

INSMED INC  
Form 10-Q  
May 13, 2009

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

FORM 10-Q  
(Mark One)

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

For the quarterly period ended March 31, 2009

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 0-30739

INSMED INCORPORATED

(Exact name of registrant as specified in its charter)

Virginia  
(State or other jurisdiction of  
incorporation or organization)

54-1972729  
(I.R.S. Employer  
Identification No.)

8720 Stony Point Parkway  
Richmond, Virginia 23235  
(Address of principal executive offices)

(804) 565-3000  
(Registrant's telephone number,  
including area code)

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

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

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

Large accelerated filer            Accelerated filer

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Non-accelerated filer  Smaller reporting company

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

As of May 1, 2009, the latest practicable date, there were 124,972,146 shares of Insmed Incorporated common stock outstanding.

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INSMED INCORPORATED

FORM 10-Q

For the Quarterly Period Ended March 31, 2009

PART I. FINANCIAL INFORMATION

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PART I  
FINANCIAL INFORMATION  
ITEM 1. FINANCIAL STATEMENTS  
INSMED INCORPORATED  
Consolidated Balance Sheets  
(in thousands, except share and per share data)

	(unaudited) March 31, 2009	December 31, 2008
Assets		
Current assets:		
Cash, cash equivalents and short-term investments	\$ 127,540	\$ 2,397
Accounts receivable, net	114	122
Prepaid expenses	30	74
Total current assets	127,684	2,593
Long-term assets:		
Certificate of deposit	2,085	-
Restricted cash, long-term	-	2,095
Deferred financing costs, net	51	70
Total long-term assets	2,136	2,165
Total assets	\$ 129,820	\$ 4,758
Liabilities and stockholders' equity (deficit)		
Current liabilities:		
Accounts payable	\$ 2,667	\$ 1,277
Accrued project costs & other	795	936
Payroll liabilities	5,048	453
Income taxes payable	2,794	-
Restricted stock unit liability	-	113
Interest payable	10	13
Deferred rent	103	168
Deferred revenue	232	302
Convertible debt	2,211	2,211
Debt discount	(476)	(596)
Net convertible debt	1,735	1,615
Total current liabilities	13,384	4,877
Long-term liabilities:		
Convertible debt	-	553
Debt discount	-	(66)
Net long-term convertible debt	-	487
Asset retirement obligation	-	2,217

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Total liabilities	13,384	7,581
Stockholders' equity (deficit):		
Common stock; \$.01 par value; authorized shares 500,000,000; issued and outstanding shares, 124,972,146 in 2009 and 122,494,010 in 2008	1,250	1,225
Additional paid-in capital	343,817	342,378
Accumulated deficit	(228,631)	(346,426)
Net stockholders' equity (deficit)	116,436	(2,823)
Total liabilities and stockholders' equity (deficit)	\$ 129,820	\$ 4,758

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

INSMED INCORPORATED  
 Consolidated Statements of Operations  
 (in thousands, except per share data - unaudited)

	Three Months Ended	
	March 31,	
	2009	2008
Royalties	\$ 28	\$ 25
Grant revenue	272	-
Other expanded access program income, net	2,070	2,328
Total revenues	2,370	2,353
Operating expenses:		
Research and development	5,868	5,368
Selling, general and administrative	3,449	1,391
Realized loss on investments	-	392
Total expenses	9,317	7,151
Operating loss	(6,947)	(4,798)
Interest income	23	279
Interest expense	(242)	(354)
Gain on sale of asset, net	127,755	-
Income (loss) before taxes	120,589	(4,873)
Income tax expense	2,794	-
Net income (loss)	\$ 117,795	\$ (4,873)
Basic net income (loss) per share	\$ 0.96	\$ (0.04)
Shares used in computing basic net profit (loss) per share	122,522	121,904
Diluted net income (loss) per share	\$ 0.96	\$ (0.04)
Shares used in computing diluted net profit (loss) per share	122,698	121,904

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

INSMED INCORPORATED  
Consolidated Statements of Cash Flows  
(in thousands - unaudited)

	Three Months Ended	
	March 31, 2009	2008
Operating activities		
Net income (loss)	\$ 117,795	\$ (4,873)
Adjustments to reconcile net income (loss) to net cash used in operating activities:		
Depreciation and amortization	205	292
Stock based compensation expense	1,439	133
Gain on sale of asset, net	(127,755)	-
Realized loss on investments	-	392
Changes in operating assets and liabilities:		
Accounts receivable	8	(77)
Other assets	44	134
Accounts payable	1,390	(100)
Accrued project costs & other	(141)	12
Payroll liabilities	4,595	168
Income tax liability	2,794	-
Deferred rent	(65)	-
Deferred income	(70)	26
Restricted stock unit liability	(113)	-
Asset retirement obligation	(2,217)	-
Interest payable	(3)	(3)
Net cash used in operating activities	(2,094)	(3,896)
Investing activities		
Cash received from asset sale, net	127,755	-
Decreases in short-term investments	-	5,601
Net cash provided by investing activities	127,755	5,601
Financing activities		
Repayment of convertible notes	(553)	(553)
Certificate of deposits	10	-
Other	25	-
Net cash used in financing activities	(518)	(553)
Increase in cash and cash equivalents	125,143	1,152
Cash and cash equivalents at beginning of period	2,397	3,554
Cash and cash equivalents at end of period	\$ 127,540	\$ 4,706
Supplemental information		
Cash paid for interest	\$ 38	\$ 68

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

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Insmed Incorporated  
Notes to Consolidated Financial Statements  
(Unaudited)

## 1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) and applicable Securities and Exchange Commission regulations for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly these financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. It is presumed that users of this interim financial information have read or have access to the audited consolidated financial statements contained in the Annual Report on Form 10-K of Insmed Incorporated (“Insmed”, the “Company”, “us” “we” or “our”), for the fiscal year ended December 31, 2008. In the opinion of our management, all adjustments (consisting of normal recurring adjustments) considered necessary for fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for the full year.

On February 12, 2009, we announced that we had entered into a definitive agreement with Merck & Co., Inc. (“Merck”) whereby Merck, through an affiliate, would purchase all assets related to our follow-on biologics platform. On March 31, 2009, we completed the sale of these assets for an aggregate purchase price of \$130 million. After fees related to the transaction, we have received proceeds to date of \$127.8 million as a result of this transaction. Taxes due on the sale will be paid by instalment during the balance of the year resulting in total expected net proceeds of approximately \$125 million.

As part of this transaction, Merck assumed the lease of our Boulder, Colorado-based manufacturing facility and acquired ownership of all the equipment in the building. In addition, upon closing of the transaction, Merck offered positions to employees of the Boulder facility. We retain our Richmond, VA corporate office, which houses our Clinical, Regulatory, Finance, and Administrative functions, in support of the continuing IPLEX™ program. The transfer of the Boulder facility to Merck takes away our internal IPLEX™ production capability. We presently believe, however, that we have sufficient inventory of IPLEX™ to support our current ongoing Amyotrophic Lateral Sclerosis Expanded Access Program (“ALS EAP”) in Europe for approximately the next twelve months together with the IPLEX™ requirement for the clinical trial currently being planned with the FDA for ALS patients in the US. Any requirements for IPLEX™ beyond our currently projected cover period or any significant increase in demand beyond our current commitments either in the Myotonic Muscular Dystrophy (“MMD”) or ALS fields will require that we identify a Contract Manufacturing Organization (“CMO”) to produce the necessary IPLEX™ to meet the demand. We estimate that the tech transfer of our IPLEX™ production process could take 12 to 18 months once a CMO has been identified.

## 2. Summary of Significant Accounting Policies

### Principles of Consolidation

The consolidated financial statements include our accounts and the accounts of our wholly-owned subsidiaries, Insmed Therapeutic Proteins, Incorporated, Insmed Pharmaceuticals, Incorporated and Celtrix Pharmaceuticals, Incorporated. All significant intercompany balances and transactions have been eliminated in consolidation.

### Use of Estimates

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

#### Reclassifications

Certain prior period amounts have been reclassified to conform to the current year presentation.

#### Cash and Cash Equivalents and short-term investments

We consider investments with maturities of three months or less when purchased to be cash equivalents. Short-term investments are available for sale and consist primarily of short-term municipal bonds and treasury securities. These securities are carried at market, which approximates cost. The cost of the specific security sold is used to compute the gain or loss on the sale of short-term investments. The table below details the breakdown of our cash and cash equivalents and our short-term investments:

	March 31, 2009	December 31, 2008
Cash and Cash Equivalents	\$ 127,540	\$ 2,145
Short-Term Investments	-	252
Total Cash and Cash Equivalents and Short-Term Investments	\$ 127,540	\$ 2,397

In June 2007, upon renewal of the lease for our former manufacturing facility located in Boulder, Colorado, we provided a Letter of Credit in the amount of \$2.1 million to cover facility restoration expenses upon termination of the lease. This amount was classified as restricted cash on the balance sheet. The accrued restoration expenses as of December 31, 2008 were \$2.2 million and were recorded in asset retirement obligations on the balance sheet. Subsequent to the transfer of this manufacturing facility to Merck on March 31, 2009, we were no longer required to maintain this letter of credit.

#### Fair Value of Financial Instruments

We consider the recorded cost of our financial instruments, which consist primarily of cash, cash equivalents and short-term investments, to approximate the fair value of the respective assets and liabilities at March 31, 2009 due to the short-term maturities of these instruments. We have adopted Statement of Financial Accounting Standard 157, Fair Value Measurements. We also hold an investment in NAPO Pharmaceuticals, Inc. ("NAPO"), which is currently valued at \$0. During the three month period ended March 31, 2008 we recorded an other than temporary impairment of this investment of \$392,000. This amount is reported as a loss on investments on our statement of operations for 2008.

#### Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board (FASB) issued Statement 123(R), Share-Based Payment, a revision of SFAS No. 123, Accounting for Stock-Based Compensation, which superseded APB Opinion No. 25, Accounting for Stock Issued to Employees. Statement 123(R) addresses the accounting for share-based payment transactions in which a company receives employee services in exchange for equity instruments of the company or liabilities that are based on the fair value of the company's equity instruments or that may be settled by the issuance of such equity instruments. This statement requires that share-based transactions be accounted for using a fair-value-based method to recognize non-cash compensation expense; this expense is recognized ratably over the requisite service period, which generally equals the vesting period of options and shares, and is adjusted for expected forfeitures. We adopted this standard at the beginning of 2006 using the modified prospective method.

## Revenue Recognition

Revenue from our Expanded Access Program in Italy is recognized when the drugs have been provided to program patients and collectibility is assured. Royalties previously paid to Tercica and Genentech are net against Expanded Access Program revenue. Grant revenue is recognized once payment has been received. Shipping and handling costs charged to customers are included in revenue.

## Research and Development

Research and development costs are expensed as incurred. Research and development expenses consist primarily of salaries and related expenses, cost to develop and manufacture drug candidates, patent protection costs, amounts paid to contract research organizations, hospitals and laboratories for the provision of services and materials for drug development and clinical trials. We do not have separate accounting policies for internal or external research and development and we do not conduct any research and development for others. Our expenses related to clinical trials are based on estimates of the services received and efforts expended pursuant to contracts with first party organizations that conduct and manage clinical trials on our behalf. These contracts set forth the scope of work to be completed at a fixed fee or amount per patient enrolled. Payments under these contracts depend on performance criteria such as the successful enrollment of patients or the completion of clinical trial milestones. Expenses are accrued based on contracted amounts applied to the level of patient enrollment and to activity according to the clinical trial protocol.

Litigation costs as they relate to our patents are recorded as research and development expenditures.

## Income Taxes

Income taxes are accounted for in accordance with FASB Statement No. 109, Accounting for Income Taxes (“FASB 109”). Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

FASB 109 also requires that deferred tax assets be reduced by a valuation allowance if it is more likely than not that some portion of the deferred tax asset will not be realized. In evaluating the need for a valuation allowance, we take into account various factors, including the expected level of future taxable income and available tax planning strategies. If actual results differ from the assumptions made in the evaluation of our valuation allowance, we record a change in valuation allowance through income tax expense in the period such determination is made.

In June 2006, FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (“FIN 48”). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with FASB 109. FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. It also provides guidance on disclosure requirements, measurement and classification provisions, and transition requirements. We implemented FIN 48 on January 1, 2007 and due to our accumulated loss position, such implementation did not have a material impact on our consolidated financial statements.

## Net Income (Loss) Per Share

The following table sets forth the computation of basic and diluted (loss) earnings per share:

Three Months Ended  
March 31,  
2009          2008  
(in thousands  
except per share data)

## Numerator:

Net income (loss) for basic and diluted earnings per share	\$	117,795	\$	(4,873)
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## Denominator:

Weighted average shares for basic earnings per share	122,522	121,904
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## Effect of dilutive securities:

Convertible debt	-	-
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Warrants	-	-
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Stock options and restricted stock	176	-
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Denominator for diluted earnings per share	122,698	121,904
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Basic earnings (loss) per share	0.96	(0.04)
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Diluted earnings (loss) per share	0.96	(0.04)
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In prior periods, our diluted net loss per share was the same as our basic net loss per share because all stock options, warrants, and other potentially dilutive securities were antidilutive and, therefore, excluded from the calculation of diluted net loss per share.

### Segment Information

We currently operate in one business segment, which is the development and commercialization of pharmaceutical products for the treatment of metabolic and endocrine diseases. We are managed and operated as one business. A single management team that reports to the Chief Executive Officer comprehensively manages the entire business. We do not operate separate lines of business with respect to our products or product candidates. Accordingly, we do not have separately reportable segments as defined by FASB Statement No. 131, Disclosure about Segments of an Enterprise and Related Information.

### 3. Recent Accounting Pronouncements

In December 2007, FASB ratified Emerging Issue Task Force (“EITF”) Issue No. 07-1, Collaborative Arrangements. The consensus requires participants in a collaborative arrangement to present the results of activities for which they act as the principal on a gross basis and to report any payments received from (made to) other collaborators based on other applicable GAAP or, in the absence of other applicable GAAP, based on analogy to authoritative literature or a reasonable, rational and consistently applied accounting policy election. The consensus also requires significant disclosures related to collaborative arrangements. This Issue was effective for us beginning on January 1, 2009. The adoption of this statement did not have any impact on our financial statements for the period ending March 31, 2009.

In May 2008, FASB issued FSP Accounting Principles Board No. 14–1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement) (“FSP APB 14–1”). FSP APB 14–1 requires the issuer of certain convertible debt instruments that may be settled in cash (or other assets) on conversion (including partial cash settlement) to separately account for the liability and equity components of the instrument in a manner that reflects the issuer's non convertible debt borrowing rate when interest cost is recognized in subsequent periods. FSP APB 14–1 was effective for us beginning on January 1, 2009. The adoption of this statement did not have any impact on our financial statements for the period ending March 31, 2009.

In June 2008, FASB ratified EITF Issue No. 08-4, Transition Guidance for Conforming Changes to Issue No. 98-5 (“EITF No. 08-4”). Per EITF No. 08-4, conforming changes made to EITF Issue No. 98-5, Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios, that result from EITF Issue No. 00-27, Application of Issue No. 98-5 to Certain Convertible Instruments, and SFAS No. 150, Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity, was effective for us beginning after January 1, 2009. The adoption of this statement did not have any impact on our financial statements for the period ending March 31, 2009.

#### 4. Equity Compensation Plan Information

As of March 31, 2009, we had two equity compensation plans under which we were granting stock options and shares of non-vested stock. We are currently granting stock-based awards from our Amended and Restated 2000 Stock Incentive Plan (the “2000 Plan”) and our Amended and Restated 2000 Employee Stock Purchase Plan (the “2000 ESPP”). Both the 2000 Plan and the 2000 ESPP are administered by the Compensation Committee of the Board of Directors and the Board of Directors (the “Board”).

The 2000 Plan was originally adopted by the Board and approved by our shareholders in 2000. Its original ten-year term was extended to March 15, 2015 when the plan was last amended. Under the terms of the 2000 Plan, we are authorized to grant a variety of incentive awards based on our common stock, including stock options (both incentive options and non-qualified options), performance shares and other stock awards. The 2000 Plan currently provides for the issuance of a maximum of 9,250,000 (adjusted for stock splits) shares of common stock. These shares are reserved for awards to all participants in the 2000 Plan, including non-employee directors.

The 2000 ESPP was adopted by the Board on April 5, 2000 and approved by our shareholders on the same date. It was amended by the Board to increase the number of shares available for issuance, and such amendment was approved by our shareholders on May 11, 2005. The 2000 ESPP was subsequently amended and restated by action of the Board on October 4, 2006 and the amendment and restatement was approved by our shareholders on December 14, 2006. Under the terms of the 2000 ESPP, eligible employees have the opportunity to purchase our common stock through stock options granted to them. An option gives its holder the right to purchase shares of our common stock, up to a maximum value of \$25,000 per year. The 2000 ESPP provides for the issuance of a maximum of 1,500,000 shares of our common stock to participating employees.

The following table presents information as of March 31, 2009, with respect to the 2000 Plan and the 2000 ESPP.

Plan Category (1)	Number of Securities to Be Issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (2)
Equity Compensation Plans Approved by Shareholders:			
Amended and Restated 2000 Stock Incentive Plan (3)	3,626,399	\$ 2.10	1,544,809 (2)
Amended and Restated 2000 Employee Stock Purchase Plan	—	—	365,380
<b>Total:</b>	<b>3,626,399</b>	<b>\$ 2.10</b>	<b>1,910,189 (3)</b>

(1) We do not have any equity compensation plans that have not been approved by our shareholders.

- (2) Amounts exclude any securities to be issued upon exercise of outstanding options, warrants and rights.
- (3) To the extent that stock options or stock appreciation rights granted under the 2000 Plan terminate, expire, or are canceled, forfeited, exchanged or surrendered without having been exercised, or if any shares of restricted stock are forfeited, the shares of common stock underlying such grants will again become available for purposes of the 2000 Plan.

A summary of the status of our stock options as of March 31, 2009, and changes for the three months then ended is presented below:

Description	2009	Average Exercise Price	Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Options outstanding at January 1, 2009	4,282,249	\$ 2.31		
Granted	-	-		
Exercised	-	-		
Cancelled	(655,850)	2.10		
Options outstanding at March 31, 2009	3,626,399	2.10	3.17	\$ 234,535
Exercisable at March 31, 2009	3,201,088	\$ 2.24	2.78	\$ 143,332

The fair value of the options granted during the three months ended March 31, 2009 was estimated at the date of grant using a Black-Scholes-Merton option-pricing model. Stock-based compensation expense related to stock options was approximately \$42,867 for the three months ended March 31, 2009.

#### Restricted Stock and Restricted Stock Units

In May 2008, under the 2000 Plan, we began granting Restricted Stock (“RS”) and Restricted Stock Units (“RSU’s”) to eligible employees, including our executives. Each RS and RSU represents a right to receive one share of our common stock or an equivalent cash payment upon the completion of a specific period of continued service or our achievement of certain performance metrics. Shares of RS are valued at the market price of our common stock on the date of grant and RSU’s are valued based on the market price on the date of settlement. RSU’s are classified as liabilities, as they are settled with a cash payment for each unit vested, equal to the fair market value of our common stock on the vesting date. We recognize noncash compensation expense for the fair values of these RS and RSU’s on a straight-line basis over the requisite vesting period of these awards.

Effective on the closing of the Merck transaction on March 31, 2009, all RS and RSU awards were fully vested. Due to the acceleration of the vesting schedule, the Company recognized \$1.4 million in stock-based compensation expense. The weighted-average grant date fair value of RS and RSU’s granted during the three months ended March 31, 2009 was \$1.00. As of March 31, 2009, there were 775,000 RS awards outstanding to our Board of Directors and Company Secretary; the remaining unrecognized stock-based compensation expense relating to these awards is \$775,000 and will be recognized over the next six months in accordance with their vesting schedule.

Below is a table of RS and RSU activity for the three months ended March 31, 2009.

	Number of Shares	
	Restricted Stock	Restricted Stock Units
Outstanding at January 1, 2009	3,155,534	1,846,605

Granted	1,404,323	368,234
Vested	3,784,857	2,214,839
Awarded as shares	2,478,136	-
Awarded as cash/withheld for taxes	1,306,721	2,214,839
Outstanding at March 31, 2009	775,000	-

## 5. Convertible Debt Financings

On March 15, 2005, we entered into several purchase agreements with a group of institutional investors, pursuant to which we issued and sold to such investors certain 5.5% convertible notes in the aggregate principal amount of \$35,000,000, which convert into a certain number of shares of our common stock (the “2005 Notes”) as well as warrants to purchase, in the aggregate, approximately 14,864,883 shares of our common stock, at an exercise price of \$1.36 per share (the “2005 Warrants”).

As of June 1, 2005, the holders of the 2005 Notes began to receive interest payments at a rate of 5.5% per annum, and such interest payments are payable quarterly until March 1, 2010. As of March 1, 2008, the 2005 Notes matured and beginning on March 1, 2008, the holders of the 2005 Notes were entitled to receive nine quarterly installments of \$552,778 in the aggregate each quarter. Any outstanding 2005 Notes must be repaid in cash or converted into shares of our common stock by March 1, 2010. Subject to the terms of the 2005 Note purchase agreements, the holders of the 2005 Notes may convert such notes into shares of our common stock at a conversion price of \$1.295 per share (as adjusted in accordance with certain adjustments for stock splits, dividends and the like) at any time prior to the close of business on March 1, 2010. Between April 1, 2005 and March 31, 2009, we received notices from certain holders of the 2005 Notes electing to voluntarily convert approximately \$30,025,000 principal amount of such notes into approximately 23,185,328 shares of our common stock at the conversion rate of one share of common stock for each \$1.295 in principal amount of the 2005 Notes. Following such conversions and principal repayment as of March 31, 2009, \$2,211,111 principal amount of the 2005 Notes remained outstanding. The holders of the 2005 Notes could elect to convert such principal into an aggregate of approximately 1.7 million shares of our common stock. The holders of the 2005 Notes have the right to require us to repurchase such notes with cash payments upon the occurrence of specified “events of default” and “repurchase events” described in the 2005 Notes. The 2005 Warrants were initially exercisable in the aggregate for 14,864,883 shares of common stock at an exercise price of \$1.36 per share. In connection with our May 2007 public stock offering, the exercise price of the 2005 Warrants was reduced to \$1.21 per share and the 2005 Warrants are currently exercisable into the aggregate of 6,021,692 shares of common stock. The 2005 Warrants will expire on March 15, 2010.

In connection with the issuance of the 2005 Notes and 2005 Warrants, we entered into registration rights agreements with the purchasers thereof pursuant to which we agreed to file a registration statement under the Securities Act of 1933, as amended, registering for resale the shares of our common stock issuable upon the conversion of the 2005 Notes or exercise of the 2005 Warrants.

As of March 31, 2009, there were 15,858,772 shares reserved for issuance for all outstanding notes, warrants and options.

## 6. Income Taxes

The Company adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes and Interpretation of FASB Statement No. 109 (“FIN 48”), as of January 1, 2007. Due to the accumulated loss position of the Company at the time of adoption, the statement had no material impact on the Company’s consolidated financial statements. The Company is subject to U.S. federal and state income taxes. Our loss carryforwards are subject to audit in any tax year in which those losses are carried and applied, notwithstanding the year of origin. The Company’s policy is to recognize

interest accrued related to unrecognized tax benefits and penalties in income tax expense. The Company has recorded no such expense.

At December 31, 2008, the Company had net operating loss (“NOL”) carryforwards for income tax purposes of approximately \$288 million, expiring in various years beginning in 2009. The deferred tax assets of approximately \$119 million at December 31, 2008, arise primarily due to NOL carryforwards for income tax purposes. The Company projects that it will be able to utilize a portion of these NOL carryforwards and deferred tax assets in 2009 and has projected a taxable expense for the year of \$2.8 million, consisting primarily of Alternative Minimum Taxes (“AMT”) to be paid. This amount is recorded on the Balance Sheet as Income tax payable. The Company has never been audited by the Internal Revenue Service.

## 7. Leases

The Company leases office space in Richmond, Virginia under an operating lease agreement expiring in October 2016. The lease provides for monthly rent of approximately \$30,800 with a 3% escalation per year. Upon the close of the Merck transaction on March 31, 2009 the Company relinquished its leases of the manufacturing facility and warehouse in Boulder, Colorado. The Company also leases a vehicle and office equipment. Future minimum payments on all these leases at March 31, 2009 are presented in the table below.

	Payments Due by Years (in thousands)					
	Total	Remainder of 2009	2010	2011	2012	2013 & Beyond
Operating lease obligations	\$ 3,401	341	428	424	431	1,777

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

### Forward Looking Statements

Statements contained herein, including without limitation, “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” contain certain projections, estimates and other forward-looking statements.

“Forward-looking statements,” as that term is defined in the Private Securities Litigation Reform Act of 1995, are not historical facts and involve a number of risks and uncertainties. Words herein such as “may,” “will,” “should,” “could,” “would,” “expects,” “plans,” “anticipates,” “believes,” “estimates,” “projects,” “predicts,” “intends,” “potential,” and similar as well as other words or expressions referencing future events, conditions or circumstances) are intended to identify forward-looking statements.

Forward-looking statements include, but are not limited to: our plans to develop and market new products and the timing of these development programs; our clinical development of product candidates, clinical trials and our ability to obtain and maintain regulatory approval for our product candidates; our estimates regarding our capital requirements and our needs for additional financing; our estimates of expenses and future revenues and profitability; our estimates of the size of the potential markets for our product candidates; our selection and licensing of product candidates; our ability to attract collaborators with acceptable development, regulatory and commercialization expertise; the benefits to be derived from corporate collaborations, license agreements and other collaborative efforts, including those relating to the development and commercialization of our product candidates; sources of revenues and anticipated revenues, including contributions from corporate collaborations, license agreements and other collaborative efforts for the development and commercialization of products; our ability to create an effective direct sales and marketing infrastructure for products we elect to market and sell directly; the rate and degree of market acceptance of our product candidates; the timing and amount of reimbursement for our product candidates; the success



of other competing therapies that may become available; and the manufacturing capacity for our product candidates.

Our actual results and the timing of certain events may differ materially from the results discussed, projected, anticipated or indicated in any forward-looking statements. Any forward-looking statement should be considered in light of factors discussed in Part II, Item 1A “Risk Factors” and elsewhere in this report. We caution readers not to place undue reliance on any such forward-looking statements, which speak only as of the date they are made. We disclaim any obligation, except as specifically required by law and the rules of the Securities and Exchange Commission, to publicly update or revise any such statements to reflect any change in our expectations or in events, conditions or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those set forth in the forward-looking statements.

The following discussion should be read in conjunction with our consolidated financial statements and related notes thereto included elsewhere in this Quarterly Report on Form 10-Q and the consolidated financial statements and related notes thereto in our Annual Report on Form 10-K, for the year ended December 31, 2008.

## Overview

We are a development stage company with expertise in recombinant protein drug development. Our corporate office is located in Richmond, Virginia.

On February 12, 2009 we announced that we had entered into a definitive agreement with Merck & Co., Inc. (“Merck”) whereby Merck, through an affiliate, would purchase all assets related to our follow-on biologics (“FOB”) platform. On March 31, 2009, we completed the sale of these assets for an aggregate purchase price of \$130 million. After fees related to the transaction, we have received to date net proceeds of \$127.8 million as a result of this transaction. Taxes due on the sale will be paid by instalment during the balance of the year resulting in total expected net proceeds of approximately \$125 million.

As part of this transaction, Merck assumed the lease of our Boulder, Colorado-based manufacturing facility and acquired ownership of all the equipment in the building. In addition, upon closing of the transaction, Merck offered positions to employees of the Boulder facility. We retain our Richmond, VA corporate office, which houses our Clinical, Regulatory, Finance, and Administrative functions, in support of the continuing IPLEX™ program. The transfer of the Boulder facility to Merck takes away our internal IPLEX™ production capability. We presently believe, however, that we have sufficient inventory of IPLEX™ to support our current ongoing Amyotrophic Lateral Sclerosis Expanded Access Program (“ALS EAP”) in Europe for approximately the next twelve months together with the IPLEX™ requirement for the clinical trial currently being planned with the FDA for ALS patients in the US. Any requirements for IPLEX™ beyond our currently projected cover period or any significant increase in demand beyond our current commitments either in the Myotonic Muscular Dystrophy (“MMD”) or ALS fields will require that we identify a Contract Manufacturing Organization (“CMO”) to produce the necessary IPLEX™ to meet the demand. We estimate that the tech transfer of our IPLEX™ production process could take 12 to 18 months once a CMO has been identified.

Until the sale of our follow-on biologics platform, we pursued a dual path strategy involving entry into the follow-on biologics arena (also known as biosimilars, biogenerics and biologics) and advancing our proprietary protein platform into niche markets with unmet needs. Following the sale of our follow-on biologics assets, we plan to continue to support our proprietary protein platform and our product, the FDA-approved IPLEX™, which is in various stages of development for a number of serious medical conditions including MMD, ALS, also known as Lou Gehrig’s disease, and Retinopathy of Prematurity (“ROP”).

We plan to use the net proceeds from the sale of our follow-on biologics platform to continue to support the development of IPLEX™ and our proprietary protein platform. We have also engaged the services of RBC to act as financial advisor in evaluating other options for use of these proceeds which could include acquisitions of complimentary businesses or technologies, product licensing or mergers, and could also include share repurchase or

the distribution of a portion of the proceeds to shareholders if we do not find attractive acquisition or licensing opportunities.

We have not been profitable and have accumulated deficits of approximately \$346 million through December 31, 2008. While we expect that, following the sale of our FOB assets to Merck, for the balance of 2009 we will operate on a cash neutral basis as a result of anticipated revenues on our Expanded Access Program and interest on the net proceeds of the sale of our FOB assets offsetting our ongoing base costs, we expect to incur significant additional losses for at least the next several years until such time as sufficient commercial revenues are generated to offset expenses. Moving forward our major source of income is expected to be the cost recovery charges for our Expanded Access Program and our major expenses will be related to research and development. In general, our expenditures may increase as development of our product candidates progresses. However, there will be fluctuations from period to period caused by differences in project costs incurred at each stage of development.

#### Research and Development Activities

Since we began operations in late 1999, we have devoted substantially all of our resources to the research and development of a number of product candidates for metabolic and endocrine diseases. Until the sale of our FOB assets on March 31, 2009, our research and development efforts were principally focused on pursuing a dual path strategy involving entry into the follow-on biologics arena (also known as biosimilars, biogenerics and biologics) and advancing our proprietary protein platform into niche markets with unmet needs. Our focus is now principally on our proprietary protein platform. Our lead proprietary protein product, the FDA-approved IPLEX™, is being studied as a treatment for several serious medical conditions including MMD and ALS. We conduct very little of our own preclinical laboratory research. We have outsourced several Phase II clinical studies with IPLEX™ and our other anti-cancer product candidates, INSM-18 and rhIGFBP-3, and plan on conducting additional clinical studies in the future.

All of our research and development expenditures, whether conducted by our own staff or by external scientists on our behalf and at our expense, are recorded as expenses as incurred and amounted to approximately \$188 million for the period since inception, in November 1999, through December 31, 2008, and \$21.1 million, \$19.2 million and \$21.0 million, for the years ended December 31, 2006, 2007 and 2008, respectively. Research and development expenses consist primarily of salaries and related expenses, costs to develop and manufacture products and amounts paid to contract research organizations, hospitals and laboratories for the provision of services and materials for drug development and clinical trials.

All of our research and development expenditures related to our proprietary protein platform are interrelated as they are all associated with drugs that modulate IGF-I activity in the human body. A significant finding in any one drug for a particular indication may provide benefits to our efforts across all of these products. All of these products also share a substantial amount of our common fixed costs such as salaries, facility costs, utilities and maintenance. Given the small portion of research and development expenses that are related to products other than IPLEX™ we have determined that very limited benefits would be obtained from implementing cost tracking systems that would be necessary to allow for cost information on a product-by-product basis.

External clinical research of IPLEX™ in the MMD indication together with the development cost of the proposed IPLEX™ trial for ALS patients in the US are expected to represent our main research and development focus for 2009.

Our clinical trials with our product candidates are subject to numerous risks and uncertainties that are outside of our control, including the possibility that necessary regulatory approvals may not be obtained. For example, the duration and the cost of clinical trials may vary significantly over the life of a project as a result of differences arising during the clinical trial protocol, including, among others, the following:

- the number of patients that ultimately participate in the trial;

- the duration of patient follow-up that is determined to be appropriate in view of results;
  - the number of clinical sites included in the trials;
- the length of time required to enroll suitable patient subjects; and
  - the efficacy and safety profile of the product candidate.

Our clinical trials may also be subject to delays or rejections based on our inability to enroll patients at the rate that we expect or our inability to produce clinical trial material in sufficient quantities and of sufficient quality to meet the schedule for our planned clinical trials.

Moreover, all of our product candidates and particularly those that are in the preclinical or early clinical trial stage must overcome significant regulatory, technological, manufacturing and marketing challenges before they can be successfully commercialized. Some of these product candidates may never reach the clinical trial stage of research and development. As preclinical studies and clinical trials progress, we may determine that collaborative relationships will be necessary to help us further develop or to commercialize our product candidates, but such relationships may be difficult or impossible to arrange. Our projects or intended projects may also be subject to change from time to time as we evaluate our research and development priorities and available resources.

Any significant delays that occur or additional expenses that we incur may have a material adverse affect on our financial position and require us to raise additional capital sooner or in larger amounts than is presently expected. In addition, as a result of the risks and uncertainties related to the development and approval of our product candidates and the additional uncertainties related to our ability to market and sell these products once approved for commercial sale, we are unable to provide a meaningful prediction regarding the period in which material net cash inflows from any of these projects is expected to become available.

## Results of Operations

Revenues for the first quarter ended March 31, 2009 were \$2.4 million, the same as the corresponding period in 2008.

The net income for the first quarter of 2009 increased to \$117.8 million or \$0.96 per share, compared with a net loss of \$4.9 million or \$0.04 per share in the first quarter of 2008. This \$122.7 million improvement was mainly due to the gain on sale of our FOB assets to Merck, which was partially offset by increases in SG&A and R&D expenses due to the recognition of stock compensation expense.

The \$2.2 million increase in total expenses was due to a \$0.5 million increase in research and development (“R&D expenses”) and a \$2.1 million increase in selling, general and administrative expenses (“SG&A Expenses”), which was partially offset by the absence of a \$0.4 million loss on investments, which was recorded in the first quarter of 2008.

The higher R&D and SG&A Expenses were due largely to the recognition of stock compensation expense for the restricted stock and restricted stock units that vested on March 31, 2009 and the award of bonuses. Interest income for the current quarter of \$23,000 was \$256,000 lower than the corresponding quarter of 2008 due to a combination of the lower interest rate environment and a lower average cash balance. Interest expense of \$242,000 was \$112,000 lower than the same quarter in 2008 due to a decrease in the debt discount amortization resulting from the lower average balance of the 2005 convertible notes, which began repayment in March 2008.

## Liquidity and Capital Resources

As of March 31, 2009, we had total cash, cash equivalents and short-term investments on hand of \$127.5 million, compared to \$2.4 million on hand as of December 31, 2008. The \$125.1 million increase in cash, cash equivalents

and short-term investments was due to the \$127.8 million in net proceeds from the sale of our FOB assets to Merck, which was minimally offset by \$2.1 million utilized to fund operations and \$0.6 million for the partial repayment of our 2005 convertible notes.

At March 31, 2009, our cash, cash equivalents and short-term investments of \$127.5 million were invested in investment grade, interest-bearing securities. Even though we currently have sufficient funds to meet our financial needs for the upcoming year, our business strategy also contemplates raising additional capital through debt or equity sales. We also plan to enter into agreements with corporate partners in order to fund operations through milestone payments, license fees and equity investments.

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

We invest excess cash in investment grade, interest-bearing securities and, at March 31, 2009, had \$127.5 million invested in money market instruments, treasury bills and municipal bonds. Such investments are subject to interest rate and credit risk. Our policy of investing in highly rated securities whose maturities at March 31, 2009 are all less than one year minimizes such risks. In addition, while a hypothetical decrease in market interest rates of 10% from March 31, 2009 levels would reduce interest income, it would not result in a loss of the principal and the decline in interest income would not be material.

### ITEM 4. CONTROLS AND PROCEDURES

**Disclosure Controls and Procedures.** We carried out an evaluation, under the supervision and with the participation of certain members of our management team, including the Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Financial Officer), of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended). Based on that evaluation, as of March 31, 2009, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are effective at the reasonable assurance level.

**Changes in Internal Controls over Financial Reporting.** During the period covered by this report, there have been no changes in our internal controls over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

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PART II  
OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are not currently a defendant in any matter of litigation; however, we could be involved in litigation in the future that could arise out of the normal course of business.

ITEM 1A. RISK FACTORS

Our operating results and financial condition have varied in the past and may in the future vary significantly depending on a number of factors. Except for the historical information in this report, the matters contained in this report include forward-looking statements that involve risks and uncertainties. The following factors, among others, could cause actual results to differ materially from those contained in forward-looking statements made in this report and presented elsewhere by management from time to time. Such factors, among others, may have a material adverse effect upon our business, results of operations and financial condition.

In Item 1A (“Risk Factors”) of our Annual Report on Form 10-K for the fiscal year ended December 31, 2008, which was filed with the Securities and Exchange Commission on March 12, 2008, we described risk factors related to our operations. Our updated risk factors are included below in this Item 1A.

You should consider carefully the following risk factors, together with all of the other information included in this quarterly report on Form 10-Q. Each of these risk factors could adversely affect our business, operating results and financial condition, as well as adversely affect the value of an investment in our common stock.

We have a history of operating losses and an expectation that we will generate operating losses for the foreseeable future, we may not achieve profitability for some time, if at all.

We are a development stage company with expertise in protein recombinant drug development. We have incurred losses each year of operation and we expect to continue incurring operating losses for the foreseeable future. The process of developing and commercializing our products requires significant pre-clinical testing and clinical trials as well as regulatory approvals for commercialization and marketing before we are allowed to begin product sales. In addition, commercialization of our drug candidates requires us to establish a sales and marketing organization and contractual relationships to enable product manufacturing and other related activities. We expect that these activities, together with our general and administrative expenses, will result in substantial operating losses for the foreseeable future. As of December 31, 2008, our accumulated deficit was \$346 million and for the year ended December 31, 2008 our consolidated net loss was \$15.7 million.

The Italian Health Authority may refuse to pay for IPLEX™ used by patients in Italy under our Expanded Access Program, which could have a material adverse effect on our business, financial condition and results of operations.

At present the Italian Health Authority approves all drug payments for IPLEX™ used by Italian patients with ALS in Italy as part of our Expanded Access Program. Should the Italian Health Authority decide to stop approving IPLEX™ for ALS it would significantly affect our cash position and could require us to raise funds sooner than anticipated, which may only be available to us on less than favorable terms.

We have not completed the research and development stage of any of our product candidates. If we are unable to successfully commercialize our products, it will materially adversely affect our business, financial condition and

results of operations.

Our long-term viability and growth depend on the successful commercialization of products which lead to revenue and profits. Pharmaceutical product development is an expensive, high risk, lengthy, complicated, resource intensive process. In order to succeed, among other things, we must be able to:

- identify potential drug product candidates;
- design and conduct appropriate laboratory, preclinical and other research;
  - submit for and receive regulatory approval to perform clinical studies;
- design and conduct appropriate preclinical and clinical studies according to good laboratory and good clinical practices;
  - select and recruit clinical investigators;
  - select and recruit subjects for our studies;
  - collect, analyze and correctly interpret the data from our studies;
  - submit for and receive regulatory approvals for marketing; and
- manufacture the drug product candidates according to current good manufacturing processes (“cGMP”).

The development program with respect to any given product will take many years and thus delay our ability to generate profits. In addition, potential products that appear promising at early stages of development may fail for a number of reasons, including the possibility that the products may require significant additional testing or turn out to be unsafe, ineffective, too difficult or expensive to develop or manufacture, too difficult to administer, or unstable.

In order to conduct the development programs for our products we must, among other things, be able to successfully:

- raise sufficient money and pay for the development of the products
  - attract and retain appropriate personnel; and
- develop relationships with other companies to perform various development activities that we are unable to perform.

Even if we are successful in developing and obtaining approval for our product candidates, there are numerous circumstances that could prevent the successful commercialization of the products such as:

- the regulatory approvals of our products are delayed or we are required to conduct further research and development of our products prior to receiving regulatory approval;
  - we are unable to build a sales and marketing group to successfully launch and sell our products;
- we are unable to raise the additional funds needed to successfully develop and commercialize our products or acquire additional products for growth;
  - we are required to allocate available funds to litigation matters;
- we are unable to manufacture the quantity of product needed in accordance with current good manufacturing practices to meet market demand, or at all;
- our product is determined to be ineffective or unsafe following approval and is removed from the market or we are required to perform additional research and development to further prove the safety and effectiveness of the product before re-entry into the market;
  - competition from other products or technologies prevents or reduces market acceptance of our products;
  - we do not have and cannot obtain the intellectual property rights needed to manufacture or market our products without infringing on another company’s patents;
- we are unsuccessful in defending against patent infringement claims being brought against us our products or technologies; or
- we are unable to obtain reimbursement for our product or such reimbursement may be less than is necessary to produce a reasonable profit.

Our growth strategy includes the commercialization of more than one product. We may not be able to identify and acquire complementary products, businesses or technologies and if acquired or licensed, they might not improve our business, financial condition or results of operations. The failure to successfully acquire, develop and commercialize products will adversely affect our business, financial condition and results of operations.

If we fail to meet the continued listing requirements of the NASDAQ Capital Market in the future, our common stock may be delisted from the NASDAQ Capital Market which may cause the value of an investment in our common stock to substantially decrease.

We may be unable to meet the continued listing requirements of the NASDAQ Capital Market in the future. To maintain the listing of our common stock on the NASDAQ Capital Market, we are required, among other things, to maintain a daily closing bid price per share of \$1.00 (the "Minimum Bid Price Requirement"). By letter dated June 18, 2007, we were notified by the NASDAQ Listing Qualification Staff (the "Staff") that the bid price for our common stock had closed below \$1.00 per share for the previous 30 consecutive business days and that in accordance with NASDAQ marketplace rules, we had been granted a 180-calendar day period, or through December 17, 2007, to regain compliance with the Minimum Bid Price Requirement. By letter dated December 20, 2007, the Staff notified us that we had failed to regain compliance with the Minimum Bid Price Requirement and that our common stock would be delisted from the NASDAQ Stock Market on December 31, 2007, if we did not transfer the listing to the NASDAQ Capital Market or appeal the Staff decision to a NASDAQ Hearings Panel (a "Panel"). By letter dated, December 26, 2007, we requested a hearing before a Panel and on January 24, 2008, we attended a Panel hearing in connection with our failure to meet the Minimum Bid Price Requirement. By decision dated February 27, 2008, the Panel transferred our common stock to the NASDAQ Capital Market and granted us the balance of the second 180-calendar day period, or until June 12, 2008, in accordance with NASDAQ marketplace rules, to regain compliance with the Minimum Bid Price Requirement. We did not regain compliance with the Minimum Bid Price Requirement and accordingly, on June 17, 2008, were notified by the Staff that our common stock would be delisted from the NASDAQ Capital Market if we did not request a hearing before a Panel. By letter dated June 24, 2008, we requested a hearing before a Panel with respect to the continued listing of our common stock on the NASDAQ Capital Market. On July 31, 2008, we had a hearing in front of the Panel. On August 29, 2008, we received a letter from the Panel stating that the Panel had granted our request to remain listed on the NASDAQ Capital Market, provided that, we evidence compliance with the Minimum Bid Price Rule on or before December 15, 2008. Subsequent to the Panel decision, due to market conditions, on October 16, 2008, NASDAQ announced that it was suspending compliance with the Minimum Bid Price Requirement for all listed companies until January 16, 2009. In connection with the suspension of the Minimum Bid Price Requirement, we were notified that the period by which we must be in compliance with the Minimum Bid Price Requirement had been extended until July 17, 2009. As of April 29, 2009, our common stock met the Minimum Bid Price Requirement for ten consecutive trading days and by letter dated May 1, 2009, NASDAQ notified us that we were in compliance with this requirement and that the Panel had determined to continue the listing of our common stock. If we fail to meet the Minimum Bid Price Requirement in the future, our common stock may be delisted from the NASDAQ Capital Market. If a delisting from the NASDAQ Capital Market were to occur, our Common Stock would be eligible, upon the application of a market maker, to trade on the OTC Bulletin Board or in the "pink sheets." These alternative markets are generally considered to be less efficient than, and not as broad as, the NASDAQ Capital Market or the NASDAQ Global Market. Therefore, delisting of our common stock from the NASDAQ Capital Market could adversely affect the trading price of our common stock and could limit the liquidity of our common stock and therefore could cause the value of an investment in our common stock to decrease. In addition, if we fail to meet the Minimum Bid Price Requirement in the future we may be required to implement a reverse stock split in order for our shares of common stock to remain listed on the NASDAQ Capital Market, which could have a material adverse affect on our stock price.

If our products fail in pre-clinical or clinical trials or if we cannot enroll enough patients to complete our clinical trials, such failure may adversely affect our business, financial condition and results of operations.

In order to sell our products, we must receive regulatory approval. Before obtaining regulatory approvals for the commercial sale of any of our products under development, we must demonstrate through pre-clinical studies and clinical trials that the product is safe and effective for use in each target indication. In addition, the results from pre-clinical testing and early clinical trials may not be predictive of results obtained in later clinical trials. There can be no assurance that our clinical trials will demonstrate sufficient safety and effectiveness to obtain regulatory approvals for our products still in development. A number of companies in the biotechnology and pharmaceutical industries have suffered significant setbacks in late stage clinical trials even after promising results in early stage development. If our developmental products fail in pre-clinical or clinical trials, it will have an adverse effect on our business, financial condition and results of operations.

The completion rate of clinical studies of our products is dependent on, among other factors, the patient enrollment rate. Patient enrollment is a function of many factors, including:

- investigator identification and recruitment;
- regulatory approvals to initiate study sites;
  - patient population size;
- the nature of the protocol to be used in the trial;
  - patient proximity to clinical sites;
  - eligibility criteria for the study; and
- competition from other companies' clinical studies for the same patient population.

We believe our planned procedures for enrolling patients are appropriate; however, delays in patient enrollment would increase costs and delay ultimate commercialization and sales, if any, of our products. Such delays could materially adversely affect our business, financial condition and results of operations.

We may be required to conduct broad, long-term clinical trials to address concerns that the long-term use of one of our leading products, IPLEX™, in broader chronic indications might increase the risk of diabetic retinopathy. This may materially adversely affect our business, financial condition and results of operations.

In previously published clinical trials of rhIGF-1, concerns were raised that long-term use of rhIGF-1 might lead to an increased incidence and/or severity of retinopathy, a disease of new blood vessel growth in the eye which results in loss of vision. Because IPLEX™ contains rhIGF-I, the FDA may require us to conduct broad, long-term clinical trials to address these concerns prior to receiving FDA approval for broad chronic indications such as diabetes. These clinical trials would be expensive and could delay our commercialization of IPLEX™ for these broader chronic indications. Adverse results in these trials could prevent our commercialization of IPLEX™ for broad chronic indications or could jeopardize existing development in other indications.

We cannot be certain that we will obtain regulatory approvals in the United States, European Union or other countries. The failure to obtain such approvals may materially adversely affect our business, financial condition and results of operations.

We are required to obtain various regulatory approvals prior to studying our products in humans and then again before we market and distribute our products. The regulatory review and approval process required to perform a clinical study in both the United States and European Union includes evaluation of preclinical studies and clinical studies, as well as the evaluation of our manufacturing process. This process is complex, lengthy, expensive, resource intensive and uncertain. Securing regulatory approval to market our products also requires the submission of extensive preclinical and clinical data, manufacturing information regarding the process and facility, scientific data characterizing our product and other supporting data to the regulatory authorities in order to establish its safety and effectiveness. This process is also complex, lengthy, expensive, resource intensive and uncertain. We have limited experience in filing and pursuing applications necessary to gain these regulatory approvals.



Data submitted to the regulators is subject to varying interpretations that could delay, limit or prevent regulatory agency approval. We may also encounter delays or rejections based on changes in regulatory agency policies during the period in which we develop a product and the period required for review of any application for regulatory agency approval of a particular product. Delays in obtaining regulatory agency approvals could adversely affect the development and marketing of any drugs that we or our collaborative partners develop. Such delays could impose costly procedures on our collaborative partners' or our activities, diminish any competitive advantages that our collaborative partners or we may attain and adversely affect our ability to receive royalties, any of which could materially adversely affect our business, financial condition and results of operations.

In order to market our products outside of the United States and European Union, our corporate partners and we must comply with numerous and varying regulatory requirements of other countries. The approval procedures vary among countries and can involve additional product testing and administrative review periods. The time required to obtain approval in these other territories might differ from that required to obtain FDA or European Agency for the Evaluation of Medicinal Products, or EMEA, approval. The regulatory approval process in these other territories includes at least all of the risks associated with obtaining FDA and EMEA approval detailed above. Approval by the FDA or the EMEA does not ensure approval by the regulatory authorities of other countries. The failure to obtain such approvals may materially adversely affect our business, financial condition and results of operations.

We may not have or be able to obtain sufficient quantities of our products to meet our supply and clinical studies obligations and our business, financial condition and results of operation may be adversely affected.

The transfer of the Boulder facility to Merck takes away our internal IPLEX™ production capability. We presently believe, however, that we have sufficient inventory of IPLEX™ to support our current ongoing ALS EAP in Europe for approximately the next twelve months together with the IPLEX™ requirement for the clinical trial currently being planned with the FDA for ALS patients in the US. Any requirements for IPLEX™ beyond our currently projected cover period or any significant increase in demand beyond our current commitments either in the MMD or ALS fields will require that we identify a Contract Manufacturing Organization or CMO to produce the necessary IPLEX™ to meet the demand. We estimate that the tech transfer of our IPLEX™ production process could take 12 to 18 months once a CMO has been identified.

We also intend to manufacture rhIGFBP-3 clinical drug substance and INSM-18 with contract manufacturers. In addition, we intend to utilize contract manufacturers for sterile filtering, filling, finishing, labeling and analytical testing.

The number of contract manufacturers with the expertise and facilities to manufacture our products is limited and it would take a significant amount of time and resources to arrange for alternative manufacturers. Even if we were to find alternative manufacturers, the prices they charge may not be commercially reasonable or may only be able to provide our products in a quantity that is less than our needs. Furthermore, if we need to change to other contract manufacturers, we would also need to transfer to these new manufacturers and validate the processes and analytical methods necessary for the production and testing of our products. Any of these factors could lead to (1) the delay or suspension of our clinical studies, regulatory submissions and regulatory approvals, or (2) higher costs of production, or (3) our failure to effectively commercialize our products.

The facilities of contract manufacturers must undergo inspections by the FDA and the EMEA for compliance with cGMP regulations. In the event these facilities do not continue to receive satisfactory cGMP inspections for the manufacture and testing of our products, we may need to fund additional modifications to our manufacturing or testing processes, conduct additional validation studies, or find alternative manufacturing and testing facilities, any of which would result in significant cost to us as well as a significant delay of up to several years in the development of our products. In addition, the facilities of any contract manufacturer we may utilize will be subject to ongoing periodic inspection by the FDA, the EMEA and other foreign agencies for compliance with cGMP regulations and

similar foreign standards. We have limited control over contract manufacturers' compliance with these regulations and standards which could limit our production of final drug product.

If our products fail to achieve market acceptance for any reason, such failure may materially adversely affect our business, financial condition and results of operations.

There can be no assurance that any of our product candidates if approved for marketing, will achieve market acceptance. If our product candidates, once approved, do not receive market acceptance for any reason, it will adversely affect our business, financial condition and results of operations. The degree of market acceptance of any drugs we develop will depend on a number of factors, including:

- the establishment and demonstration in the medical community of the clinical efficacy and safety of our products;
  - our products' potential advantages over existing and future treatment methods;
  - the price of our products; and
- reimbursement policies of government and third-party payers, including hospitals and insurance companies.

For example, even after we obtain regulatory approval to sell our products, physicians and healthcare payers could conclude that our products are not safe and effective and physicians could choose not to use them to treat patients. Our competitors may also develop new technologies or products which are more effective or less costly, or that seem more cost-effective than our products.

In addition, legislation and regulations affecting the pricing of pharmaceuticals may change in ways adverse to us. While we cannot predict the likelihood of any legislative or regulatory proposals, if the government or an agency adopts such proposals, they could materially adversely affect our business, financial condition and results of operations.

We are dependent upon retaining and attracting key personnel and others, the loss of which could materially adversely affect our business, financial condition and results of operations.

We depend highly on the principal members of our scientific and management staff, the loss of whose services might significantly delay or prevent the achievement of research, development or business objectives and would materially adversely affect our business, financial condition and results of operations. Our success depends, in large part, on our ability to attract and retain qualified management, scientific and medical personnel, and on our ability to develop and maintain important relationships with commercial partners, leading research institutions and key distributors. We face intense competition for such personnel and relationships. We cannot assure that we will attract and retain such persons or maintain such relationships.

We expect that our potential expansion into areas and activities requiring additional expertise, such as further clinical trials, governmental approvals, manufacturing, sales, marketing and distribution will place additional requirements on our management, operational and financial resources. We expect these demands will require an increase in management and scientific personnel and the development of additional expertise by existing management personnel. The failure to attract and retain such personnel or to develop such expertise could materially adversely affect our business, financial condition and results of operations.

We rely on collaborative relationships for our success. If we are unable to form these relationships it could materially adversely impact our business, financial condition and results of operations.

We currently rely and may in the future rely on a number of significant collaborative relationships for intellectual property rights, research funding, manufacturing, analytical services, preclinical development, clinical development and sales and marketing. For example, almost all of our clinical trial work is done in collaboration with academic institutions and we have licensed intellectual property to permit the development, manufacture and commercialization

of our products. Reliance on collaborative relationships poses a number of risks, including the following:

- we may not be able to effectively control whether our corporate partners will devote sufficient resources to our programs or products;
- disputes may arise in the future with respect to the ownership of rights to technology developed with, licensed to or licensed from corporate partners;
- disagreements with corporate partners could result in loss of intellectual property rights, delay or terminate the research, development or commercialization of product candidates or result in litigation or arbitration;
  - contracts with our corporate partners may fail to provide sufficient protection of our intellectual property;
    - we may have difficulty enforcing the contracts if one of these partners fails to perform;
- corporate partners have considerable discretion in electing whether to pursue the development of any additional products and may pursue technologies or products either on their own or in collaboration with our competitors; and
  - corporate partners with marketing rights may choose to devote fewer resources to the marketing of our products than they do to products of their own development.

Given these risks, a great deal of uncertainty exists regarding the success of our current and future collaborative efforts. Failure of these efforts could delay, impair or prevent the development and commercialization of our products and adversely affect our business, financial condition and results of operations.

Our growth strategy includes acquiring complementary businesses or technologies that may not be available or, if available and purchased or licensed, might not improve our business, financial condition or results of operations.

As part of our business strategy, we expect to pursue acquisitions and in-license new products and technologies. Nonetheless, we cannot assure you that we will identify suitable acquisitions or products or that we can make such acquisitions or enter into such license agreements on acceptable terms. If we acquire businesses, those businesses may require substantial capital, and we cannot provide assurance that such capital will be available in sufficient amounts or that financing will be available in amounts and on terms that we deem acceptable. Furthermore, the integration of acquired businesses may result in unforeseen difficulties that require a disproportionate amount of management's attention and our other resources. Finally, we cannot provide assurance that we will achieve productive synergies and efficiencies from these acquisitions.

We intend to conduct proprietary development programs with collaborators, and any conflicts with them could harm our business, financial condition and results of operations. We intend to enter into collaborative relationships which will involve our collaborators conducting proprietary development programs. Any conflict with our collaborators could reduce our ability to obtain future collaboration agreements and negatively influence our relationship with existing collaborators, which could reduce our revenues and have an adverse effect on our business, financial condition and results of operations. Moreover, disagreements with our collaborators could develop over rights to our intellectual property.

Certain of our collaborators could also be or become competitors. Our collaborators could harm our product development efforts by:

- developing competing products;
- precluding us from entering into collaborations with their competitors;
  - failing to obtain regulatory approvals;
  - terminating their agreements with us prematurely; or
- failing to devote sufficient resources to the development and commercialization of products.

We may need additional funds in the future to continue our operations, but we face uncertainties with respect to our access to capital that could materially adversely impact our business, financial condition and results of operations.

We may require additional future capital in order to acquire complementary businesses or technology or continue our research and development activities. On March 31, 2009, we completed the sale of our FOB assets for an aggregate purchase price of \$130 million. After fees, taxes and other costs related to the transaction, we expect net proceeds of approximately \$125 million as a result of this transaction. However, our future capital requirements will depend on many factors, including factors associated with:

- research and development, including, among other items, preclinical testing and clinical studies,
  - process development;
  - obtaining marketing, sales and distribution capabilities;
    - obtaining regulatory approvals;
    - retaining employees and consultants;
- filing and prosecuting patent applications and enforcing patent claims;
  - establishing strategic alliances;
    - manufacturing; and
  - potential future litigation.

We may also need to spend more money than currently expected because we may further change or alter drug development plans, acquire additional drugs or drug candidates or we may misjudge our costs. We have no committed sources of capital and do not know whether additional financing will be available when needed, or, if available, that the terms will be favorable. There can be no assurance that our cash reserves together with any subsequent funding will satisfy our capital requirements. The failure to satisfy our capital requirements will adversely affect our business, financial condition and results of operations.

We may seek additional funding through strategic alliances, private or public sales of our securities or licensing all or a portion of our technology. Such funding may significantly dilute existing shareholders or may limit our rights to our currently developing technology. There can be no assurance, however, that we can obtain additional funding on reasonable terms, or at all. If we cannot obtain adequate funds, we may need to significantly curtail our product development programs and relinquish rights to our technologies or drug candidates. This may adversely affect our business, financial condition and results of operations.

We may not accurately predict the protection afforded by our patents and proprietary technology and if our predictions are wrong, this may materially adversely affect our business, financial condition and results of operations.

Our success will depend in part on our ability to obtain patent protection for our products, prevent third parties from infringing on our patents, and refrain from infringing on the patents of others, both domestically and internationally.

Our patent positions are highly uncertain, and any future patents we receive for our potential products will be subject to this uncertainty, which may adversely affect our business, financial condition and results of operations. We intend to actively pursue patent protection for products resulting from our research and development activities that have significant potential commercial value. Nevertheless, it is possible that, in the patent application process, certain claims may be rejected or may achieve such limited allowance that the value of the patents would be diminished. Further, there can be no assurance that any patents obtained will afford us adequate protection. In addition, any patents we procure may require cooperation with companies holding related patents. We may have difficulty forming a successful relationship with these other companies.

Third parties may claim that we are infringing upon or have misappropriated their proprietary rights. Various third parties have obtained, and are attempting to obtain, patent protection relating to the production and use of our approved product and product candidates. We can give no assurances as to whether any issued patents, or patents that may later issue to third parties, would affect our contemplated commercialization of IPLEX™ or any other product. We can give no assurances that such patents can be avoided, invalidated or licensed. With respect to any infringement claim asserted by a third party, we can give no assurances that we will be successful in the litigation or that such litigation would not have a material adverse effect on our business, financial condition and results of operation. In the

event of a successful claim against us for infringement or misappropriation of a third party's proprietary rights, we may be required to:

- pay damages, including up to treble damages, and the other party's attorneys' fees, which may be substantial;
- cease the development, manufacture, marketing and sale of products or use of processes that infringe the proprietary rights of others;
- expend significant resources to redesign our products or our processes so that they do not infringe the proprietary rights of others, which may not be possible;
- redesign our products or processes to avoid third party proprietary rights, we may suffer significant regulatory delays associated with conducting additional clinical trials or other steps to obtain regulatory approval; and
- obtain one or more licenses arising out of a settlement of litigation or otherwise from third parties for the infringed proprietary rights, which may not be available to us on acceptable terms or at all.

Furthermore, litigation with any third party, even if the allegations are without merit, would likely be expensive and time-consuming and divert management's attention.

Any conclusions we may have reached regarding non-infringement and invalidity are based in part on a review of publicly available databases and other information. There may be information not available to us or otherwise not reviewed by us that might change our conclusions. Moreover, as described above, the scope and validity of patent claims are determined based on many facts and circumstances, and in a litigation, a court may reach a different conclusion on any given patent claim than the conclusions that we have reached.

In addition, we may have to undertake costly litigation to enforce any patents issued or licensed to us or to determine the scope and validity of another party's proprietary rights. We can give no assurances that a court of competent jurisdiction would validate our issued or licensed patents. An adverse outcome in litigation or an interference or other proceeding in a court or patent office could materially adversely affect our business, financial condition and results of operations.

We operate in a highly competitive environment and if we are unable to adapt to our environment, we may be unable to compete successfully, which will materially adversely affect our business, financial condition and results of operations.

Biotechnology and related pharmaceutical technology have undergone and should continue to experience rapid and significant change. We expect that the technologies associated with biotechnology research and development will continue to develop rapidly. Our future success will depend in large part on our ability to maintain a competitive position with respect to these technologies. Any compounds, products or processes that we develop may become obsolete before we recover any expenses incurred in connection with their development. Rapid technological change could make our products obsolete, which could materially adversely affect our business, financial condition and results of operations.

We expect that successful competition will depend, among other things, on product efficacy, safety, reliability, availability, timing and scope of regulatory approval and price. Specifically, we expect crucial factors will include the relative speed with which we can develop products, complete the clinical testing and regulatory approval processes and supply commercial quantities of the product to the market. We expect competition to increase as technological advances are made and commercial applications broaden. In each of our potential product areas, we face substantial competition from large pharmaceutical, biotechnology and other companies, universities and research institutions. Relative to us, most of these entities have substantially greater capital resources, research and development staffs, facilities and experience in conducting clinical studies and obtaining regulatory approvals, as well as in manufacturing and marketing pharmaceutical products. Many of our competitors may achieve product commercialization or patent protection earlier than us. Furthermore, we believe that our competitors have used, and may continue to use, litigation to gain a competitive advantage. Finally, our competitors may use different technologies or approaches to the development of products similar to the products we are seeking to develop.

Competitors could develop and gain FDA approval of products containing rhIGF-1, which could adversely affect our competitive position in all indications where we are currently developing IPLEX™.

rhIGF-1 manufactured by other parties may be approved for use in other indications in the United States in the future, including MMD and ALS. In the event there are other rhIGF-1 products approved by the FDA to treat indications other than those covered by IPLEX™, physicians may elect to prescribe a competitor's product containing rhIGF-1 to treat the indications for which IPLEX™ has received and may receive approval. This is commonly referred to as off-label use. While under FDA regulations a competitor is not allowed to promote off-label use of its product, the FDA does not regulate the practice of medicine and as a result cannot direct physicians as to what product containing rhIGF-1 to prescribe to their patients. As a result, we would have limited ability to prevent off-label use of a competitor's product containing rhIGF-1 to treat any diseases for which we have received FDA approval, even if it violates our patents and we have orphan drug exclusivity for the use of rhIGF-1 to treat such diseases.

If another party obtains orphan drug exclusivity for a product that is essentially the same as a product we are developing in a particular indication, we may be precluded or delayed from commercializing the product in that indication. This may materially adversely affect our business, financial condition and results of operations.

Under the Orphan Drug Act, the FDA may grant orphan drug designation to drugs intended to treat a rare disease or condition, which is generally a disease or condition that affects fewer than 200,000 individuals in the United States. The company that obtains the first marketing approval from the FDA for a designated orphan drug for a rare disease receives marketing exclusivity for use of that drug for the designated condition for a period of seven years. Similar laws exist in EU. If a competitor obtains approval of the same drug for the same indication or disease before us, we would be blocked from obtaining approval for our product for seven or more years, unless our product can be shown to be clinically superior. In addition, more than one drug may be approved by the FDA for the same orphan indication or disease as long as the drugs are different drugs. As a result, even if our product is approved and receives orphan drug exclusivity, as in the case of our drug IPLEX™, the FDA can still approve different drugs for use in treating the same indication or disease covered by our product, which could create a more competitive market for us.

Confidentiality agreements with employees and others may not adequately prevent disclosure of trade secrets and other proprietary information. Disclosure of this information may materially adversely affect our business, financial condition and results of operations.

In order to protect our proprietary technology and processes, we rely in part on confidentiality agreements with our corporate partners, employees, consultants, outside scientific collaborators and sponsored researchers and other advisors. These agreements may not effectively prevent disclosure of confidential information and may not provide an adequate remedy in the event of unauthorized disclosure of confidential information. In addition, others may independently discover trade secrets and proprietary information. Costly and time-consuming litigation could be necessary to enforce and determine the scope of our proprietary rights, and failure to obtain or maintain trade secret protection could adversely affect our competitive business, financial condition and results of operations.

Our research, development and manufacturing activities at our former Boulder Facility involved the use of hazardous materials, which could expose us to damages that could materially adversely affect our results of operations and financial condition.

Our research, development and manufacturing activities at our former Boulder Facility involved the controlled use of hazardous materials, including hazardous chemicals and radioactive materials. Under the terms and conditions of our agreement with Merck for the sale of our FOB assets, we retained our obligations and liabilities under any environmental law relating to activities conducted before March 31, 2009 but which arise at any time during the two-year period beginning on March 31, 2009. If any such obligation or liability arises, we could be subject to an

obligation to indemnify Merck for any losses incurred by Merck which could materially adversely affect our results of operations and financial condition.

We may be subject to product liability claims if our products harm people, and we have only limited product liability insurance.

The manufacture and sale of human therapeutic products involve an inherent risk of product liability claims and associated adverse publicity. We currently have only limited product liability insurance for our products. We do not know if we will be able to maintain existing or obtain additional product liability insurance on acceptable terms or with adequate coverage against potential liabilities. This type of insurance is expensive and may not be available on acceptable terms. If we are unable to obtain or maintain sufficient insurance coverage on reasonable terms or to otherwise protect against potential product liability claims, we may be unable to commercialize our products. A successful product liability claim brought against us in excess of our insurance coverage, if any, may require us to pay substantial amounts. This could have a material adverse effect our business, financial condition and results of operations.

If our settlement agreement with Tercica and Genentech was terminated, the Consent order from the court would be reinstated, which would have a material adverse effect on our business, financial condition and results of operations.

As part of our settlement agreement with Genentech and Tercica, we entered into a Consent Judgment and Permanent Injunction in the United States District Court for the Northern District of California. If our settlement agreement with Tercica and Genentech is terminated, the Consent Judgment and Permanent Injunction against us will survive termination, which would have a material adverse effect on our business, financial condition and results of operations as we would no longer have a license to manufacture IPLEX™ using the present process without incurring significant penalties and royalties.

Conversion of our outstanding notes and exercise of warrants and options issued by us will significantly dilute the ownership interest of existing shareholders.

As of March 31, 2009, the convertible notes issued by us in March 2005 and the warrants issued by us in May 2007, March 2005, November 2004 and July 2003 were convertible into and exercisable for up to approximately 12.7 million shares of our common stock, representing approximately 10% of our then outstanding common stock.

As of March 31, 2009, our outstanding options and stock grants to our employees, officers, directors and consultants were exercisable for up to 3.2 million shares of our common stock, representing approximately an additional three percent of our then outstanding common stock.

The conversion or exercise of some or all of our convertible notes, warrants and options will significantly dilute the ownership interests of existing shareholders. Any sales in the public market of the common stock issuable upon such conversion or exercise could adversely affect prevailing market prices of our common stock.

The market price of our stock has been and may continue to be highly volatile and historically, we have never paid dividends on our common stock.

Our common stock is listed on the Nasdaq Capital Market under the ticker symbol "INSM." The market price of our stock has been and may continue to be highly volatile, and announcements by us or by third parties may have a significant impact on our stock price. These announcements may include:

- our listing status on the Nasdaq Capital Market;
- results of our clinical studies and preclinical studies, or those of our corporate partners or our competitors;
  - our operating results;

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- developments in our relationships with corporate partners;
  - developments affecting our corporate partners;
  - developments affecting our corporate partners;
- negative regulatory action or regulatory approval with respect to our announcement or our competitors' announcements of new products,
- government regulation, reimbursement changes and governmental investigation or audits related to us or to our products,
  - developments related to our patents or other proprietary rights or those of our competitors;
    - changes in the position of securities analysts with respect to our stock; and
  - operating results below the expectations of public market analysts and investors.

In addition, the stock market has from time to time experienced extreme price and volume fluctuations, which have particularly affected the market prices for emerging biotechnology and biopharmaceutical companies, and which have often been unrelated to their operating performance. These broad market fluctuations may adversely affect the market price of our common stock.

In the past, when the market price of a stock has been volatile, holders of that stock have often instituted securities class action litigation against the company that issued the stock. If any of our shareholders brought a lawsuit against us, we could incur substantial costs defending the lawsuit. The lawsuit could also divert the time and attention of our management.

Future sales by existing shareholders may lower the price of our common stock, which could result in losses to our shareholders. Future sales of substantial amounts of common stock in the public market, or the possibility of such sales occurring, could adversely affect prevailing market prices for our common stock or our future ability to raise capital through an offering of equity securities. Substantially all of our common stock is freely tradable in the public market without restriction under the Securities Act, unless these shares are held by "affiliates" of our company, as that term is defined in Rule 144 under the Securities Act.

Historically we have never paid dividends on our common stock and we currently intend to retain our future earnings, if any, to fund the development and growth of our businesses and, therefore, we do not anticipate paying any cash dividends from earnings in the foreseeable future. We are currently reviewing options for the use of the proceeds from the sale of our FOB assets to Merck. One of these options may include a special dividend to common shareholders.

Certain provisions of Virginia law, our articles of incorporation and our amended and restated bylaws, and our Rights Plan make a hostile takeover by a third party difficult.

Certain provisions of Virginia law and our articles of incorporation and amended and restated bylaws could hamper a third party's acquisition of, or discourage a third party from attempting to acquire control of us. The conditions could also limit the price that certain investors might be willing to pay in the future for shares of our common stock. These provisions include:

- a provision allowing us to issue preferred stock with rights senior to those of the common stock without any further vote or action by the holders of the common stock. The issuance of preferred stock could decrease the amount of earnings and assets available for distribution to the holders of common stock or could adversely affect the rights and powers, including voting rights, of the holders of the common stock. In certain circumstances, such issuance could have the effect of decreasing the market price of the common stock;
- the existence of a staggered board of directors in which there are three classes of directors serving staggered three-year terms, thus expanding the time required to change the composition of a majority of directors and perhaps discouraging someone from making an acquisition proposal for us;
-



the amended and restated bylaws' requirement that shareholders provide advance notice when nominating our directors;

- the inability of shareholders to convene a shareholders' meeting without the chairman of the board, the president or a majority of the board of directors first calling the meeting; and
- the application of Virginia law prohibiting us from entering into a business combination with the beneficial owner of 10% or more of our outstanding voting stock for a period of three years after the 10% or greater owner first reached that level of stock ownership, unless we meet certain criteria.

In addition, in May 2001, our board of directors approved the adoption of a Rights Plan under which shareholders received rights to purchase new shares of preferred stock if a person or group acquires 15% or more of our common stock. These provisions are intended to discourage acquisitions of 15% or more of our common stock without negotiations with the board. The rights trade with our common stock, unless and until they are separated upon the occurrence of certain future events. Our board of directors may redeem the rights at a price of \$0.01 per right prior to the time a person acquires 15% or more of our common stock.

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

None.

## ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## ITEM 5. OTHER INFORMATION

We have not made any material changes to the procedures by which our stockholders may recommend director nominees to our Nominating Committee of the Board or our Board.

## ITEM 6. EXHIBITS

10.1 Asset Purchase Agreement, dated February 12, 2009, between Protein Transaction LLC (a wholly owned subsidiary of Merck & Co. Inc.) Insmmed Incorporated and Merck & Co., Inc. (previously filed as Exhibit 10.1 to Insmmed Incorporated's Current Report on Form 8-K on February 13, 2009 and incorporated herein by reference).

31.1 Rule 13a-14(a)/15d-14(a) Certification of Geoffrey Allan, Ph.D., Chairman of the Board and Chief Executive Officer of Insmmed Incorporated.

31.2 Rule 13a-14(a)/15d-14(a) Certification of Kevin P. Tully, C.G.A., Executive Vice President and Chief Financial Officer of Insmmed Incorporated.

32.1 Certification of Geoffrey Allan, Ph.D., Chairman of the Board and Chief Executive Officer of Insmmed Incorporated, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*

32.2 Certification of Kevin P. Tully, C.G.A., Executive Vice President and Chief Financial Officer of Insmmed Incorporated, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.\*

\* This certification accompanies this Quarterly Report on Form 10-Q pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not be deemed filed by the Company for purposes of the Securities Exchange Act of 1934.

SIGNATURE

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.

INSMED INCORPORATED  
(Registrant)

Date: May 13, 2009

By: /s/ Kevin P. Tully  
Kevin P. Tully, C.G.A.,  
EVP & Chief Financial Officer