

FACET BIOTECH CORP  
Form 10-Q  
May 08, 2009  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM 10-Q**

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(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**

**Commission File Number: 0-19756**

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## Facet Biotech Corporation

(Exact name of registrant as specified in its charter)

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

**26-3070657**  
(I.R.S. Employer  
Identification Number)

**1500 Seaport Boulevard**

**Redwood City, CA 94063**

(Address of principal executive offices and Zip Code)

**(650) 454-1000**

(Registrant's telephone number, including area code)

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

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

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

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Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

As of April 30, 2009, there were 24,548,841 shares of the Registrant's Common Stock outstanding.

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We own or have rights to numerous trademarks, trade names, copyrights and other intellectual property used in our business, including Facet Biotech and the Facet Biotech logo, each of which is considered a trademark, and *Nuvion*®. All other company names, tradenames and trademarks included in this Quarterly Report are trademarks, registered trademarks or trade names of their respective owners.

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

**FACET BIOTECH CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(unaudited)

(in thousands, except per share data)

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2009</b>	<b>2008</b>
<b>Revenues:</b>		
Collaboration	\$ 7,237	\$ 2,682
Other	2,362	2,000
Total revenues	9,599	4,682
<b>Costs and expenses:</b>		
Research and development	24,065	45,237
General and administrative	10,259	12,765
Restructuring charges	4,205	5,547
Asset impairment charges		3,521
Gain on sale of assets		(49,671)
Total costs and expenses	38,529	17,399
Loss from operations	(28,930)	(12,717)
Interest and other income	180	3
Interest expense	(422)	(434)
Loss before income taxes	(29,172)	(13,148)
Income tax expense		28
Net loss	\$ (29,172)	\$ (13,176)
<b>Net loss per basic and diluted share</b>	<b>\$ (1.22)</b>	<b>\$ (0.55)</b>
<b>Shares used to compute net loss per basic and diluted share</b>	<b>23,905</b>	<b>23,901</b>

See accompanying notes.



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## FACET BIOTECH CORPORATION

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share data)

	March 31, 2009 (unaudited)	December 31, 2008 (Note 1)
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 287,998	\$ 397,611
Marketable securities	55,986	
Prepaid and other current assets	20,029	19,382
Total current assets	364,013	416,993
Long-term marketable securities	33,624	
Long-term restricted cash	5,807	5,807
Property and equipment, net	102,205	105,671
Intangible assets, net	6,998	7,409
Other assets	1,948	2,141
Total assets	\$ 514,595	\$ 538,021
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Accounts payable	\$ 853	\$ 337
Accrued compensation	6,371	3,669
Other accrued liabilities	8,224	3,635
Deferred revenue	13,009	13,234
Current portion of lease financing liability	907	862
Total current liabilities	29,364	21,737
Long-term deferred revenue	41,856	44,901
Long-term lease financing liability	25,061	25,316
Other long-term liabilities	10,992	10,434
Total liabilities	107,273	102,388
Stockholders' equity:		
Preferred stock, par value \$0.01 per share, 10,000 shares authorized; no shares were outstanding at March 31, 2009 and December 31, 2008, respectively		
Common stock, par value \$0.01 per share, 140,000 shares authorized; 23,905 and 23,901 shares issued and outstanding at March 31, 2009 and December 31, 2008, respectively		
Additional paid-in capital	239	239
Accumulated deficit	456,190	455,380
Accumulated other comprehensive loss	(48,669)	(19,497)
Accumulated other comprehensive loss	(438)	(489)
Total stockholders' equity	407,322	435,633
Total liabilities and stockholders' equity	\$ 514,595	\$ 538,021

See accompanying notes.

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## FACET BIOTECH CORPORATION

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(in thousands)

	Three Months Ended March 31,	
	2009	2008
<b>Cash flows from operating activities:</b>		
Net loss	\$ (29,172)	\$ (13,176)
Adjustments to reconcile net loss to net cash used in operating activities:		
Asset impairment charges		3,521
Depreciation	3,517	7,176
Amortization of intangible assets	411	412
Stock-based compensation expense	876	
Allocation of stock-based compensation expense from parent		3,460
Expense allocation from parent		610
Gain on sale of assets		(49,671)
Loss on disposal of equipment	18	127
Changes in assets and liabilities:		
Other current assets	(896)	(2,671)
Other assets	193	574
Accounts payable	516	(338)
Accrued liabilities	7,260	(7,244)
Other long-term liabilities	578	742
Deferred revenue	(3,270)	(643)
Total adjustments	9,203	(43,945)
Net cash used in operating activities	(19,969)	(57,121)
<b>Cash flows from investing activities:</b>		
Purchases of marketable securities	(89,329)	
Proceeds from the sale of property and equipment		236,560
Purchase of property and equipment	(106)	(612)
Transfer from restricted cash		10,000
Net cash provided by (used in) investing activities	(89,435)	245,948
<b>Cash flows from financing activities:</b>		
Issuance of common stock	1	
Payments on long-term lease financing liability	(210)	(169)
Transfers to parent		(188,658)
Net cash used in financing activities	(209)	(188,827)
Net decrease in cash and cash equivalents	(109,613)	
Cash and cash equivalents at beginning of the period	397,611	
Cash and cash equivalents at end the period	\$ 287,998	\$

See accompanying notes.



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**FACET BIOTECH CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**March 31, 2009**

**(unaudited)**

**1. Basis of Presentation and Summary of Significant Accounting Policies**

Basis of Presentation

Facet Biotech Corporation (we, us, our, Facet Biotech, the Company) was organized as a Delaware corporation in July 2008 by PDL Biopharma, Inc. (PDL) as a wholly-owned subsidiary of PDL. PDL organized the Company in preparation for the Spin-off of the Company, which was effected on December 18, 2008 (the Spin-off). In connection with the Spin-off, PDL contributed to us PDL's Biotechnology Business and PDL distributed to its stockholders all of the outstanding shares of our common stock. Following the Spin-off, we became an independent, publicly traded company owning and operating what previously had been PDL's Biotechnology Business.

Prior to the Spin-off, PDL's Biotechnology Business, now operated by the Company, was not operated by a legal entity separate from PDL and a direct ownership relationship did not exist among all the components comprising the Biotechnology Business. We describe the Biotechnology Business transferred to us by PDL in connection with the Spin-off as though the Biotechnology Business were our business for all historical periods described. However, Facet Biotech had not operated the Biotechnology Business prior to the Spin-off. References in these Condensed Consolidated Financial Statements to the historical assets, liabilities, products, business or activities of our business are intended to refer to the historical assets, liabilities, products, business or activities of the Biotechnology Business as those were conducted as part of PDL prior to the Spin-off.

For the purposes of preparing the financial statements of the Biotechnology Business for the three months ended March 31, 2008, which were derived from PDL's historical consolidated financial statements, allocations of revenues, research and development expenses, asset impairment charges, restructuring charges, gains on sales of assets and non-operating income and expenses to Facet Biotech were made on a specific identification basis. Facet Biotech's operating expenses also included allocations related to information technology and facilities costs. Management believes that the Condensed Consolidated Statements of Operations for the three months ended March 31, 2008 include a reasonable allocation of costs incurred by PDL, which benefited Facet Biotech. However, such expenses may not be indicative of the actual level of expense that we would have incurred if we had operated as an independent, publicly traded company.

The accompanying condensed consolidated financial statements are unaudited, but include all adjustments (consisting only of normal, recurring adjustments) that we consider necessary for a fair presentation of our financial position at such dates and the operating results and cash flows for those periods. Certain information normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP) has been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for quarterly reporting.

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The information included in this Quarterly Report on Form 10-Q should be read in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2008 filed with the SEC. The Condensed Consolidated Balance Sheet as of December 31, 2008 is derived from our audited consolidated financial statements as of that date.

Our revenues, expenses, assets and liabilities vary during each quarter of the year. Therefore, the results and trends in these interim condensed consolidated financial statements may not be indicative of results for any other interim period or for the entire year. For example, revenue recognized in connection with the reimbursement of our research and development expenses under the terms of our collaboration agreements may vary period-to-period, and milestone payments received from our out-licensing agreements are often times recognized immediately when earned and could significantly affect the revenue reported in each period.

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Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries after elimination of inter-company accounts and transactions.

Management Estimates

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

Revenue Recognition

*Collaboration Agreements*

Under our collaborations with Biogen Idec Inc. (Biogen Idec) and Bristol-Myers Squibb Company (BMS), we share development costs related to the products covered by the collaboration. The purpose of the collaboration agreements is to create synergies while bringing a product candidate to market by sharing technologies, know-how and costs. Once a product is brought to market, we would share in commercialization costs as well as in profits related to the product, or generate a royalty based on net sales. Our collaboration agreements involve a combination of upfront fees, milestones and development costs for which we are not able to establish fair value of the undelivered elements. As such, we recognize these upfront fees, milestones and reimbursements of development costs as the services are performed. Each quarter, we and our collaborator reconcile what each party has incurred in terms of development costs, and we record either a net receivable or a net payable on our consolidated balance sheet. For each quarterly period, if we have a net receivable from a collaborator, we recognize revenues by such amount, and if we have a net payable to our collaborator, we recognize additional research and development R&D expenses by such amount. Therefore, our revenues and R&D expenses may fluctuate depending on which party in the collaboration is conducting the majority of the development activities.

For all periods presented, we have adopted Emerging Issues Task Force (EITF) Issue No. 07-1, Accounting for Collaborative Arrangements (EITF 07-1), which requires certain income statement presentation of transactions with third parties and of payments between the parties to the collaborative arrangement, along with disclosure about the nature and purpose of the arrangement.

*Out-License Agreements*

We have entered into license agreements under which licensees have obtained from us licenses to certain of our intellectual property rights, including patent rights, related to certain development product candidates, which we believe are not a strategic fit for our portfolio development

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strategy. In these arrangements, the licensee is customarily responsible for all of the development work on the licensed development product. We have no significant future performance obligations under these agreements. Upfront consideration that we receive for license agreements is recognized as revenue upon execution and delivery of the license agreement and when payment is reasonably assured. If the agreements require continuing involvement in the form of development, manufacturing or other commercialization efforts by us, we recognize revenues in the same manner as the final deliverable in the arrangement. Under out-license agreements, we may also receive annual license maintenance fees, payable at the election of the licensee to maintain the license in effect. We have no performance obligations with respect to such fees, and they are recognized as they are due and when payment is reasonably assured.

### *Humanization Agreements*

Under our humanization agreements, the licensee typically pays us an upfront fee to humanize an antibody. We recognize revenue related to these fees as the humanization work is performed, which is typically over three to six months, or upon acceptance of the humanized antibody by the licensee if such acceptance clause exists in the agreement. Under our humanization agreements, we may also receive annual maintenance fees, payable at the election of the licensee to maintain the humanization and know-how licenses in effect. We have no performance obligations with respect to such fees, and therefore, we recognize these fees as revenues when they are due and when payment is reasonably assured.

### *Milestones*

Our licensing and humanization arrangements may contain milestones related to reaching particular stages in product development. We recognize at risk milestone payments upon achievement of the underlying milestone event and when they are due and payable under the arrangement. Milestones are deemed to be at risk when, at the onset of an arrangement,

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management believes that they will require a reasonable amount of effort to be achieved and are not simply reached by the lapse of time or through a perfunctory effort. Milestones which are not deemed to be at risk are recognized as revenue in the same manner as up-front payments. We also receive milestone payments under patent license agreements, under which we have no further obligations, when our licensees reach certain stages of development with respect to the licensed product. We recognize these milestones as revenue once they have been reached and payment is reasonably assured.

Significant Customers and Revenues by Geographic Area

The following table summarizes revenues as a percentage of total revenues from our licensees and collaborators, which individually accounted for 10 percent or more of our revenues for the three months ended March 31, 2009 and 2008:

	Three Months Ended	
	March 31,	
	2009	2008
<b>Licensees</b>		
Biogen Idec	21%	57%
BMS	54%	*
EKR Therapeutics, Inc.	18%	*
Abbott Laboratories	*	21%
Progenics Pharmaceuticals, Inc.	*	21%

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\*Less than 10 percent

Cash Equivalents, Restricted Cash, Marketable Securities and Concentration of Credit Risk

We consider all highly liquid investments with initial maturities of three months or less at the date of purchase to be cash equivalents. We place our cash, cash equivalents and marketable securities with high-credit-quality financial institutions and, by policy, limit the amount of credit exposure in any one financial instrument. As of March 31, 2009 and December 31, 2008, we had a total of \$5.8 million of restricted cash, which supported letters of credit serving as a security deposit for our Redwood City, California property leases.

Earnings per Share

We calculate basic net loss per share by dividing net loss by the weighted-average number of common shares outstanding during the reported period. Diluted net loss per share is calculated using the sum of the weighted-average number of common shares outstanding and dilutive common equivalent shares outstanding. Common equivalent shares result from the assumed exercise of stock options, the assumed release of restrictions of issued restricted stock and the assumed issuance of common shares under our Employee Stock Purchase Plan (ESPP) using the treasury stock method.

For the three months ended March 31, 2008, the computation of net loss per basic and diluted share and the weighted-average shares outstanding are presented based on the 23.9 million shares that were issued in connection with the Spin-off on December 18, 2008. For the three months ended March 31, 2009, since we were in a net loss position, we did not include the effect of outstanding common equivalent shares in the diluted net loss per share calculations as their effect would have been anti-dilutive. We have excluded, on a weighted-average basis, 0.9 million of common equivalent shares relating to restricted stock awards from our diluted earnings per share calculations for the three months ended March 31, 2009.

### Income Taxes

Prior to July 2008, the operations of Facet Biotech were included in PDL's consolidated U.S. federal and state income tax returns and in tax returns of certain PDL foreign subsidiaries. Prior to the Spin-off on December 18, 2008, our provision for income taxes was determined as if Facet Biotech had filed tax returns separate and apart from PDL. We do not expect to record any federal or state income tax expense during 2009 based upon our projected U.S. tax loss for 2009. The income tax expense for the first quarter of 2008 related solely to foreign taxes on income earned by our foreign operations.

### **2. Stock-Based Compensation**

Prior to January 2009, our employees had received stock-based compensation awards only under PDL's equity compensation plans and, therefore, the amounts pertaining to the first quarter of 2008 relate to stock-based compensation expense that was allocated to Facet Biotech's operations related to PDL's stock-based equity awards. All non-vested PDL equity instruments

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held by Facet Biotech employees were cancelled on December 18, 2008 when those employees ceased being employed by a wholly-owned subsidiary of PDL as a result of the Spin-off. In January 2009, we began granting equity awards under our 2008 Equity Incentive Plan and in March 2009, we commenced employee participation in our 2008 Employee Stock Purchase Plan.

Stock-based compensation expense recognized under Statement of Financial Accounting Standards (SFAS) No. 123, Share-Based Payment (Revised 2004) (SFAS No. 123(R)) for employees and directors was as follows:

(in thousands)	Three Months Ended March 31,			
		2009		2008
Research and development	\$	386	\$	1,638
General and administrative		490		1,822
Total stock-based compensation expense	\$	876	\$	3,460

Valuation Assumptions

The stock-based compensation expense recognized under SFAS No. 123(R) was determined using the Black-Scholes option valuation model. Option valuation models require the input of subjective assumptions and these assumptions can vary over time. The weighted-average assumptions underlying stock-based compensation recognized under SFAS No. 123(R) related to awards granted under our equity plans were as follows:

	Three Months Ended March 31, 2009
<b>Stock Option Plans</b>	
Expected life, in years	5.3
Risk free interest rate	1.9%
Volatility	85%
Dividend yield	
<b>Employee Stock Purchase Plans</b>	
Expected life, in years	0.5
Risk free interest rate	0.5%
Volatility	115%
Dividend yield	

Stock Option Activity

A summary of our stock option activity for the period is presented below:

(share amounts in thousands)

**Stock Options**

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	Number of Shares	Weighted- Average Exercise Price
Outstanding as of December 31, 2008		\$
Granted	1,166	\$ 6.19
Exercised	(1)	\$ 6.17
Forfeited	(11)	\$ 6.17
Outstanding as of March 31, 2009	1,154	\$ 6.19
Exercisable as of March 31, 2009	38	\$ 6.18

Total unrecognized compensation expense related to unvested stock options outstanding as of March 31, 2009, excluding potential forfeitures, was \$4.6 million, which we expect to recognize over a weighted-average period of 3.6 years.

In April 2009, we granted approximately 688,000 fully-vested stock options to our employees (Value Transfer Grants). Consistent with the intent of these grants as disclosed in prior filings with the SEC, the Value Transfer Grants were provided to our employees to compensate them for the estimated value of vested PDL stock options that were forfeited in connection with the Spin-off. We expect the total fair value of the Value Transfer Grants to be between \$4 and \$5 million, as calculated using the Black-Scholes valuation model. As these stock options were fully vested as of the grant date, we will recognize 100 percent of the fair value of the Value Transfer Grants as stock-based compensation expense in the second quarter of 2009.



Table of ContentsRestricted Stock Award Activity

A summary of our restricted stock award activity for the period is presented below:

(share amounts in thousands)	Restricted Stock Awards	
	Number of Shares	Weighted-Average Grant-Date Fair Value
Unvested at December 31, 2008		\$
Granted	687	\$ 6.18
Vested	(11)	\$ 6.17
Forfeited	(20)	\$ 6.17
Unvested at March 31, 2009	656	\$ 6.18

Total unrecognized compensation expense related to unvested restricted stock outstanding as of March 31, 2009, excluding potential forfeitures, was \$3.8 million, which we expect to recognize over a weighted-average period of 2.5 years.

Employee Stock Purchase Plan

On March 1, 2009, employees were, for the first time, able to participate in the Facet Biotech 2008 ESPP. The stock-based compensation expense recognized in connection with our ESPP for the quarter ending March 31, 2009 was approximately \$0.1 million. Prior to the Spin-off, employees of PDL's Biotechnology Business were eligible to participate in PDL's 1993 ESPP plan. The stock-based compensation expense allocated to the Biotechnology Business and recognized in connection with PDL's ESPP for the quarter ended March 31, 2008 was \$0.3 million.

**3. Comprehensive Loss**

Comprehensive loss is comprised of net loss and other comprehensive income (loss). Specifically, we include in other comprehensive loss the changes in unrealized gains and losses on our holdings of available-for-sale securities, which are excluded from our net loss. In addition, other comprehensive loss includes the liability that has not yet been recognized as net periodic benefit cost for our postretirement benefit plan. The following table presents the calculation of our comprehensive loss:

(in thousands)	Three Months Ended	
	2009	2008
Net loss	\$ (29,172)	\$ (13,176)
Other comprehensive loss:		
Change in unrealized gains and losses on marketable securities	32	

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Change in postretirement benefit liability not yet recognized in net periodic benefit expense		19		18
Total comprehensive loss	\$	(29,121)	\$	(13,158)

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In March 2008, we sold our Minnesota manufacturing facility and related operations to an affiliate of Genmab A/S (Genmab), for total cash proceeds of \$240 million. Under the terms of the purchase agreement, Genmab acquired our manufacturing and related administrative facilities in Brooklyn Park, Minnesota, and related assets therein, and assumed certain lease obligations related to our former facilities in Plymouth, Minnesota (together, the Manufacturing Assets). We recognized a pre-tax gain of \$49.7 million upon the close of the sale in March 2008. Such gain represents the \$240 million in gross proceeds, less the net book value of the underlying assets transferred of \$185.4 million and \$4.9 million in transaction costs and other charges.

**5. Restructuring Charges**

The following table summarizes the restructuring activity for the first quarter of 2009, as discussed below, as well as the remaining liability balance, which is included in other accrued liabilities, at March 31, 2009:

(in thousands)	Personnel Related	Facilities Related	Total
Balance at December 31, 2008	\$ 1,956	\$ 135	\$ 1,956
Restructuring charges	4,070	135	4,205
Payments	(3,387)	(135)	(3,522)
Adjustments	(12)		(12)
Balance at March 31, 2009	\$ 2,627	\$ 135	\$ 2,627

2008 Company-wide Restructuring

In an effort to reduce our operating costs to a level more consistent with our competitors, in March 2008 we commenced a restructuring plan pursuant to which we immediately eliminated approximately 120 employment positions and would eliminate approximately 130 additional employment positions over the subsequent 12 months (the 2008 Restructuring Plan). All impacted employees were notified in March 2008.

Employees terminated in connection with the restructuring efforts were eligible for a specified severance package. We are recognizing severance charges for Transition Employees over their respective estimated service periods. During the three months ended March 31, 2008 and 2009, we recognized restructuring charges of \$5.5 million and \$0.2 million, respectively, under the 2008 Restructuring Plan, primarily consisting of post-termination severance costs as well as salary accruals relating to the portion of the 60-day notice period over which the terminated employees would not be providing services to the Company. We expect to pay the severance benefits under the 2008 Restructuring Plan by the end of the third quarter of 2009.

2008 French Office Restructuring

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During the fourth quarter of 2008, we decided to close our offices in France, which at the time employed seven individuals. During the first quarter of 2009, we recognized \$0.5 million in restructuring charges under this restructuring plan, of which \$0.4 million related to severance benefits and approximately \$0.1 million related to a contract termination fee for one of our French office leases. We expect to pay all obligations related to the closure of our French office by the end of the second quarter of 2009.

### 2009 Company-wide Restructuring

As a result of a strategic review process to enhance our focus and significantly reduce our operating expenses, we undertook a reduction in force in early 2009, pursuant to which we eliminated approximately 80 positions (the 2009 Restructuring Plan). As a result of the 2009 restructuring activities, we recognized charges related to severance benefits totaling approximately

\$3.5 million in the first quarter of 2009. We expect to pay the majority of the severance benefits related to the 2009 Restructuring Plan by the end of the third quarter of 2009.

In connection with the 2009 Restructuring Plan, we are vacating one of our two leased facilities in Redwood City (the Administration Building) and consolidating our operations into the other facility. In connection with the abandonment of the Administration Building, we expect to recognize lease-related charges in the second quarter of 2009. The restructuring charges will include estimated future facility costs for which we will obtain no future economic benefit, net of estimated future sublease income, over the term of our lease. Our estimates of future sublease income will involve significant

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assumptions regarding the time required to contract with subtenants, the amount of idle space we are able to sublease and the potential future sublease rates. We believe that it will take some time to contract with subtenants and that our contractual lease rates may be above market rates for comparable facilities. At this time, we are not able to make a good faith estimate of the amount or range of amounts of these additional charges or costs.

**6. Asset Impairment Charges**

Total asset impairment charges recognized during the three months ended March 31, 2009 and 2008 were zero and \$3.5 million, respectively. During the first quarter of 2008, such charges primarily represented the cost of certain research equipment that was expected to have no future useful life and certain information technology projects that were terminated and had no future benefit to us as a result of our restructuring activities.

**7. Other Accrued Liabilities**

Other accrued liabilities consisted of the following:

(in thousands)	March 31, 2009	December 31, 2008
Consulting and services	\$ 1,938	\$ 644
Restructuring	2,627	1,956
Accrued clinical and pre-clinical trial costs	1,499	1,031
Other	2,160	4
<b>Total</b>	<b>\$ 8,224</b>	<b>\$ 3,635</b>

**8. Fair Value Measurements**

SFAS No. 157, Fair Value Measurements establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include:

- Level 1 quoted prices in active markets for identical assets and liabilities
- Level 2 observable inputs other than quoted prices in active markets for identical assets and liabilities
- Level 3 unobservable inputs

At March 31, 2009, we determined the fair values of our financial assets using Level 1 and Level 2 inputs, as reflected in the table below:

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(in thousands)	Level 1		Level 2		Level 3		Total
Institutional money market funds	\$	258,567	\$		\$		\$ 258,567
Securities of U.S. Government sponsored entities				74,597			74,597
Corporate securities (1)				14,988			14,988
Total financial assets	\$	258,567	\$	89,585	\$		\$ 348,152

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(1) All corporate securities held at March 31, 2009, were secured by the U.S. Government under the terms of the Treasury Loan Guarantee Program.

We have excluded from the table above \$29.5 million of cash, which is included in the cash and cash equivalents caption in the Consolidated Balance Sheet as of March 31, 2009. As of December 31, 2008 all of our excess capital was held in cash accounts and was reflected as cash and cash equivalents in the Consolidated Balance Sheet.

## 9. Contingencies

As permitted under Delaware law, pursuant to the terms of our bylaws, we have agreed to indemnify our officers and directors and, pursuant to the terms of indemnification agreements, we have agreed to indemnify our executive officers and directors for certain events or occurrences, subject to certain limits, while the officer or director is or was serving as an officer or director of the Company. While the maximum amount of potential future indemnification is unlimited, we have a director and officer insurance policy in place that limits our exposure and may enable us to recover a portion of any future amounts paid. We believe the fair value of these indemnification agreements and bylaw provisions are immaterial, and accordingly, we have not recorded the fair value liability associated with these agreements as of March 31, 2009 or as of December 31, 2008.

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Under the terms of the Separation and Distribution Agreement, we and PDL each agreed to indemnify the other from and after the Spin-off with respect to the indebtedness, liabilities and obligations retained by our respective companies. These indemnification obligations could be significant. The ability to satisfy these indemnities if called upon to do so will depend upon the future financial strength of each of our companies. We cannot determine whether we will have to indemnify PDL for any substantial obligations in the future, nor can we be sure that, if PDL has to indemnify us for any substantial obligations, PDL will have the ability to satisfy those obligations.

In April 2009, we became aware of assertions from one of PDL's former commercial product distributors that it believes it should be reimbursed for overpayments of certain amounts relating to sales rebates on the sale of the Busulfex® commercial product in one European region during the 2006 and 2007 fiscal periods. While we are still investigating these assertions and their validity, under the terms of the indemnification provisions contained in the Separation and Distribution Agreement, we could be responsible for any amounts ultimately deemed due and payable to this distributor by PDL should these assertions be deemed valid. As any potential liability related to these assertions are neither probable nor estimable at this time, we have not recorded any liability relating to this matter on our balance sheet as of March 31, 2009.

**10. Subsequent Events**

In connection with the abandonment of the Administration Building under our 2009 Restructuring Plan, we expect to recognize lease-related charges in the second quarter of 2009. See Note 5 for more details of the lease-related charges and the 2009 Restructuring Plan.

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

*This report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended. All statements other than statements of historical facts are forward looking statements for purposes of these provisions, including any projections of earnings, revenues or other financial items, any statements of the plans and objectives of management for future operations, any statements concerning proposed new products or licensing or collaborative arrangements, any statements regarding future economic conditions or performance, and any statement of assumptions underlying any of the foregoing. In some cases, forward-looking statements can be identified by the use of terminology such as believes, may, will, expects, plans, anticipates, estimates, potential, or continue or the negative thereof or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this report are reasonable, there can be no assurance that such expectations or any of the forward-looking statements will prove to be correct, and actual results could differ materially from those projected or assumed in the forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to inherent risks and uncertainties, including the risk factors set forth below, and for the reasons described elsewhere in this report. All forward-looking statements and reasons why results may differ included in this report are made as of the date hereof, and we assume no obligation to update these forward-looking statements or reasons why actual results might differ.*

**OVERVIEW**

The information included in this management's discussion and analysis of financial conditions should be read in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2008 filed with the Securities and Exchange Commission (SEC), and our unaudited Consolidated Financial Statements for the three months ended March 31, 2009, as well as other disclosures, including the disclosures under Risk Factors, that have been included in this Quarterly Report on Form 10-Q.

Facet Biotech Corporation (we, us, our, the Company) is a biotechnology company that takes a disciplined, biology-driven approach to identify and develop oncology therapeutics. We have core competencies in tumor biology and antibody engineering, as evidenced by our pipeline of four clinical-stage candidates, all of which are products of our research efforts, as well as our proprietary protein engineering technology platform. Our business strategy focuses primarily on the following areas: (i) focusing our efforts in oncology, (ii) advancing our existing pipeline, (iii) expanding our pipeline and (iv) refining our protein engineering platform technologies.

**Basis of Presentation**

Facet Biotech was organized as a Delaware corporation in July 2008 by PDL BioPharma, Inc. (PDL) as a wholly owned subsidiary of PDL. PDL organized the Company in preparation for the Spin-off of the Company, which was effected on December 18, 2008 (the Spin-off). Prior to the Spin-off, PDL's Biotechnology Business was not operated by a legal entity separate from PDL and a direct ownership relationship did not exist among all the components comprising the Biotechnology Business. We describe the Biotechnology Business transferred to us by PDL in connection with the Spin-off as though the Biotechnology Business were our business for all historical periods described. However, Facet Biotech had not conducted any operations prior to the Spin-off. References in this quarterly report to the historical assets, liabilities, products, business or activities of our business are intended to refer to the historical assets, liabilities, products, business or activities of the Biotechnology Business as those were conducted as part of PDL prior to the Spin-off.



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We have prepared the condensed consolidated financial statements for the three months ended March 31, 2008 using PDL's historical cost basis of the various activities that comprise the Biotechnology Business as a component of PDL and reflect the results of operations and cash flows of the Biotechnology Business as a component of PDL. The statements of operations for the three months ended March 31, 2008 include expense allocations for general corporate overhead functions historically shared with PDL, including finance, legal, human resources, investor relations and other administrative functions, which include the costs of salaries, benefits, stock-based compensation and other related costs, as well as consulting and other professional services. Where appropriate, these allocations were made on a specific identification basis. Otherwise, the expenses related to services provided to the Biotechnology Business by PDL were allocated to Facet Biotech based on the relative percentages, as compared to PDL's other businesses, of headcount or another appropriate methodology depending on the nature of each item of cost to be allocated.

Table of Contents**Research and Development Programs**

We currently have several investigational compounds in various stages of development for the treatment of cancer and immunologic diseases, three of which we are developing with our collaboration partners; two with Biogen Idec Inc. and one with Bristol-Myers Squibb Company (BMS). The table below lists the antibodies for which we are pursuing development activities either on our own or in collaboration with other companies. These product candidates are at early stages of development, and none of our product candidates have been approved by the United States Food and Drug Administration (FDA) or commercialized in the indication in which our trials are focused. Not all clinical trials for each product candidate are listed below. The development and commercialization of our product candidates are subject to numerous risks and uncertainties, as noted in our Risk Factors of this Quarterly Report. For details on the development status of each product in the table below, please refer to Item 1 in our Annual Report on Form 10-K for the year ended December 31, 2008 as well as the Recent Developments section of this report below.

Product Candidate	Indication/Description	Program Status	Collaborator
Daclizumab	Multiple sclerosis	Phase 2	Biogen Idec
Volociximab (M200)	Solid tumors	Phase 1/2	Biogen Idec
Elotuzumab (HuLuc63)	Multiple myeloma	Phase 1	BMS
PDL192	Solid tumors	Phase 1	
PDL241	Immunologic diseases	Preclinical	*
Other preclinical research candidates	Oncology	Multiple candidates under evaluation	

\* BMS has an option to expand our collaboration to include the PDL241 antibody upon completion of certain pre-agreed preclinical studies, which we expect to complete in the second half of 2009.

**Recent Developments**

The following represents the significant events or developments that have occurred in the first quarter of 2009 and up to the date of the filing of this quarterly report:

- In January 2009, we undertook a restructuring effort pursuant to which we will eliminate approximately 80 positions. After the implementation of this 2009 restructuring plan, our workforce will be comprised of approximately 200 employment positions. We expect to recognize costs related to severance and post-termination benefits totaling approximately \$3.6 million, of which we recognized \$3.5 million in the first quarter of 2009.
- During April and early May 2009, we consolidated nearly all of our operations into one of our two leased facilities in Redwood City, and we will recognize lease-related restructuring charges in the second quarter of 2009 in connection with our vacating one of the two buildings. At this time, we are not able to make a good faith estimate of the amount or range of amounts of these charges. (See Note 10 to the Condensed Consolidated Financial Statements for further discussion of this charge.)

- In the first quarter for 2009, we and Biogen Idec announced that the FDA and European regulatory agencies agreed to consider an expanded SELECT study as one pivotal trial, thus requiring us to conduct only one additional registration-enabling study. As a result, we are preparing to amend the SELECT trial to increase the sample size from 300 to 600 patients and change the primary endpoint to annualized relapse rate.

#### **Summary Financial Results for the First Quarter of 2009 and Outlook**

In the first quarter of 2009, our total revenues were \$9.6 million, an increase from \$4.7 million in the comparable period in 2008. Our total expenses in the first quarter of 2009 were \$38.5 million, representing an increase from the \$17.4 million in operating expenses reported in the comparable 2008 period. This increase was due to the \$49.7 million reduction in operating expenses in the first quarter of 2008 as a result of the gain that we recognized on the sale of our former manufacturing and related administrative facilities in Brooklyn Park, Minnesota and the related assets (the Manufacturing Assets). Excluding this gain, operating expenses decreased by \$28.5 million compared to the first quarter of 2008.

Our net loss for the first quarter of 2009 was \$29.2 million, compared to \$13.2 million in the prior-year comparable period. In the first three months of 2009, net cash used in operating activities was \$20.0 million, a decrease from \$57.1 million used in operating activities in the comparable period in 2008. At March 31, 2009, we had cash, cash equivalents, marketable securities and restricted cash of \$383.4 million, compared to \$403.4 million at December 31, 2008.

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We expect that in the near-term, our total revenues will be marginally higher than amounts recognized in 2008, driven primarily by revenues recognized under our BMS collaboration. Future revenues will vary from period to period and will depend substantially on (1) whether we are successful in our existing collaborations and receive milestone payments thereunder, (2) whether we enter into new collaboration agreements or out-license agreements, (3) the potential milestone payments we receive related to our out-licensing agreements, (4) whether and to what extent expected development timelines change, which would impact the rate at which we recognize revenue related to certain previously received collaboration payments, and (5) the level of royalties we receive under the asset purchase agreement with EKR Therapeutics, Inc. (EKR), which was assigned to us by PDL in connection with the Spin-off. Our future collaboration revenues also will vary depending on which party in any collaboration is incurring the majority of development costs in any period (see our policy for revenues recognized under our collaboration agreements in Note 1 to the Condensed Consolidated Financial Statements).

Once we complete our restructuring activities in mid-2009, we expect our total operating expenses to be significantly lower than prior periods and increases or decreases thereof to correlate generally with the number of products we have under development and the phases of such development programs. Future operating expenses also will depend on whether we acquire the rights to additional products through in-licensing agreements or other means or enter into new collaboration agreements and will vary from period to period depending on which party in our existing collaboration, and any potential new collaboration, is incurring the majority of development costs in any period.

In addition, in April 2009, we granted approximately 688,000 fully-vested stock options to our employees (Value Transfer Grants). Consistent with the intent of these grants as disclosed in prior filings with the SEC, the Value Transfer Grants were provided to our employees to compensate them for the estimated value of vested PDL stock options that were forfeited in connection with the Spin-off. We expect the total fair value of the Value Transfer Grants to be between \$4 and \$5 million, as calculated using the Black-Scholes valuation model. As these stock options were fully vested as of the grant date, we will recognize 100 percent of the fair value of the Value Transfer Grants as stock-based compensation expense in the second quarter of 2009.

**CRITICAL ACCOUNTING POLICIES AND THE USE OF ESTIMATES**

There have been no material changes in our critical accounting policies, estimates and judgments during the quarter ended March 31, 2009 compared to the disclosures in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2008.

Table of Contents**RESULTS OF OPERATIONS***Three Months Ended March 31, 2009 and 2008***Revenues**

Revenues consist of (1) license and milestone revenues from collaborations, (2) reimbursement of research and development (R&D) expenses under collaborations and (3) other revenues. Other revenues include license, maintenance and milestone revenues from the out-licensing of our technologies, humanization revenues and royalties.

(in thousands)	Three Months Ended			% Change
	March 31,			
	2009	2008		
License and milestone revenues from collaborations	\$ 3,045	\$ 1,825		67%
Reimbursement of R&D expenses from collaborations	4,192	857		389%
Other	2,362	2,000		18%
Total revenues	\$ 9,599	\$ 4,682		105%

Total revenues increased by \$4.9 million during the quarter ended March 31, 2009 from the comparable 2008 period due primarily to an additional \$1.0 million and \$4.2 million of license revenues and reimbursement of research and development (R&D) expenses, respectively, recognized under our collaboration with BMS, which was executed in the third quarter of 2008, and the recognition of \$1.7 million of royalties received under our agreement with EKR. Such increases in revenues were partially offset by a reduction in revenues of \$0.6 million under our collaboration with Biogen Idec from the first quarter of 2008, due principally to increased expenses incurred by Biogen Idec under our collaboration in 2009 (see discussion below), and a \$1.4 million reduction in milestone and other revenues in 2009 from the first quarter of 2008.

With respect to the reimbursement of development costs, each quarter, we and our collaborators reconcile the development costs each party has incurred, and we record either a net receivable or a net payable in our consolidated financial statements. For each quarterly period, if we have a net receivable from a collaborator, we recognize revenues by such amount, and if we have a net payable to our collaborator, we recognize additional research and development expenses by such amount. Therefore, our revenues and research and development expenses may fluctuate depending on which party in the collaboration is incurring the majority of the development costs in any particular quarterly period.

**Costs and Expenses**

(in thousands)	Three Months Ended			% Change
	March 31,			
	2009	2008		
Research and development	\$ 24,065	\$ 45,237		(47)%
General and administrative	10,259	12,765		(20)%
Restructuring charges	4,205	5,547		*

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Asset impairment charges				3,521	*
Gain on sale of assets				(49,671)	*
Total costs and expenses	\$	38,529	\$	17,399	121%

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\* Not presented as calculation is not meaningful.

*Research and Development Expenses*

Our R&D activities include (1) Research, (2) Process Sciences, Manufacturing and Quality, and (3) Preclinical Sciences and Clinical Development. Our research activities include progressing candidates with validated targets and biological pathways from the preclinical stage to the clinic, utilizing translational research to better inform the clinical investigation of our therapeutics and refining our protein engineering technology platform. Our process sciences, manufacturing and quality activities include process, pharmaceutical and analytical development as well as supply chain and quality functions. Preclinical sciences and clinical development are comprised of preclinical development, toxicology, pharmacokinetics, bioanalytics and clinical development, which includes regulatory, safety, medical writing, biometry, U.S. and European

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clinical operations and program management. Our total R&D expenses for the first quarter of 2009 grouped by functional area within our R&D organization were as follows:

(in thousands)	Three Months Ended March 31, 2009	
Preclinical sciences and clinical development	\$	11,955
Process sciences, manufacturing and quality		7,105
Research		5,005
<b>Total R&amp;D expenses</b>	<b>\$</b>	<b>24,065</b>

We track our costs and expenses on a functional area basis and, as a result, we do not have detailed or complete cost breakdowns for our development programs. However, commencing in 2009, our financial systems now allow us to develop estimates of the direct costs associated with each of our active clinical and preclinical programs (Direct Program Costs), which include out-of-pocket expenses as well as estimated employee-related costs. Out-of-pocket costs include costs of conducting our clinical trials, such as fees to clinical research organizations (CROs) and clinical investigators, and monitoring, data management, drug supply and manufacturing expenses, costs of conducting preclinical studies and technology licensing fees. The employee-related costs were estimated by applying an average per-employee cost for our research and development organization to the number of direct employees dedicated to the programs during the quarter ended March 31, 2009. Our Direct Program Costs do not include: (i) allocations of research and development management or overhead costs, (ii) allocations of facilities and information technology (IT) expenses, (iii) depreciation expenses, (iv) amortization of intangible assets, or (v) stock-based compensation. The following table reflects our estimated Direct Program Costs for each of our active clinical and preclinical development programs, as well as Other Direct R&D Costs and Costs Allocated to R&D, as described in the footnotes below, for the first quarter of 2009:

(in thousands)	Three Months Ended March 31, 2009		
<b>Estimated Direct Program Costs:</b>			
Daclizumab (1)	\$	2,820	
Elotuzumab (2)		4,589	
Volociximab (3)		1,165	
PDL 241		1,469	
PDL 192		1,121	
Other R&D Programs (4)		1,818	
			<b>% of Total R&amp;D Costs</b>
<b>Total estimated direct program costs</b>	<b>\$</b>	<b>12,982</b>	<b>54%</b>
<b>Other Direct R&amp;D Costs (5)</b>		<b>3,703</b>	<b>15%</b>
<b>Costs Allocated to R&amp;D:</b>			
Depreciation and amortization		1,118	5%
Corporate overhead (6)		5,876	24%
Stock compensation		386	2%
<b>Total R&amp;D expenses</b>	<b>\$</b>	<b>24,065</b>	

- (1) Daclizumab costs include \$1.8 million in expense reimbursements payable to Biogen Idec under our collaboration agreement.
- (2) Elotuzumab costs include \$3.9 million of development expenses that are reimbursable to us by BMS under our collaboration agreement. The \$3.9 million that is reimbursable by BMS is reflected within collaboration revenues in the condensed consolidated financial statements for the three months ended March 31, 2009.

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- (3) Volociximab costs include \$0.1 million in expense reimbursements payable to Biogen Idec under our collaboration agreement.
- (4) Other R&D Programs consist primarily of research, protein engineering and preclinical trial activities related to programs that have not reached the late preclinical stage.
- (5) Other Direct R&D Costs include non-program research and development costs, such as non-program specific research, process sciences and manufacturing activities, quality and compliance activities related to laboratory, manufacturing and clinical practices, and senior management time across all of our R&D activities as senior management does not allocate its time to specific programs.
- (6) Corporate overhead represents allocations of facilities and IT costs to R&D expenses.



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R&D expenses decreased by \$21.2 million from the first quarter of 2008 to the first quarter of 2009 due primarily to lower employee-related and overhead expenses in 2009 resulting from the impact of both the sale of the Manufacturing Assets during the first quarter of 2008 and our restructuring activities. This reduction in costs was also driven by a decrease in volociximab development costs and partially offset by increases in development costs for elotuzumab and daclizumab due to the progress of these programs.

*General and Administrative Expenses*

General and administrative expenses generally consist of costs of personnel, professional services, consulting and other expenses related to our administrative functions, including finance, information technology, facilities, legal, human resources, business development and marketing, and an allocation of facility and overhead costs. The \$2.5 million decrease in general and administrative expenses during the first quarter of 2009 in comparison to 2008 was driven by lower legal and other expenses associated with the broader strategic initiatives that were underway during the first quarter of 2008 as well as lower employee-related expenses in 2009 resulting from the 2008 and 2009 restructuring and other cost reduction activities.

*Restructuring Charges*

*The restructuring charges incurred during the first quarter of 2009 related to \$3.5 million of expenses recognized in connection with our 2009 restructuring activities, \$0.5 million in connection with the closure of our offices in Paris, France during the first quarter of 2009 and \$0.2 million in charges related to transition employees under our 2008 Restructuring Plan. The \$5.5 million of restructuring charges incurred during the first quarter of 2008 related solely to our 2008 restructuring activities. The decrease in restructuring charges during the first quarter of 2009 in comparison to 2008 is primarily attributable to the lower number of employees terminated under the 2009 plan in comparison to the 2008 plan. See Note 5 to the Condensed Consolidated Financial Statements for additional information.*

*Gain on Sale of Assets*

In March 2008, we sold our Manufacturing Assets to an affiliate of Genmab A/S (Genmab) for total cash proceeds of \$240 million. We recognized a pre-tax gain of \$49.7 million upon the close of the sale in March 2008.

*Asset Impairment Charges*

Total asset impairment charges recognized during the three months ended March 31, 2009 and 2008 were zero and \$3.5 million, respectively. During the first quarter of 2008, such charges primarily represented the cost of certain research equipment that we expected to have no future useful life and certain information technology projects that we terminated that had no future benefit to us as a result of our restructuring activities.

**Interest and Other Income and Interest Expense**

(in thousands)	Three Months Ended				% Change
	March 31,				
	2009	2008			
Interest and other income	\$ 180	\$ 3			*
Interest expense	(422)	(434)			*
Total interest and other income, net and interest expense	\$ (242)	\$ (431)			*

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\* Not presented as calculation is not meaningful.

Interest and other income relates to interest earned on our cash and available-for-sale securities accounts during the periods. The increase in interest income during the first quarter of 2009 from the first quarter of 2008 is due to our investment in the first quarter of 2009 of the \$405 million cash distribution to us from PDL in December 2008 in connection with the Spin-off. Interest expense consists primarily of a portion of our lease payments on one of our two leased facilities in Redwood City, California. For accounting purposes, we are considered to be the owner of the leased property and we have recorded the fair value of the building and a corresponding long-term financing liability on our Consolidated Balance Sheets.

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**Income Taxes**

Prior to July 2008, the operations of Facet Biotech were included in PDL's consolidated U.S. federal and state income tax returns and in tax returns of certain PDL foreign subsidiaries. Prior to the Spin-off on December 18, 2008, our provision for income taxes was determined as if Facet Biotech had filed tax returns separate and apart from PDL. We do not expect to record any federal or state income tax expense during 2009 based upon our projected U.S. tax loss for 2009. The income tax expense for the first quarter of 2008 related solely to foreign taxes on income earned by our foreign operations. We are currently in the process of dissolving our foreign operations and therefore expect our foreign tax expense will be zero for 2009.

**LIQUIDITY AND CAPITAL RESOURCES**

In connection with the Spin-off, PDL provided to us cash and cash equivalents of \$405 million. We expect this initial \$405 million cash contribution, as well as future payments from Biogen Idec and BMS related to our collaboration agreements with these entities, and royalty and milestone revenues from certain other agreements, will fund our operations and working capital requirements through approximately the end of 2012 based on current operating plans. Prior to the Spin-off on December 18, 2008, the Biotechnology Business of PDL was funded entirely by PDL.

Net cash used in operating activities for the three months ended March 31, 2009 was \$20.0 million, compared to \$57.1 million in the corresponding period in 2008. The decrease in net cash used in operating activities during the first three months of 2009 was primarily attributable to lower employee-related and overhead expenses resulting from both the sale of our Manufacturing Assets during the first quarter of 2008 and our restructuring efforts as well as changes in our working capital balances during the period.

Net cash used in investing activities was \$89.4 million for the three months ended March 31, 2009, compared to net cash provided by investing activities of \$245.9 million in the comparable period in 2008. The net cash used in investing activities in the first quarter of 2009 was primarily related to the purchase of marketable securities. The net cash provided by investing activities in the first quarter of 2008 was attributable primarily to net proceeds of \$236.6 million received in connection with the sale of the Manufacturing Assets and the release of \$10.0 million of restricted cash relating to our Redwood City, California, facility.

Net cash used in financing activities for the three months ended March 31, 2009 was \$0.2 million, compared to \$188.8 million in the comparable period in 2008. During the first quarter of 2009, cash used in financing activities was primarily related to payments on our long-term financing liability. Net cash used in financing activities in 2008 was primarily due to net funding to our parent company as well as due to payments on our long-term financing liability.

Our future capital requirements will depend on numerous factors, including, among others, progress of product candidates in clinical trials; the ability of our licensees to obtain regulatory approval and successfully manufacture and market products licensed under our patents; the continued or additional support by our collaborators or other third parties of R&D efforts and clinical trials; investment in existing and new R&D programs; time required to gain regulatory approvals; our ability to obtain and retain funding from third parties under collaborative arrangements; the demand for our potential products, if and when approved; potential acquisitions of technology, product candidates or businesses by us; our ability to sublease our excess capacity; and the costs of defending or prosecuting any patent opposition or litigation

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necessary to protect our proprietary technology. In order to develop and obtain regulatory approval for our potential products, we will need to raise substantial additional funds through equity or debt financings, collaborative or out-licensing arrangements or other means. We cannot assure that such additional financing will be available on acceptable terms, if at all, and such financing may only be available on terms dilutive to our stockholders.

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As of March 31, 2009, our contractual commitments had not changed materially from those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2008, with the exception of the scheduled payments made under our Redwood City facilities leases during the first quarter of 2009. Our material contractual obligations under lease, debt, construction, contract manufacturing and other agreements as of December 31, 2008, were as follows:

(In thousands)	Payments Due by Period				Total
	Less Than 1 Year	1-3 Years	3-5 Years	More than 5 Years	
<b>CONTRACTUAL OBLIGATIONS</b>					
Lease payments(1)	\$ 6,779	\$ 13,914	\$ 16,777	\$ 100,334	\$ 137,804
Other lease related obligations(2)	5,827	11,922	12,296	53,412	83,457
Other(3)	398	340	178	1,345	2,261
Contract manufacturing	3,789	6,400			10,189
Total contractual obligations	\$ 16,793	\$ 32,576	\$ 29,251	\$ 155,091	\$ 233,711

- (1) Lease payments represent actual and estimated contractual rental payments under our facility leases in Redwood City, California and Paris, France. Included in these contractual obligations are amounts related to the Lab Building in Redwood City, for which we have a liability on our consolidated financial statement of \$26.2 million as of December 31, 2008. These lease obligations reflect our estimates of future lease payments, which are subject to potential escalations based on market conditions after the year 2014 and, therefore, could be higher than amounts included in the table.
- (2) Other lease-related obligations reflect estimated amounts that we are contractually required to pay over the term of the Redwood City leases, including insurance, property taxes and common area maintenance fees. Such amounts are estimated based on historical costs that we have incurred since the inception of the leases.
- (3) Other contractual obligations include post-retirement benefits and other operating leases for office equipment.

In addition to the amounts disclosed in the table above, we had committed to make payments for certain retention related benefits totaling approximately \$5.1 million as of December 31, 2008. Further, we had committed to make potential future milestone payments to third parties as part of in-licensing and product development programs. Payments under these agreements generally become due and payable only upon achievement of certain clinical development, regulatory and/or commercial milestones. Because the achievement of these milestones has not yet occurred, such contingencies have not been recorded in our Consolidated Balance Sheet as of December 31, 2008. We estimate that such milestones that could be due and payable over the next year approximate \$0.9 million and milestones that could be due and payable over the next three years approximate \$4.3 million.

In addition to the contractual obligation discussed above, under the terms of the Separation and Distribution Agreement, we agreed to indemnify PDL with respect to indebtedness, liabilities and obligations, other than PDL's convertible notes, that PDL will retain that do not relate to PDL's Royalty Business. In April 2009, we became aware of assertions from one of PDL's former commercial product distributors that it believes it should be reimbursed for overpayments of certain amounts relating to sales rebates on the sale of the Busulfex® commercial product in one European region during the 2006 and 2007 fiscal periods. While we are still investigating these assertions and their validity, under the terms of the indemnification provisions contained in the Separation and Distribution Agreement, we could be responsible for any amounts ultimately deemed due and payable to this distributor by PDL should these assertions be deemed valid. As any potential liability related to these assertions are neither probable nor estimable at this time, we have not recorded any liability relating to this matter on our balance sheet as of March 31, 2009.



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**RISK FACTORS**

*This Quarterly Report includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities and Exchange Act of 1934, as amended. All statements other than statements of historical facts are forward looking statements for purposes of these provisions, including any projections of earnings, revenues or other financial items, any statements of the plans and objectives of management for future operations, any statements concerning proposed new products or licensing or collaborative arrangements, any statements regarding future economic conditions or performance, and any statement of assumptions underlying any of the foregoing. In some cases, forward-looking statements can be identified by the use of terminology such as believes, may, will, expects, plans, anticipates, estimates, potential, or continue or the negative thereof or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this Quarterly Report are reasonable, there can be no assurance that such expectations or any of the forward-looking statements will prove to be correct, and actual results could differ materially from those projected or assumed in the forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to inherent risks and uncertainties, including the risk factors set forth below, and for the reasons described elsewhere in this Quarterly Report. All forward-looking statements and reasons why results may differ included in this Quarterly Report are made as of the date hereof, and we assume no obligation to update these forward-looking statements or reasons why actual results might differ.*

***If our research and development efforts are not successful, we may not be able to effectively develop new products.***

We are engaged in research activities intended to, among other things, progress therapeutic candidates into clinical development. In the near-term, we will focus on obtaining new product candidates through various means, including in-licensing them from or entering in to strategic collaborations with institutions or other biotechnology or pharmaceutical companies. Acquiring rights to products in this manner poses risks, including that we may not be unable to successfully integrate the research, development and commercialization capabilities necessary to bring these products to market. In addition, we may not be able to identify or acquire suitable products to in-license.

Our antibody product candidates are in various stages of development and many are in an early development stage. If we are unsuccessful in our research efforts to identify and obtain rights to new validated targets and develop product candidates that lead to the required regulatory approvals and the successful commercialization of products, our ability to develop new products could be harmed.

***Our business strategy is dependent on our ability to in-license or otherwise acquire the rights to develop and commercialize products.***

We have determined that for the foreseeable future, the expansion of our existing pipeline should be accomplished primarily through the in-licensing or other acquisition of additional pre-clinical and clinical oncology programs. Therefore, our future success will depend in substantial part upon identifying and in-licensing or otherwise acquiring such therapeutic products from third parties. While we are actively seeking clinical programs that fit within our strategic objectives, the competition for the acquisition of attractive oncology programs is intense, and we cannot assure you that we will be able to in-license or otherwise acquire clinical programs in the future on acceptable terms, if at all. In addition, we may acquire clinical programs for indications in which we have limited expertise and, as a result, we may need to attract and retain additional personnel or expand existing functions to manage the development of these programs. There can be no assurance that we will not meet challenges in integrating potential new programs or personnel to manage those programs, and any such programs could be delayed or fail as a result.

If we are unable to in-license or otherwise acquire development programs on acceptable terms and successfully develop and commercialize them, our business could be harmed.

*Unless our clinical studies demonstrate the safety and efficacy of our product candidates, we will not be able to commercialize our product candidates.*

To obtain regulatory approval to market and sell any of our existing or future product candidates, we must satisfy the FDA and other regulatory authorities abroad, through extensive preclinical and clinical studies, that our product candidates have an acceptable safety profile and are efficacious. We may not conduct the types of testing eventually required by regulatory authorities to demonstrate an adequate safety profile for the particular indication, or the tests may indicate that the safety profile of our product candidates is unacceptably inferior to therapeutics with comparable efficacy or otherwise unsuitable for use in humans in light of the expected therapeutic benefit of the product candidate. Clinical trials and preclinical testing are expensive, can take many years and have an uncertain outcome. In addition, initial testing in preclinical studies or in phase 1 or phase 2 clinical trials may indicate that the safety profile of a product candidate is adequate for approval, but does not ensure that safety issues may not arise in later trials, or that the overall safety profile for a product candidate will be sufficient for regulatory approval in any particular product indication. We may experience numerous unforeseen events during, or as a result of, the preclinical testing or clinical studies or clinical development, which could delay or prevent our ability to develop or commercialize our product candidates, including:

- our testing or trials may produce inconclusive or negative safety results, which may require us to conduct additional testing or trials or to abandon product candidates that we believed to be promising;



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- our product candidates may have unacceptable pharmacology, toxicology or carcinogenicity; and
- our product candidates may cause significant adverse effects in patients.

Even if we are able to demonstrate efficacy of any product candidate, any adverse safety events would increase our costs and could delay or prevent our ability to continue the development of or commercialize our product candidates, which would adversely impact our business, financial condition and results of operations. We are aware that our drug candidates can cause various adverse side effects in humans, some of which are predictable and some of which are unpredictable. We proceed to evaluate the safety and efficacy of these drug candidates based on data we accumulate from preclinical assessments and ongoing clinical studies. We believe that our drug candidates have an acceptable safety profile for the potential indications in which we are currently conducting clinical trials. Data from ongoing or future clinical trials may indicate that a drug candidate causes unanticipated or more significant adverse side effects either used alone or when used in combination with other drugs, in particular patient populations or at increased dosages or frequency of administration. This may lead us to conclude that the drug candidate does not have an acceptable safety profile for a particular patient population or use.

***The clinical development of drug products is inherently uncertain and expensive and subject to extensive government regulation.***

Our future success depends almost entirely upon the success of our clinical development efforts. Clinical development, however, is a lengthy, time-consuming and expensive process and subject to significant risks of failure. In addition, we must expend significant amounts to comply with extensive government regulation of the clinical development process.

Before obtaining regulatory approvals for the commercial sale of any products, we must demonstrate through preclinical testing and clinical trials that our product candidates are safe and effective for their intended use in humans. We have incurred and will continue to incur substantial expense for, and we have devoted and expect to continue to devote a significant amount of time to, preclinical testing and clinical trials. Despite the time and expense incurred, our clinical trials may not adequately demonstrate the safety and effectiveness of our product candidates.

Completion of clinical development generally takes several years or more. The length of time necessary to complete clinical trials and submit an application for marketing and manufacturing approvals varies significantly according to the type, complexity and intended use of the product candidate and is difficult to predict. Further, we, the FDA, the EMEA, investigational review boards or data safety monitoring boards may decide to temporarily suspend or permanently terminate ongoing trials. Failure to comply with extensive regulations may result in unanticipated delay, suspension or cancellation of a trial or the FDA's or EMEA's refusal to accept test results. As a result of these factors, we cannot predict the actual expenses that we will incur with respect to preclinical or clinical trials for any of our potential products, and we expect that our expense levels will fluctuate unexpectedly in the future. Despite the time and expense incurred, we cannot guarantee that we will successfully develop commercially viable products that will achieve FDA or EMEA approval or market acceptance, and failure to do so would materially harm our business, financial condition and results of operations.

Early clinical trials such as phase 1 and 2 trials generally are designed to gather information to determine whether further trials are appropriate and, if so, how such trials should be designed. As a result, data gathered in these trials may indicate that the endpoints selected for these trials are not the most relevant for purposes of assessing the product or the design of future trials. Moreover, success or failure in meeting such early clinical trial endpoints may not be dispositive of whether further trials are appropriate and, if so, how such trials should be designed. We may

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decide, or the FDA or other regulatory agencies may require us, to make changes in our plans and protocols. Such changes may relate, for example, to changes in the standard of care for a particular disease indication, comparability of efficacy and toxicity of potential drug product where a change in the manufacturing process or manufacturing site is proposed, or competitive developments foreclosing the availability of expedited approval procedures. We may be required to support proposed changes with additional preclinical or clinical testing, which could delay the expected time line for concluding clinical trials.

Larger or later stage clinical trials may not produce the same results as earlier trials. Many companies in the pharmaceutical and biotechnology industries, including us, have suffered significant setbacks in clinical trials, including advanced clinical trials, even after promising results had been obtained in earlier trials. For example, in August 2007, PDL announced that it would terminate the phase 3 program of its *Nuvion*® (visilizumab) antibody in intravenous steroid-refractory ulcerative colitis because data from treated patients showed insufficient efficacy and an inferior safety profile in the visilizumab arm compared to IV steroids alone.

Even when a drug candidate shows evidence of efficacy in a clinical trial, it may be impossible to further develop or receive regulatory approval for the drug if it causes an unacceptable incidence or severity of side effects, or further development may be slowed by the need to find dosing regimens that do not cause such side effects.

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In addition, we may not be able to successfully commence and complete all of our planned clinical trials without significant additional resources and expertise because we have a number of potential products in clinical development. The approval process takes many years, requires the expenditure of substantial resources, and may involve post-marketing surveillance and requirements for post-marketing studies. The approval of a product candidate may depend on the acceptability to the FDA or other regulatory agencies of data from our clinical trials. Regulatory requirements are subject to frequent change. Delays in obtaining regulatory approvals may:

- adversely affect the successful commercialization of any drugs that we develop;
- impose costly procedures on us;
- diminish any competitive advantages that we may attain; and
- adversely affect our receipt of any revenues or royalties.

In addition, we may encounter regulatory delays or failures of our clinical trials as a result of many factors, all of which may increase the costs and expense associated with the trial, including:

- changes in regulatory policy during the period of product development;
- delays in obtaining sufficient supply of materials to enroll and complete clinical studies according to planned timelines;
- delays in obtaining regulatory approvals to commence a study;
- delays in identifying and reaching agreement on acceptable terms with prospective clinical trial sites;
- delays in the enrollment of patients;

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- lack of efficacy during clinical trials; or
- unforeseen safety issues.

Regulatory review of our clinical trial protocols may cause us in some cases to delay or abandon our planned clinical trials. Our potential inability to commence or continue clinical trials, to complete the clinical trials on a timely basis or to demonstrate the safety and efficacy of our potential products, further adds to the uncertainty of regulatory approval for our potential products.

*We may be unable to enroll a sufficient number of patients in a timely manner in order to complete our clinical trials.*

The rate of completion of clinical trials is significantly dependent upon the rate of patient enrollment. Patient enrollment is a function of many factors, including:

- the size of the patient population;
- perceived risks and benefits of the drug under study;
- availability of competing therapies, including those in clinical development;
- availability of clinical drug supply;
- availability of clinical trial sites;
- design of the protocol;
- proximity of and access by patients to clinical sites;
- patient referral practices of physicians;

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- eligibility criteria for the study in question; and
- efforts of the sponsor of and clinical sites involved in the trial to facilitate timely enrollment.

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We may have difficulty obtaining sufficient patient enrollment or clinician support to conduct our clinical trials as planned, and we may need to expend substantial additional funds to obtain access to resources or delay or modify our plans significantly. These considerations may result in our being unable to successfully achieve our projected development timelines, or potentially even lead us to consider the termination of ongoing clinical trials or development of a product for a particular indication.

***If our collaborations are not successful or are terminated by our collaborators, we may not effectively develop and market some of our product candidates.***

We have agreements with biotechnology and other companies to develop, manufacture and market certain of our potential products. In some cases, we rely on our collaborators to manufacture such products and essential components for those products, design and conduct clinical trials, compile and analyze the data received from these trials, obtain regulatory approvals and, if approved, market these licensed products. As a result, we may have limited or no control over the manufacturing, development and marketing of these potential products and little or no opportunity to review the clinical data prior to or following public announcement. In addition, the design of the clinical studies may not be sufficient or appropriate for regulatory review and approval and we may have to conduct further studies in order to facilitate approval.

In September 2005 and August 2008, respectively, we entered into collaboration agreements with Biogen Idec for the joint development of daclizumab in certain indications, including MS, and volociximab (M200) in all indications, and BMS for the co-development of elotuzumab in multiple myeloma and other potential oncology indications. These agreements are particularly important to us. The collaboration agreements provide significant combined resources for the development, manufacture and potential commercialization of covered products. We and our collaborators each assume certain responsibilities and share expenses. Because of the broad scope of the collaborations, we are particularly dependent upon the performance by Biogen Idec and BMS of their respective obligations under the agreements. The failure of Biogen Idec or BMS to perform their obligations, our failure to perform our obligations, our failure to effectively manage the relationships, or a material contractual dispute between us and either of our collaborators could have a material adverse effect on our prospects or financial results. Moreover, our financial results depend in substantial part upon our efforts and related expenses for these programs. Our revenues and expenses recognized under each collaboration will vary depending on the work performed by us and our collaborators in any particular reporting period.

We rely on other collaborators, such as contract manufacturers, clinical research organizations, medical institutions and clinical investigators, including physician sponsors, to conduct nearly all of our clinical trials, including recruiting and enrolling patients in the trials. If these parties do not successfully carry out their contractual duties or meet expected deadlines, we may be delayed or may not obtain regulatory approval for or commercialize our product candidates. If any of the third parties upon whom we rely to conduct our clinical trials do not comply with applicable laws, successfully carry out their obligations or meet expected deadlines, our clinical trials may be extended, delayed or terminated.

If the quality or accuracy of the clinical data obtained by third party contractors is compromised due to their failure to adhere to applicable laws, our clinical protocols or for other reasons, we may not obtain regulatory approval for or successfully commercialize any of our product candidates. If our relationships with any of these organizations or individuals terminates, we believe that we would be able to enter into arrangements with alternative third parties. However, replacing any of these third parties could delay our clinical trials and could jeopardize our ability to obtain regulatory approvals and commercialize our product candidates on a timely basis, if at all.

Our collaborators can terminate our collaborative agreements under certain conditions, and in some cases on short notice. A collaborator may terminate its agreement with us or separately pursue alternative products, therapeutic approaches or technologies as a means of developing treatments for the diseases targeted by us, or our collaborative effort. Even if a collaborator continues to contribute to the arrangement, it may nevertheless decide not to actively pursue the development or commercialization of any resulting products. In these circumstances, our ability to

pursue potential products could be severely limited.

In 2004 and 2005, we entered into two collaboration arrangements with Roche for the joint development and commercialization of daclizumab for the treatment of asthma and other respiratory diseases and transplant indications. In 2006, Roche notified us of its election to discontinue its involvement in both of these collaboration arrangements. As a result of the termination of this relationship, we suspended the active clinical development of daclizumab in these indications and, consequently, the development expenses related to the development of daclizumab in these indications were reduced from historical and forecasted levels. Under the terms of the agreement governing this collaboration with Roche, the costs of clinical studies and other development costs were shared by Roche through the effective termination dates, so our financial condition was not materially affected as a result of the termination of these collaborations.

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Continued funding and participation by collaborators will depend on the continued timely achievement of our research and development objectives, the retention of key personnel performing work under those agreements and on each collaborator's own financial, competitive, marketing and strategic capabilities and priorities. These considerations include:

- the commitment of each collaborator's management to the continued development of the licensed products or technology;
- the relationships among the individuals responsible for the implementation and maintenance of the development efforts; and
- the relative advantages of alternative products or technology being marketed or developed by each collaborator or by others, including their relative patent and proprietary technology positions, and their ability to manufacture potential products successfully.

Our ability to enter into new relationships and the willingness of our existing collaborators to continue development of our potential products depends upon, among other things, our patent position with respect to such products. If we are unable to successfully maintain our patents we may be unable to collect royalties on existing licensed products or enter into additional agreements.

In addition, our collaborators may independently develop products that are competitive with products that we have licensed to them. This could reduce our revenues or the likelihood of achieving revenues under our agreements with these collaborators.

***We must protect our patent and other intellectual property rights to succeed.***

Our success is dependent in significant part on our ability to develop and protect patent and other intellectual property rights and operate without infringing the intellectual property rights of others.

Our pending patent applications may not result in the issuance of valid patents or the claims and claim scope of our issued patents may not provide competitive advantages. Also, our patent protection may not prevent others from developing competitive products using related or other technology that does not infringe our patent rights. A number of companies, universities and research institutions have filed patent applications or received patents in the areas of antibodies and other fields relating to our programs. Some of these applications or patents may be competitive with our applications or have claims that could prevent the issuance of patents to us or result in a significant reduction in the claim scope of our issued patents. In addition, patent applications are confidential for a period of time after filing. We therefore may not know that a competitor has filed a patent application covering subject matter similar to subject matter in one of our patent applications or that we were the first to invent the innovation we seek to patent. This may lead to disputes including interference proceeding or litigation to determine rights to patentable subject matter. These disputes are often expensive and may result in our being unable to patent an innovation.



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The scope, enforceability and effective term of patents can be highly uncertain and often involve complex legal and factual questions and proceedings. No consistent policy has emerged regarding the breadth of claims in biotechnology patents, so that even issued patents may later be modified or revoked by the relevant patent authorities or courts. These proceedings could be expensive, last several years and either prevent issuance of additional patents to us or result in a significant reduction in the scope or invalidation of our patents. Any limitation in claim scope could reduce our ability to negotiate future collaborative research and development agreements based on these patents. Moreover, the issuance of a patent in one country does not assure the issuance of a patent with similar claim scope in another country, and claim interpretation and infringement laws vary among countries, so we are unable to predict the extent of patent protection in any country.

In addition to seeking the protection of patents and licenses, we also rely upon trade secrets, know-how and continuing technological innovation that we seek to protect, in part, by confidentiality agreements with employees, consultants, suppliers and licensees. If these agreements are not honored, we might not have adequate remedies for any breach. Additionally, our trade secrets might otherwise become known or patented by our competitors.

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*We may need to obtain patent licenses from others in order to manufacture or sell our potential products and we may not be able to obtain these licenses on terms acceptable to us or at all.*

Other companies, universities and research institutions may obtain patents that could limit our ability to use, import, manufacture, market or sell our products or impair our competitive position. As a result, we may need to obtain licenses from others before we could continue using, importing, manufacturing, marketing, or selling our products. We may not be able to obtain required licenses on terms acceptable to us, if at all. If we do not obtain required licenses, we may encounter significant delays in product development while we redesign potentially infringing products or methods or we may not be able to market our products at all.

We do not have a license to an issued U.S. patent assigned to Stanford University and Columbia University, which may cover a process used to produce our potential products. We have been advised that an exclusive license has been previously granted to a third party, Centocor, under this patent. If our processes were found to be covered by either of these patents, we might need to obtain licenses or to significantly alter our processes or products. We might not be able to successfully alter our processes or products to avoid conflicts with these patents or to obtain licenses on acceptable terms or at all.

We do not have licenses to issued U.S. patents which may cover one of our development-stage products. If we successfully develop this product, we might need to obtain licenses to these patents to commercialize the product. In the event that we need to obtain licenses to these patents, we may not be able to do so on acceptable terms or at all.

*The failure to gain market acceptance of our product candidates among the medical community would adversely affect any product revenue we may receive in the future.*

Even if approved, our product candidates may not gain market acceptance among physicians, patients, third-party payers and the medical community. We may not achieve market acceptance even if clinical trials demonstrate safety and efficacy and we obtain the necessary regulatory and reimbursement approvals. The degree of market acceptance of any product candidates that we develop will depend on a number of factors, including:

- establishment and demonstration of clinical efficacy and safety;
- cost-effectiveness of our product candidates;
- their potential advantage over alternative treatment methods;
- reimbursement policies of government and third-party payers; and

- marketing and distribution support for our product candidates, including the efforts of our collaborators where they have marketing and distribution responsibilities.

Physicians will not recommend our products until clinical data or other factors demonstrate the safety and efficacy of our product as compared to conventional drug and other treatments. Even if we establish the clinical safety and efficacy of our product candidates, physicians may elect not to use our product for any number of other reasons, including whether the mode of administration of our products is effective for certain indications. Antibody products, including our product candidates as they would be used for certain disease indications, are typically administered by infusion or injection, which requires substantial cost and inconvenience to patients. Our product candidates, if successfully developed, may compete with a number of drugs and therapies that may be administered more easily. The failure of our product candidates to achieve significant market acceptance would materially harm our business, financial condition and results of operations.

*We face significant competition.*

We face significant competition from entities who have substantially greater resources than we have, more experience in the commercialization and marketing of pharmaceuticals, superior product development capabilities and superior personnel resources. Potential competitors in the United States and other countries include major pharmaceutical, biotechnology and chemical companies, specialized pharmaceutical companies and universities and other research institutions. These entities have developed and are developing human or humanized antibodies or other compounds for treating cancers or immunologic diseases that may compete with our products in development and technologies that may compete with our development products or antibody technologies. These competitors may succeed in more rapidly developing and marketing technologies and products that are more effective than our product candidates or technologies or that would render any future commercialized products or technology obsolete or noncompetitive. Our product candidates and any future commercialized products may also face significant competition from both brand-name and generic manufacturers that could adversely affect any future sales of our products.

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If daclizumab were to be approved for the treatment of relapsing multiple sclerosis, it would face competition from currently approved and marketed products, including interferons, such as Biogen Idec's Avonex®, Bayer HealthCare Pharmaceuticals' Betaseron® and EMD Serono Inc.'s Rebif®, a non-interferon immune modifier, Teva Pharmaceutical Industries Ltd.'s Copaxone®, and a monoclonal antibody, Biogen Idec and Elan Pharmaceuticals, Inc.'s Tysabri®. Further competition could arise from drugs currently in development, including Novartis Pharmaceutical Corporation's (Novartis) FTY720 and other monoclonal antibodies in development, such as Genzyme Corporation's Campath®, Genmab A/S's ofatumumab, and Genentech, Inc. (Genentech) and Roche's ocrelizumab.

If elotuzumab were to be approved for the treatment of multiple myeloma, it would face competition from currently approved and marketed products, including Celgene Corporation's Revlimid® and Thalomid® and Millennium Pharmaceuticals, Inc.'s Velcade®. Further competition could arise from drugs currently in development, including Centocor, Inc.'s CNTO-328, Genentech and Seattle Genetics, Inc.'s dacetuzumab, Novartis and Xoma Ltd.'s lucatumumab, and Pfizer Inc.'s (Pfizer) CP-751871.

If volociximab (M200) were to be approved for the treatment of non-small cell lung cancer or ovarian cancer, it would face competition from a number of other anti-angiogenic agents in pre-clinical and clinical development, including antibody candidates such as Pfizer's CP-751,871, ImClone Systems Incorporated's (ImClone) Erbitux® and Novartis's ASA404, each of which are in more advanced stages of development than is volociximab. In addition, many other VEGF or VEGFR targeted agents are in advanced stage of development and many other anti-angiogenesis agents are in earlier stage of development, which could compete with volociximab should it be approved for marketing.

If PDL192 were to be approved for the treatment of solid tumors, it would face competition from many agents that are used for solid tumors, such as ImClone's Erbitux®, Genentech's Avastin®, and other monoclonal antibodies and targeted agents in development which potentially modulate the TWEAK pathway, including Biogen Idec's anti-Tweak monoclonal antibody, BIIB023.

Any product that we or our collaborators succeed in developing and for which regulatory approval is obtained must then compete for market acceptance and market share. The relative speed with which we and our collaborators can develop products, complete the clinical testing and approval processes, and supply commercial quantities of the products to the market compared to competitive companies will affect market success. In addition, the amount of marketing and sales resources and the effectiveness of the marketing used with respect to a product will affect its marketing success.

The biotechnology and pharmaceutical industries are highly competitive. None of our current product candidates is approved for marketing and we do not expect any of our candidates to receive marketing approval in the next several years, if at all. The competitive environment for any of our product candidates which may be approved for marketing at the time of commercialization is highly speculative and uncertain, but we anticipate that such products would face substantial competition from marketed products and from product candidates in development, if approved.

***Changes in the U.S. and international health care industry, including regarding reimbursement rates, could adversely affect the commercial value of our development product candidates.***

The U.S. and international health care industry is subject to changing political, economic and regulatory influences that may significantly affect the purchasing practices and pricing of pharmaceuticals. The FDA and other health care policies may change, and additional government

regulations may be enacted, which could prevent or delay regulatory approval of our product candidates. Cost containment measures, whether instituted by health care providers or imposed by government health administration regulators or new regulations, could result in greater selectivity in the purchase of drugs. As a result, third-party payers may challenge the price and cost effectiveness of our products. In addition, in many major markets outside the United States, pricing approval is required before sales may commence. As a result, significant uncertainty exists as to the reimbursement status of approved health care products.

We may not be able to obtain or maintain our desired price for the products we develop. Any product we introduce may not be considered cost effective relative to alternative therapies. As a result, adequate third-party reimbursement may not be available to enable us to obtain or maintain prices sufficient to realize an appropriate return on our investment in product development, should any of our development products be approved for marketing. Also, the trend towards managed health care in the United States and the concurrent growth of organizations such as health maintenance organizations, as well as legislative proposals to reform health care or reduce government insurance programs, may all result in lower prices, reduced reimbursement levels and diminished markets for our development products. These factors will also affect the products that are marketed by our collaborators and licensees. We cannot predict the likelihood, nature or extent of adverse government regulation that may arise from future legislation or administrative action, either in the United States or abroad. If we are not able to maintain regulatory compliance, we might not be permitted to market our future products and our business could suffer.

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*We may be unable to obtain or maintain regulatory approval for our products.*

Even if the FDA grants us marketing approval for a product, the FDA may impose post-marketing requirements, such as:

- labeling and advertising requirements, restrictions or limitations, such as the inclusion of warnings, precautions, contra-indications or use limitations that could have a material impact on the future profitability of our product candidates;
- adverse event reporting;
- testing and surveillance to monitor our product candidates and their continued compliance with regulatory requirements; and
- inspection of products and manufacturing operations and, if any inspection reveals that the product or operation is not in compliance, prohibiting the sale of all products, suspending manufacturing or withdrawing market clearance.

The discovery of previously unknown problems with our product candidates, including adverse events of unanticipated severity or frequency, may result in restrictions of the products, including withdrawal from manufacture. Additionally, certain material changes affecting an approved product such as manufacturing changes or additional labeling claims are subject to further FDA review and approval. The FDA may revisit and change its prior determination with regard to the safety or efficacy of our products and withdraw any required approvals after we obtain them. Even prior to any formal regulatory action requiring labeling changes or affecting manufacturing, we could voluntarily decide to cease the distribution and sale or recall any of our future products if concerns about their safety and efficacy develop.

As part of the regulatory approval process, we or our contractors must demonstrate the ability to manufacture the pharmaceutical product to be approved. Accordingly, the manufacturing process and quality control procedures are required to comply with the applicable FDA cGMP regulations and other regulatory requirements. Good manufacturing practice regulations include requirements relating to quality control and quality assurance as well as the corresponding maintenance of records and documentation. Manufacturing facilities must pass an inspection by the FDA before initiating commercial manufacturing of any product. Pharmaceutical product manufacturing establishments are also subject to inspections by state and local authorities as well as inspections by authorities of other countries. To supply pharmaceutical products for use in the United States, foreign manufacturing establishments must comply with these FDA approved guidelines. These foreign manufacturing establishments are subject to periodic inspection by the FDA or by corresponding regulatory agencies in these countries under reciprocal agreements with the FDA. The FDA enforces post-marketing regulatory requirements, such as cGMP requirements, through periodic unannounced inspections. Failure to pass an inspection could disrupt, delay or shut down our manufacturing operations. Although we do not have currently marketed products, the foregoing considerations would be important to our future selection of contract manufacturers.

Our collaborators, licensees and we also are subject to foreign regulatory requirements regarding the manufacture, development, marketing and sale of pharmaceutical products and, if the particular product is manufactured in the United States, FDA and other U.S. export provisions. These requirements vary widely in different countries. Difficulties or unanticipated costs or price controls may be encountered by us or our licensees or

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marketing collaborators in our respective efforts to secure necessary governmental approvals. This could delay or prevent us, our licensees or our marketing collaborators from marketing potential pharmaceutical products.

Further, regulatory approvals may be withdrawn if we do not comply with regulatory standards or if problems with our products occur. In addition, under a BLA, the manufacturer continues to be subject to facility inspection and the applicant must assume responsibility for compliance with applicable pharmaceutical product and establishment standards. If we fail to comply with applicable FDA and other regulatory requirements at any stage during the regulatory process, we may be subject to sanctions, including:

- warning letters;
- clinical holds;
- product recalls or seizures;
- changes to advertising;
- injunctions;

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- refusal of the FDA to review pending market approval applications or supplements to approval applications;
- total or partial suspension of product manufacturing, distribution, marketing and sales;
- civil penalties;
- withdrawals of previously approved marketing applications; and
- criminal prosecutions.

*We rely on sole source, third parties to manufacture our products.*

We do not have the capability to manufacture any of our development-stage products. We rely upon third parties, including Biogen Idec and Genmab, for our manufacturing requirements, and we will be reliant on BMS for the manufacture of elotuzumab if this program progresses into phase 2 development. If we experience supply problems with our manufacturing partners, there may not be sufficient supplies of our development-stage products for us to meet clinical trial demand, in which case our operations and results could suffer. In addition, routine failures in the manufacturing process may lead to increased expenses and result in unforeseen delays in the progress of our clinical studies.

Our products must be manufactured in facilities that comply with FDA and other regulations, and the process for qualifying and obtaining approval for a manufacturing facility is time-consuming. The manufacturing facilities on which we rely will be subject to ongoing, periodic unannounced inspection by the FDA and state agencies to ensure compliance with good manufacturing practices and other requirements.

If our relationship with Genmab or Biogen Idec were to terminate unexpectedly or on short notice or expire without being renewed, our ability to meet clinical trial demand for our development-stage products could be adversely affected while we qualify a new manufacturer for that product and our operations and future results could suffer. In addition, we would need to expend a significant amount of time and incur significant costs to qualify a new manufacturer and transfer technology to the new manufacturer, which would also adversely affect our results of operations.

Product supply interruptions, whether as a result of regulatory action or the termination of a relationship with a manufacturer, could significantly delay clinical development of our potential products, reduce third-party or clinical researcher interest and support of proposed clinical trials, and possibly delay commercialization and sales of these products.



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Our ability to file for, and to obtain, regulatory approvals for our products, as well as the timing of such filings, will depend on the abilities of the contract manufacturers we engage. We or our contract manufacturers may encounter problems with the following:

- development of advanced manufacturing procedures, process controls and scalability of our manufacturing processes;
- production costs and yields;
- quality control and assurance;
- availability of qualified personnel;
- availability of raw materials;
- adequate training of new and existing personnel;
- ongoing compliance with standard operating procedures;
- ongoing compliance with applicable regulations;
- production costs; and
- development of advanced manufacturing techniques and process controls.

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***Manufacturing changes may result in delays in obtaining regulatory approval or marketing for our products.***

When we make changes in the manufacturing process driven by increases in demand for our products in clinical studies, we may be required to demonstrate to the FDA and corresponding foreign authorities that the changes have not caused the resulting drug material to differ significantly from the drug material previously produced. Further, any significant manufacturing changes for the production of our product candidates could result in delays in development or regulatory approval or in the reduction or interruption of commercial sales of our product candidates. Our or our contract manufacturers' inability to maintain manufacturing operations in compliance with applicable regulations within our planned time and cost parameters could materially harm our business, financial condition and results of operations.

We have made manufacturing changes and are likely to make additional manufacturing changes for the production of our products currently in clinical development. These manufacturing changes or an inability to immediately show comparability between old and new materials before and after making manufacturing changes could result in delays in development or regulatory approvals or in reduction or interruption of commercial sales and could impair our competitive position.

***We must comply with extensive government regulations and laws.***

We and our collaboration partners are subject to extensive regulation by federal government, state governments, and the foreign countries in which we conduct our business.

In particular, we are subject to extensive and rigorous government regulation as a developer of drug products. For example, the FDA regulates, among other things, the development, testing, research, manufacture, record-keeping, labeling, storage, approval, quality control, adverse event reporting, advertising, promotions, sale and distribution of biotechnology products. Our product candidates are subject to extensive regulation by foreign governments. The regulatory review and approval process, which includes preclinical studies and clinical trials of each product candidate, is lengthy, expensive and uncertain.

We must rely on our contract manufacturers and third-party suppliers for regulatory compliance and adhering to the FDA's current Good Manufacturing Practices (cGMP) requirements. If these manufacturers or suppliers fail to comply with applicable regulations, including FDA pre- or post-approval inspections and cGMP requirements, then the FDA could sanction us. These sanctions could include fines, injunctions, civil penalties, failure of regulatory authorities to grant marketing approval of our products, delay, suspension or withdrawal of approvals, license revocation, product seizures or recalls, operational restrictions or criminal prosecutions, any of which could significantly and adversely affect our business.

If our operations are found to violate any applicable law or other governmental regulations, we may be subject to civil and criminal penalties, damages and fines. Similarly, if the hospitals, physicians or other providers or entities with which we do business are found non-compliant with applicable laws, they may be subject to sanctions, which could also have a negative impact on us. The risk of our being found in violation of these laws is increased by the fact that many of them have not been fully interpreted by the regulatory authorities or the courts, and their provisions are open to a variety of interpretations, and additional legal or regulatory change. Any action against us for violation of these laws, even if we successfully defend against it, could cause us to incur significant legal expenses, divert our management's attention from the operation of our business and damage our reputation.

We expend a significant amount on compliance efforts and such expenses are unpredictable and may adversely affect our results. Changing laws, regulations and standards may also create uncertainty and increase insurance costs. We are committed to compliance and maintaining high standards of corporate governance and public disclosure. As a result, we intend to invest all reasonably necessary resources to comply with evolving standards, and this investment may result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

*We may incur significant costs in order to comply with environmental regulations or to defend claims arising from accidents involving the use of hazardous materials.*

We are subject to federal, state and local laws and regulations governing the use, discharge, handling and disposal of materials and wastes used in our operations. As a result, we may be required to incur significant costs to comply with these laws and regulations. We cannot eliminate the risk of accidental contamination or injury from these materials. In the event of such an accident, we could be held liable for any resulting damages and incur liabilities, which exceed our resources. In addition, we cannot predict the extent of the adverse effect on our business or the financial and other costs that might result from any new government requirements arising out of future legislative, administrative or judicial actions.

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***We may be subject to product liability claims, and our insurance coverage may not be adequate to cover these claims.***

We face an inherent business risk of exposure to product liability claims in the event that the use of products during research and development efforts or after commercialization results in adverse effects. This risk exists even with respect to any products that receive regulatory approval for commercial sale. While we maintain liability insurance for our products, it may not be sufficient to satisfy any or all liabilities that may arise. Also, adequate insurance coverage may not be available in the future at acceptable cost, if at all.

We maintain product liability insurance for claims arising from the use of our product candidates in clinical trials prior to FDA approval at levels that we believe are appropriate for similarly situated companies in the biotechnology industry. However, we may not be able to maintain our existing insurance coverage or obtain additional coverage on commercially reasonable terms for the use of our other product candidates and products in the future. Also, our insurance coverage and resources may not be sufficient to satisfy liability resulting from product liability claims, which could materially harm our business, financial condition or results of operations. While we believe our product liability insurance is reasonable, we cannot assure you that this coverage will be adequate to protect us in the event of a claim.

***We may be required to satisfy certain indemnification obligations to PDL or may not be able to collect on indemnification rights from PDL.***

Under the terms of the Separation and Distribution Agreement, we agreed to indemnify PDL from and after the Spin-off with respect to indebtedness, liabilities and obligations, other than PDL's convertible notes, that PDL will retain that do not relate to PDL's Royalty Business. Our ability to satisfy these indemnities, if called upon to do so, will depend upon our future financial strength.

In April 2009, we became aware of assertions from one of PDL's former commercial product distributors that it believes it should be reimbursed for overpayments of certain amounts relating to sales rebates on the sale of the Busulfex® commercial product in one European region during the 2006 and 2007 fiscal periods. While we are still investigating these assertions and their validity, under the terms of the indemnification provisions contained in the Separation and Distribution Agreement, we could be responsible for any amounts ultimately deemed due and payable to this distributor by PDL should these assertions be deemed valid. As any potential liability related to these assertions are neither probable nor estimable at this time, we have not recorded any liability relating to this matter on our balance sheet as of March 31, 2009.

We are not aware of any other potential material indemnification obligations at this time, but any such indemnification obligations that may arise could be significant. We cannot determine whether we will have to indemnify PDL for any substantial obligations in the future.

***We must attract and retain highly skilled employees in order to succeed.***

To be successful, we must attract and retain qualified clinical, scientific and management personnel and we face significant competition for experienced personnel. If we do not succeed in attracting and retaining qualified personnel, particularly at the management level, our business could be impaired. In connection with PDL's strategic review and asset sale processes, PDL eliminated a significant number of employment positions. In October 2007, we effected a workforce reduction related to our former manufacturing operations, which included the termination of 103 employees, and, in March 2008, we eliminated 166 employment positions resulting from the sale of the Manufacturing Assets. Also in

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March 2008, we commenced a restructuring effort pursuant to which we would terminate approximately 250 employment positions and, in January 2009, we announced a further reduction in force pursuant to which we eliminated approximately 80 positions. Subsequent to all restructuring efforts, which we expect to occur by the third quarter of 2009, we anticipate that our workforce will consist of approximately 200 employment positions. The uncertainty caused by these strategic reviews and asset sale processes, restructuring and related reductions-in-force that we have undertaken created anxiety among our employees. We believe that this caused attrition to increase because of employees uncertainty regarding the continuation of employment. We have put in place severance, retention and compensation programs in an effort to mitigate the number of voluntary terminations, however, these programs may not provide effective incentive to employees to stay with us. The uncertainty may also make the recruitment of key personnel more difficult, which could adversely affect our operations, particularly if we lose and need to replace key executives. The Spin-off represents a further change and our employees may have concerns about our prospects as a stand-alone company, including our ability to successfully operate the new entity and our ability maintain our independence. If we are not successful in assuring our employees of our prospects as an independent company, our employees may seek other employment, which could materially adversely affect our business. We are particularly dependent on our executive officers, and we generally do not have employment agreements with specified terms with our executives. We are currently engaged in a search for a new Chief Medical Officer and a Vice President of Research. The failure to timely

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recruit a new Chief Medical Officer and Vice President of Research could adversely impact the effectiveness of our research and development efforts. Also, we rely on our research, development and product operations staff, all of whom are valuable but the loss of any one of whom would not have a material adverse effect on the Company.

*We anticipate that we will incur losses for the foreseeable future. We may never achieve or sustain profitability.*

Our business has experienced significant net losses and we expect to continue to incur additional net losses over the next several years as we continue our research and development activities and incur significant preclinical and clinical development costs. During the years ended December 31, 2008, 2007 and 2006, we recognized a cumulative loss of \$575.8 million. Since we or our collaborators or licensees may not successfully develop additional products, obtain required regulatory approvals, manufacture products at an acceptable cost or with appropriate quality, or successfully market such products with desired margins, our expenses may continue to exceed any revenues we may receive. Our commitment of resources to the continued development of our products will require significant additional funds for development. Our operating expenses also may increase if:

- our earlier stage potential products move into later stage clinical development, which is generally a more expensive stage of development;
- additional preclinical product candidates are selected for further clinical development;
- we in-license or otherwise acquire additional products;
- we pursue clinical development of our potential products in new indications;
- we increase the number of patents we are prosecuting or otherwise expend additional resources on patent prosecution, defense or analyses; and
- we invest in research or acquire additional technologies or businesses.

In the absence of substantial licensing, milestone and other revenues from third-party collaborators, royalties on sales of products licensed under our intellectual property rights, future revenues from our products in development or other sources of revenues, we will continue to incur operating losses and will likely require additional capital to fully execute our business strategy. The likelihood of reaching, and time required to reach, sustained profitability are highly uncertain.

*If additional capital is not available, we may have to curtail or cease operations.*

Although we expect that we will have sufficient cash to fund our operations and working capital requirements through approximately the end of 2012 based on current operating plans, we may need to raise additional capital in the future to:

- fund our research and development programs;
- develop and commercialize our product candidates;
- respond to competitive pressures; and
- acquire complementary businesses or technologies.

Our future capital needs depend on many factors, including:

- the scope, duration and expenditures associated with our research and development programs;
- continued scientific progress in these programs;
- the costs and expenses related to, and the consequences of, potential licensing or acquisition transactions, if any;
- competing technological developments;
- our proprietary patent position, if any, in our product candidates;

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- our facilities expenses, which will vary depending on the time and terms of any facility sublease we may enter into; and
- the regulatory approval process for our product candidates.

We may seek to raise necessary funds through public or private equity offerings, debt financings or additional collaborations and licensing arrangements. We may not be able to obtain additional financing on terms favorable to us, if at all. General market conditions may make it very difficult for us to seek financing from the capital markets. We may be required to relinquish rights to our technologies or product candidates, or grant licenses on terms that are not favorable to us, in order to raise additional funds through collaborations or licensing arrangements. If adequate funds are not available, we may have to delay, reduce or eliminate one or more of our research or development programs and reduce overall overhead expenses. These actions may reduce the market price of our common stock.

***We may obtain future financing through the issuance of debt or equity, which may have an adverse effect on our stockholders or may otherwise adversely affect our business.***

If we raise funds through the issuance of debt or equity, any debt securities or preferred stock issued will have rights, preferences and privileges senior to those of holders of our common stock in the event of liquidation. In such event, there is a possibility that once all senior claims are settled, there may be no assets remaining to pay out to the holders of common stock. In addition, if we raise funds through the issuance of additional equity, whether through private placements or public offerings, such an issuance would dilute ownership of current stockholders in us.

The terms of debt securities may also impose restrictions on our operations, which may include limiting our ability to incur additional indebtedness, to pay dividends on or repurchase our capital stock, or to make certain acquisitions or investments. In addition, we may be subject to covenants requiring us to satisfy certain financial tests and ratios, and our ability to satisfy such covenants may be affected by events outside of our control.

***We may not receive the contingent consideration related to the sale of the product rights to new formulations of Cardene and the ularitide development-stage product under the Asset Purchase Agreement with EKR.***

In March 2008, PDL sold the product rights to the marketed product Cardene, new formulations of Cardene IV and the ularitide development-stage product, among other assets, to EKR. The transaction included contingent consideration of up to \$85 million in development and sales milestones related to the new Cardene IV formulations, \$25 million of which PDL received in August 2008, as well as royalty payments related to sales of the new Cardene IV formulations and ularitide. In connection with the Spin-off, PDL assigned to us the asset purchase agreement under which EKR is obligated to pay the remaining \$60 million in milestone payments and royalty payments dependent upon certain contingencies, including future net sales. In November 2008, PDL received its first royalty payment from EKR on net sales of new formulations of the Cardene product (the Cardene Pre-Mixed Bag), which commercially launched in September 2008. Also in September 2008, products were introduced by The Medicines Company and by Teva Pharmaceuticals that compete with Cardene. Although Teva's competing product was withdrawn from the market, we expect that Teva will reintroduce a competing product. As a result of this increased competition in the market served by Cardene, we do not expect to receive the \$60 million in milestone payments that we would earn only if EKR achieves certain Cardene Pre-Mixed Bag sales thresholds or material amounts of royalties on sales of the Cardene Pre-Mixed Bag.



*We have no history operating as an independent company upon which you can evaluate us.*

We have a very limited operating history as a stand-alone entity. While our Biotechnology Business had constituted a substantial part of the historic operations of PDL, we had not operated as a stand-alone company without the Royalty Business prior to the Spin-off. As an independent company, our ability to satisfy our obligations and achieve profitability will be solely dependent upon the future performance of our Biotechnology Business, and we are not able to rely upon the capital resources and cash flows of the Royalty Business, which remained with PDL.

We may not be able to successfully implement the changes necessary to operate independently, and we may incur additional costs operating independently, which would have a negative effect on our business, results of operations and financial condition.

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***Our historical financial information is not necessarily indicative of our future financial position, future results of operations or future cash flows and may not reflect what our financial position, results of operations or cash flows would have been as a stand-alone company during the periods presented.***

Our historical financial information included in this Quarterly Report for the three months ended March 31, 2008 does not necessarily reflect what our results of operations or cash flows would have been as a stand-alone company during the periods presented and is not necessarily indicative of our future results of operations or future cash flows. This is primarily a result of the following factors:

- prior to our separation, our business was operated by PDL as part of its broader corporate organization and we did not operate as a stand-alone company;
- certain general administrative functions were performed by PDL for the combined entity. Our historical consolidated financial statements reflect allocations of costs for services shared with PDL. These allocations may differ from the costs we will incur for these services as an independent company;
- our historical financial statements include the operation of our manufacturing facility. The facility was sold in the first quarter of 2008;
- during 2007 and 2008, we substantially reduced the number of employees of the Biotechnology Business, and we are in the process of implementing the reductions; and
- after the completion of the Spin-off from PDL, the cost of capital for our business may be higher than PDL's cost of capital prior to our separation because PDL's credit ratings were better than what we currently anticipate ours will be in the foreseeable future.

***Our operating expenses and results and any future revenue likely will fluctuate in future periods.***

Our revenues and expenses may be unpredictable and may fluctuate from quarter to quarter due to, among other things, the timing and the unpredictable nature of clinical trial, manufacturing and related expenses, including payments owed by us and to us under collaborative agreements for reimbursement of expenses, and future milestone revenues under collaborative agreements. In addition, the recognition of clinical trial and other expenses that we otherwise would recognize over a period of time under applicable accounting principles may be accelerated in certain circumstances. In such a case, it may cause our expenses during that period to be higher than they otherwise would have been had the circumstances not occurred. For example, if we terminate a clinical trial for which we paid non-refundable upfront fees to a clinical research organization and in which we did not accrue all of the patient costs, the recognition of the expense associated with those fees that we were recognizing as we accrued patient costs would be accelerated and recognized in the period in which the termination occurred.

*The market price for our shares may fluctuate widely.*

Market prices for securities of biotechnology companies have been highly volatile, and we expect such volatility to continue for the foreseeable future, so that investment in our securities involves substantial risk. Additionally, the stock market from time to time has experienced significant price and volume fluctuations unrelated to the operating performance of particular companies. The following are some of the factors that may have a significant effect on the market price of our common stock:

- results of clinical trials;
- approval or introduction of competing products and technologies;
- developments or disputes as to patent or other proprietary rights;
- failures or unexpected delays in timelines for our potential products in development, including the obtaining of regulatory approvals;
- delays in manufacturing or clinical trial plans;
- fluctuations in our operating results;
- announcements by other biotechnology or pharmaceutical companies;

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- initiation, termination or modification of agreements with our collaborators or disputes or disagreements with collaborators;
- acquisition of rights to develop and potentially commercialize products through in-licensing agreements and other means;
- loss of key personnel;
- litigation or the threat of litigation;
- public concern as to the safety of drugs developed by us;
- sales of our common stock held by insiders; and
- comments and expectations of results made by securities analysts or investors.

If any of these factors causes us to fail to meet the expectations of securities analysts or investors, or if adverse conditions prevail or are perceived to prevail with respect to our business, the price of the common stock would likely drop significantly. A significant drop in the price of a company's common stock often leads to the filing of securities class action litigation against the Company. This type of litigation against us could result in substantial costs and a diversion of management's attention and resources.

***Your percentage ownership in Facet Biotech may be diluted in the future.***

Your percentage ownership in Facet Biotech may be diluted in the future because of equity awards that we expect will be granted to our directors, officers and employees as well as other equity instruments that may be issued in the future such as debt and equity financing. Under the Facet Biotech 2008 Equity Incentive Plan (the 2008 Equity Incentive Plan), which provides for the grant of equity-based awards, including restricted stock, restricted stock units, stock options, stock appreciation rights and other equity-based awards, to our directors, officers and other employees, advisors and consultants, we have reserved a total of 3.5 million shares of our common stock for issuance. Through April 2009, we have granted 1.9 million shares in stock option and restricted stock awards, and we expect to continue to grant additional equity-based awards to our employees and directors in the future.

*Provisions in our certificate of incorporation and bylaws and of Delaware law may prevent or delay an acquisition of our company, which could decrease the trading price of our common stock.*

Our certificate of incorporation, bylaws and Delaware law contain provisions that are intended to deter coercive takeover practices and inadequate takeover bids by making such practices or bids unacceptably expensive to the raider and to encourage prospective acquirors to negotiate with our Board rather than to attempt a hostile takeover. These provisions include, among others:

- no right of our stockholders to act by written consent;
- procedures regarding how stockholders may present proposals or nominate directors for election at stockholder meetings;
- the right of our Board to issue preferred stock without stockholder approval; and
- no stockholder rights to call a special stockholders meeting.

Delaware law also imposes some restrictions on mergers and other business combinations between us and any holder of 15 percent or more of our outstanding common stock.

We believe these provisions protect our stockholders from coercive or otherwise unfair takeover tactics by requiring potential acquirors to negotiate with our Board and by providing our Board with more time to assess any acquisition proposal. These provisions are not intended to make our company immune from takeovers. However, these provisions apply even if the offer may be considered beneficial by some stockholders and could delay or prevent an acquisition that our Board determines is not in the best interests of our company and our stockholders.

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

We place our cash, cash equivalents and marketable securities with multiple financial institutions in the United States. Deposits with banks may exceed the amount of insurance provided on such deposits. While we monitor the cash balances in our operating accounts and adjust the cash balances as appropriate, these cash balances could be impacted if the underlying financial institutions fail or could be subject to other adverse conditions in the financial markets. To date, we have not experienced any loss or lack of access to cash in our operating accounts or to our cash equivalents and marketable securities in our investment portfolios. Financial instruments that potentially subject us to concentrations of credit risk consist primarily of money market funds, U.S. government-sponsored enterprise securities and commercial paper secured under the Treasury Loan Guarantee Program. Our investment policy limits the amount we may invest in any one type of investment issuer, thereby reducing credit risk concentrations.

The fair value of our cash equivalents and marketable securities at March 31, 2009 was \$348.2 million. These investments include \$258.6 million of cash equivalents which are due in less than three months, \$56.0 million of short-term investments which are due within one year and \$33.6 million of long-term investments which are due between one year and two years from March 31, 2009. Our investment strategy is to manage our marketable securities portfolio to preserve principal and liquidity while maximizing the return on the investment portfolio through the full investment of available funds. We invest the majority of our marketable securities portfolio in short-term securities with at least an investment grade rating of A to minimize interest rate and credit risk as well as to provide for an immediate source of funds. Although changes in interest rates may affect the fair value of the marketable securities portfolio and cause unrealized gains or losses, such gains or losses would not be realized unless the investments are sold. Due to the nature of our investments, which are primarily money market funds, U.S. government-sponsored enterprise securities and commercial paper secured under the Treasury Loan Guarantee Program, we have concluded that there is no material market risk exposure.

If market interest rates were to have increased by 1 percent as of March 31, 2009, the fair value of our portfolio would have declined by approximately \$1 million. The modeling technique used measures changes in the fair values arising from an immediate hypothetical shift in market interest rates and assumes ending fair values include principal plus accrued interest. As of March 31, 2009, a portion of our portfolio was invested in a Treasury security based money market fund. Due to historically low yields in the Treasury market and Treasury money market funds, some Treasury based money market funds have closed to new investors and/or limited additional deposits. Additionally, some Treasury money market funds have been in a negative yield situation, causing investors to lose shares, despite the shares maintaining a \$1.00 net asset value. Credit and liquidity risks in the current market could also adversely affect the value of our investments in prime money market funds. If the difference between amortized cost and outside market valuations becomes significant, the fund's valuation may change causing the fund to break the buck (move from the USD 1.00 net asset value). Many of the current issues affecting prime money market funds involve investments in commercial paper issued by Structured Investment Vehicles, or SIVs. Rating agencies have downgraded certain commercial paper issues and issuers, which has caused some funds to hold investments that no longer are in the top tier and become ineligible securities and need to be sold. These securities held by the money market fund may be sold below its amortized cost resulting in losses and funds breaking the buck if the fund sponsor does not step in and buy above the current market value. Because of the recent difficulty encountered by certain funds, those funds have restricted withdrawals in some cases. Our money market funds maintained a positive yield, a USD 1.00 net asset value and were not subject to deposit or withdrawal restrictions as of March 31, 2009. However, if credit market conditions persist or worsen, the value of our money market funds could be adversely affected.

In addition, we have a lease financing liability, which was \$26.0 million at March 31, 2009, related to one of our two leased facilities in Redwood City, California (the Lab Building). Lease payments related to this financing liability, including amounts representing interest and ground rental expense, are reflected in the table below. Payments under the Lab Building lease agreement are subject to potential escalations based on market conditions after the year 2014 and, therefore, could be higher than amounts included in the table.

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(In thousands)	2009 *	2010	2011	2012	2013	Thereafter	Total
<b>Lease Financing Liability</b>							
Lease payments, including amounts representing interest and ground rental expense	\$ 2,621	\$ 3,616	\$ 3,743	\$ 3,874	\$ 4,009	\$ 36,914	\$ 54,777

\* The 2009 amount represents payments for the nine-month period between April 1, 2009 and December 31, 2009.

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**ITEM 4T. CONTROLS AND PROCEDURES**

***Evaluation of disclosure controls and procedures.*** We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the Exchange Act)) that are designed to ensure that information required to be disclosed in its reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including the chief executive officer and the chief financial officer, to allow timely decisions regarding required disclosures. Under the supervision and with the participation of our management, including our chief executive officer and chief financial officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, our chief executive officer and chief financial officer have concluded that our disclosure controls and procedures were effective as of March 31, 2009.

***Changes in internal control over financial reporting.*** There has been no change in the internal control over financial reporting of the Company that occurred during the first fiscal quarter covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

***Limitations on the effectiveness of controls.*** A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues, if any, within an organization have been detected. We continue to improve and refine our internal controls and our compliance with existing controls is an ongoing process.

**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

From time to time, we may be party to a variety of legal proceedings that arise in the normal course of our business. While the results of these legal proceedings cannot be predicted with certainty, management believes that the final outcome of currently pending proceedings will not have, individually or in the aggregate, a material adverse effect on our financial position, results of operations or cash flows.

**ITEM 1A. RISK FACTORS**

There have been no material changes from the risk factors disclosed in the Risk Factors section of our Annual Report on Form 10-K for the year ended December 31, 2008.



**ITEM 6. EXHIBITS**

- 31.1 Certification of Principal Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act, as amended
- 31.2 Certification of Principal Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act, as amended
- 32.1 Certification by the Chief Executive Officer and the Chief Financial Officer of PDL BioPharma, Inc., as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. 1350)

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**SIGNATURES**

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

Dated: May 8, 2009

FACET BIOTECH CORPORATION  
(Registrant)

/s/ Faheem Hasnain  
Faheem Hasnain  
President and Chief Executive Officer  
(Principal Executive Officer)

/s/ Andrew L. Guggenlime  
Andrew L. Guggenlime  
Senior Vice President and Chief Financial Officer  
(Principal Financial Officer)

/s/ Herb C. Cross  
Herb C. Cross  
Corporate Controller  
(Principal Accounting Officer)