively affect our business and our results of operations and financial condition; and
- if nominees advanced by activist shareholders are elected or appointed to our Board of Directors with a specific agenda, it may adversely affect our ability to effectively and timely implement our strategic plans or to realize long-term value from our assets, and this could in turn have an adverse effect on our business and on our results of operations and financial condition.

A proxy contest could also cause our stock price to experience periods of volatility. Further, if a proxy contest results in a change in control of our Board of Directors, such an event could give third parties certain rights under our existing contractual obligations, which could adversely affect our business.

We may be subject to disruptive unsolicited takeover attempts in the future.

We have in the past and may in the future be subject to unsolicited attempts to gain control of our company. Responding to any such attempt would distract management attention away from our business and would require us to incur significant costs. Moreover, any unsolicited takeover attempt may disrupt our business by causing uncertainty among current and potential employees, producers, suppliers, customers and other constituencies important to our success, which could negatively impact our financial results and business initiatives. Other disruptions to our business include potential volatility in our stock price and potential adverse impacts on the timing of, and our ability to consummate, acquisitions of products and companies.

Certain provisions applicable to the Convertible Notes and the Senior Notes could delay or prevent an otherwise beneficial takeover or takeover attempt.

Certain provisions applicable to the Convertible Notes and the indenture governing the Convertible Notes, the Senior Notes and the Note Purchase Agreement, could make it more difficult or more expensive for a third party to acquire us. For example, if an acquisition event constitutes a fundamental change under the indenture for the Convertible Notes or a major transaction under the Note Purchase Agreement, holders of the Convertible Notes or the Senior Notes, as applicable, will have the right to require us to repurchase their notes in cash. In addition, if an acquisition event constitutes a “make-whole fundamental change” under the indenture, we may be required to increase the conversion rate for holders who convert their Convertible Notes in connection with such make-whole fundamental change. In any of these cases, and in other cases, our obligations under the Convertible Notes and the indenture, the Senior Notes and the Note Purchase Agreement, as well as provisions of our organizational documents and other agreements, could increase the cost of acquiring us or otherwise discourage a third party from acquiring us or removing incumbent management.

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Provisions in our restated articles of incorporation, bylaws and California law might discourage, delay or prevent a change of control of our company or changes in our management and, therefore, depress the market price of our common stock.

Certain provisions of our articles of incorporation and the California General Corporation Law could discourage a third party from acquiring, or make it more difficult for a third party to acquire, control of our company without the approval of our Board of Directors. These provisions could also limit the price that certain investors might be willing to pay in the future for shares of our common stock. Certain provisions allow the Board of Directors to authorize the issuance of preferred stock with rights superior to those of the common stock.

On July 12, 2015, our Board of Directors adopted and approved an amendment and restatement to our bylaws (the Amended Bylaws). The Amended Bylaws, among other things, provide for the establishment of a measurement record date for purposes of ascertaining shareholders eligible to call for a special meeting of shareholders and establish certain other procedures relating to the calling of a special meeting of shareholders. The Amended Bylaws also supplement the advanced notice requirements and procedures for the submission by shareholders of nominations for the Board of Directors and of other proposals to be presented at shareholder meetings, and provide that the exclusive forum for any shareholder to bring any: (i) derivative action, (ii) claim asserting a breach of fiduciary duty, (iii) action under the California Corporations Code or our organizational documents or (iv) other action relating to our internal affairs, shall in each case be the Santa Clara County Superior Court within the State of California or, if no state court located within the State of California has jurisdiction, the federal district court for the Northern District of California. The Amended Bylaws also make certain other ministerial changes.

We are also subject to the provisions of Section 1203 of the California General Corporation Law, which requires a fairness opinion to be provided to our shareholders in connection with their consideration of any proposed “interested party” reorganization transaction.

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

We have never declared or paid any cash dividends on our common stock. We currently anticipate that we will retain future earnings for the development, operation and expansion of our business and do not anticipate declaring or paying any cash dividends for the foreseeable future. In addition, our ability to pay cash dividends on our common stock may be prohibited or limited by the terms of any future debt financing arrangement. Any return to shareholders will therefore be limited to the increase, if any, of our stock price.

Business interruptions could limit our ability to operate our business and may also effect the success of our commercialization partners.

Our operations and infrastructure, and those of our partners, third party suppliers and vendors are vulnerable to damage or interruption from cyber-attacks and security breaches, human error, natural disasters, fire, flood, the effects of climate change, power loss, telecommunications failures, equipment failures, intentional acts of theft, vandalism, terrorism and similar events. In particular, our corporate headquarters are located in the San Francisco Bay area, which has a history of seismic activity. We have not established a formal disaster recovery plan, and our back-up operations and our business interruption insurance may not be adequate to compensate us for losses that occur. A significant business interruption could result in losses or damages incurred by us and require us to cease or curtail our operations.

For example, Hurricanes Irma and Maria caused significant devastation and damage throughout Puerto Rico in 2017, including widespread flooding and power loss. As a result, we experienced delays in the manufacture, packaging and delivery of certain dosage strengths of NUCYNTA ER in fourth quarter of 2017 and the first quarter of 2018. We and Collegium may continue to experience further outages in the future. Any delay in the manufacture, packaging or delivery of NUCYNTA ER and NUCYNTA could adversely affect the success of our commercialization partner Collegium, which in turn could adversely affect our business, financial condition and results of operations.

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Data breaches and cyber-attacks could compromise our intellectual property or other sensitive information and cause significant damage to our business.

In the ordinary course of our business, we collect, maintain and transmit sensitive data on our computer networks and information technology systems, including our intellectual property and proprietary or confidential business information. The secure maintenance of this information is critical to our business. We believe that companies have been increasingly subject to a wide variety of security incidents, cyber-attacks and other attempts to gain unauthorized access. These threats can come from a variety of sources, ranging in sophistication from an individual hacker to a state-sponsored attack and motives (including corporate espionage). Cyber threats may be generic, or they may be custom-crafted to target our information systems. Cyber-attacks are becoming increasingly more prevalent and much harder to detect and defend against. Our network and storage applications and those of our third party vendors may be subject to unauthorized access by hackers or breached due to operator error, malfeasance or other system disruptions.

It is often difficult to anticipate or immediately detect such incidents and the damage caused by such incidents. These data breaches and any unauthorized access or disclosure of our information or intellectual property could compromise our intellectual property and expose sensitive business information, including the information of our business partners. Cyber-attacks could cause us to incur significant remediation costs, result in product development delays, disrupt key business operations and divert attention of management and key information technology resources. Our network security and data recovery measures and those of our third party vendors may not be adequate to protect against such security breaches and disruptions. These incidents could also subject us to liability, expose us to significant expense and cause significant harm to our business.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Not applicable.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

Not applicable.

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ITEM 6. EXHIBITS

(a) Exhibits

3.1	(1)	Third Amended and Restated Articles of Incorporation
3.2	(2)	Certificate of Amendment to Amended and Restated Articles of Incorporation
3.3	(3)	Certificate of Amendment to Amended and Restated Articles of Incorporation
3.4	(4)	Certificate of Determination of Series RP Preferred Stock of the Company
3.5	(5)	Certificate of Amendment to Certificate of Determination of Series RP Preferred Stock of the Company
3.6	(5)	Certificate of Determination of Series B Junior Participating Preferred Stock of the Company
3.7	(6)	Certificate of Amendment to Certificate of Determination of Series A Preferred Stock
3.8	(7)	Amended and Restated Bylaws
10.1	(*)	Office Lease dated February 28, 2018 by and between the Company and Lake Forest Landmark Company LLC
31.1	(*)	Certification pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 of Arthur J. Higgins
31.2	(*)	Certification pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934 of August J. Moretti
32.1	(**)	Certification pursuant to 18 U.S.C. Section 1350 of Arthur J. Higgins
32.2	(**)	Certification pursuant to 18 U.S.C. Section 1350 of August J. Moretti
101	(*)	Interactive Data Files pursuant to Rule 405 of Regulation S-T

(1)Incorporated by reference to the Company’s registration statement on Form SB-2 (File No. 333-25445)

(2)Incorporated by reference to the Company’s Form 10-K filed on March 31, 2003 (File No. 001-13111)

(3)Incorporated by reference to the Company’s Form 8-K filed on May 19, 2015 (File No. 001-13111)

(4)Incorporated by reference to the Company’s Form 10-Q filed on May 10, 2005 (File No. 001-13111)

(5)Incorporated by reference to the Company’s Form 8-K filed on July 13, 2015 (File No. 001-13111)

(6)Incorporated by reference to the Company’s Form 8-K filed on July 29, 2015 (File No. 001-13111)

(7)Incorporated by reference to the Company’s Form 8-K filed on May 22, 2017 (File No. 001-13111)

(*)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.

Date: May 10, 2018 DEPOMED, INC.

/s/ Arthur J. Higgins
Arthur J. Higgins
President and Chief Executive Officer

/s/ August J. Moretti
August J. Moretti
Chief Financial Officer