

Innoviva, Inc.
Form 10-Q
May 04, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2018

OR

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

For the transition period from _____ to _____

Commission File Number: 000-30319

INNOVIVA, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

94-3265960
(I.R.S. Employer
Identification No.)

2000 Sierra Point Parkway, Suite 500

Brisbane, CA 94005

(Address of Principal Executive Offices)

(650) 238-9600

(Registrant's Telephone Number, Including Area Code)

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

Emerging growth company

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

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

The number of shares of registrant's common stock outstanding on April 30, 2018 was 101,470,190.

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(In thousands, except per share data)

	March 31, 2018 (unaudited)	December 31, 2017 *
Assets		
Current assets:		
Cash and cash equivalents	\$ 27,138	\$ 73,336
Short-term marketable securities	29,322	55,739
Related party receivables from collaborative arrangements	55,835	70,540
Prepaid expenses and other current assets	950	754
Total current assets	113,245	200,369
Property and equipment, net	197	209
Capitalized fees paid to a related party, net	163,266	166,722
Other assets	37	37
Total assets	\$ 276,745	\$ 367,337
Liabilities and Stockholders Deficit		
Current liabilities:		
Accounts payable	\$ 66	\$ 601
Accrued personnel-related expenses	537	1,721
Accrued interest payable	2,545	5,920
Other accrued liabilities	918	1,500
Current portion of long-term debt		25,000
Total current liabilities	4,066	34,742
Long-term debt, net of current portion, discount and issuance costs	484,591	574,362
Other long-term liabilities	835	940
Commitments and contingencies		
Stockholders deficit:		
Preferred stock: \$0.01 par value, 230 shares authorized, no shares issued and outstanding		
Common stock: \$0.01 par value, 200,000 shares authorized, 101,475 and 102,046 shares issued as of March 31, 2018 and December 31, 2017, respectively	1,014	1,019
Treasury stock: 150 shares as of March 31, 2018 and December 31, 2017	(3,263)	(3,263)
Additional paid-in capital	1,257,880	1,258,151
Accumulated other comprehensive loss	(22)	(18)
Accumulated deficit	(1,469,167)	(1,498,748)
Total Innoviva stockholders deficit	(213,558)	(242,859)
Noncontrolling interest	811	152
Total stockholders deficit	(212,747)	(242,707)
Total liabilities and stockholders deficit	\$ 276,745	\$ 367,337

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See accompanying notes to condensed consolidated financial statements.

*Condensed consolidated balance sheet as of December 31, 2017 has been derived from audited consolidated financial statements.

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INNOVIVA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended March 31,	
	2018	2017
Royalty revenue from a related party, net of amortization of capitalized fees paid to a related party of \$3,456 in the three months ended March 31, 2018 and 2017	\$ 52,380	\$ 40,271
Revenue from collaborative arrangements from a related party		221
Total net revenue	52,380	40,492
Operating expenses:		
Research and development		354
General and administrative	8,985	10,795
General and administrative - related party	2,700	
Total operating expenses	11,685	11,149
Income from operations	40,695	29,343
Other (expense) income, net	(3,099)	47
Interest income	391	236
Interest expense	(7,657)	(12,781)
Net income	30,330	16,845
Net income attributable to noncontrolling interest	749	
Net income attributable to Innoviva stockholders	\$ 29,581	\$ 16,845
Basic net income per share attributable to Innoviva stockholders	\$ 0.29	\$ 0.16
Diluted net income per share attributable to Innoviva stockholders	\$ 0.27	\$ 0.15
Shares used to compute Innoviva basic and diluted net income per share:		
Shares used to compute basic net income per share	100,604	107,487
Shares used to compute diluted net income per share	113,566	120,336

See accompanying notes to condensed consolidated financial statements.

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INNOVIVA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Three Months Ended March 31,	
	2018	2017
Net income	\$ 30,330	\$ 16,845
Unrealized loss on marketable securities, net	(4)	(2)
Comprehensive income	30,326	16,843
Comprehensive income attributable to noncontrolling interest	749	
Comprehensive income attributable to Innoviva stockholders	\$ 29,577	\$ 16,843

See accompanying notes to condensed consolidated financial statements.

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INNOVIVA, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Three Months Ended March 31,	
	2018	2017
Cash flows from operating activities		
Net income	\$ 30,330	\$ 16,845
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,468	3,496
Stock-based compensation	2,169	2,507
Amortization of debt discount and issuance costs	2,092	687
Loss on extinguishment of debt	3,137	
Amortization of premium (discount) on short-term investments	(100)	17
Amortization of lease guarantee	(81)	(81)
Changes in operating assets and liabilities:		
Receivables from collaborative arrangements	14,705	3,120
Prepaid expenses and other current assets	(196)	(114)
Accounts payable	(535)	2,176
Accrued personnel-related expenses and other accrued liabilities	(1,702)	752
Accrued interest payable	(3,375)	(1,428)
Other long-term liabilities	2	5
Deferred revenue		(221)
Net cash provided by operating activities	49,914	27,761
Cash flows from investing activities		
Maturities of marketable securities	31,875	26,387
Purchases of marketable securities	(5,362)	(3,992)
Net cash provided by investing activities	26,513	22,395
Cash flows from financing activities		
Repurchase of shares to satisfy tax withholding	(2,611)	(553)
Payments of principal on senior secured term loans	(120,000)	
Payments of cash dividends to stockholders	(38)	(67)
Proceeds from issuances of common stock, net	114	8
Payment of principal on non-recourse notes due 2029		(7,752)
Distributions to noncontrolling interest	(90)	
Net cash used in financing activities	(122,625)	(8,364)
Net (decrease) increase in cash and cash equivalents	(46,198)	41,792
Cash and cash equivalents at beginning of period	73,336	118,016
Cash and cash equivalents at end of period	\$ 27,138	\$ 159,808
Supplemental disclosure of cash flow information		
Cash paid for interest	\$ 8,941	\$ 13,522

See accompanying notes to condensed consolidated financial statements.

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INNOVIVA, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Description of Operations and Summary of Significant Accounting Policies

Description of Operations

Innoviva, Inc. (referred to as *Innoviva*, the *Company*, or *we* and other similar pronouns) is focused on royalty management. Innoviva's portfolio includes the respiratory assets partnered with Glaxo Group Limited (*GSK*), including RELVAR®/BREO®ELLIPTA® (fluticasone furoate/ vilanterol, *FF/VI*), ANORO® ELLIPTA®(umeclidinium bromide/ vilanterol, *UMEC/VI*) and TRELEGY® ELLIPTA® (the combination *FF/UMEC/VI*). Under the Long-Acting Beta2 Agonist (*LABA*) Collaboration Agreement, Innoviva is eligible to receive the associated royalty revenues from RELVAR®/BREO® ELLIPTA® and ANORO® ELLIPTA®. Innoviva is also entitled to 15% of royalty payments made by GSK under its agreements originally entered into with us, and since assigned to Theravance Respiratory Company, LLC (*TRC*), relating to TRELEGY® ELLIPTA® and any other product or combination of products that may be discovered and developed in the future under the LABA Collaboration Agreement and the Strategic Alliance Agreement with GSK (referred to herein as the *GSK Agreements*), which have been assigned to TRC other than RELVAR®/BREO® ELLIPTA® and ANORO® ELLIPTA®.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (*GAAP*) for interim financial information. Accordingly, they do not include all of the information and notes required by GAAP for complete financial statements. In our opinion, the unaudited condensed consolidated financial statements have been prepared on the same basis as audited consolidated financial statements and include all adjustments, consisting of only normal recurring adjustments, necessary for the fair presentation of our financial position, results of operations, comprehensive income and cash flows. The interim results are not necessarily indicative of the results of operations to be expected for the year ending December 31, 2018 or any other period.

The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2017 filed with the Securities and Exchange Commission (*SEC*) on February 23, 2018.

Variable Interest Entity

We evaluate our ownership, contractual and other interest in entities to determine if they are variable interest entities (VIE), whether we have a variable interest in those entities and the nature and extent of those interests. Based on our evaluations, if we determine we are the primary beneficiary of such VIEs, we consolidate such entities into our financial statements. We consolidate the financial results of TRC, which we have determined to be a VIE, because we have the power to direct the economically significant activities of TRC and the obligation to absorb losses of, or the right to receive benefits from, TRC.

Accounting Pronouncement Adopted by the Company

In April 2016, the Financial Accounting Standards Board (the FASB) issued Accounting Standards Update (ASU) 2016-10 to clarify the implementation guidance on licensing and the identification of performance obligations consideration included in ASU 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), which is also known as ASC 606, was issued in May 2014 and outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. In March 2016, the FASB issued ASU 2016-08 to provide amendments to clarify the implementation guidance on principal versus agent considerations. We implemented the standard on the effective date of January 1, 2018 on a modified retrospective basis to contracts which were not completed as of this date. Adoption of this standard did not have a material impact on our consolidated financial statements as we did not have any unrecognized transaction price, other than sales-based royalty revenue, or any remaining performance obligations under our collaboration agreements. We continue to recognize royalty revenue when it is earned.

Table of Contents***Recently Issued Accounting Pronouncement Not Yet Adopted***

In February 2016, the FASB issued ASU 2016-02, *Leases*, which supersedes the lease recognition requirements in ASC Topic 840, *Leases*. The standard requires an entity to recognize right-of-use assets and lease liabilities arising from a lease for both financing and operating leases in the consolidated balance sheets but recognize the impact on the consolidated statement of operations and cash flows in a similar manner under current GAAP. The standard also requires additional qualitative and quantitative disclosures. The standard is effective for us at the beginning January 1, 2019 and requires transition under a modified retrospective method. The most significant impact of the update to us is that we will be required to recognize a right-of-use asset and lease liability for the operating lease agreement that was not previously included on the balance sheet under the existing lease guidance. We anticipate that the treatment of the lease on our consolidated statement of operations and cash flows will not materially be affected by the adoption of the new standard.

2. Net Income Per Share

Basic net income per share attributable to Innoviva stockholders is computed by dividing net income attributable to Innoviva stockholders by the weighted-average number of shares of common stock outstanding. Diluted net income per share attributable to Innoviva stockholders is computed by dividing net income attributable to Innoviva stockholders by the weighted-average number of shares of common stock and dilutive potential common stock equivalents then outstanding. Dilutive potential common stock equivalents include the assumed exercise, vesting and issuance of employee stock awards using the treasury stock method, as well as common stock issuable upon assumed conversion of our convertible subordinated notes due 2023 (the 2023 Notes) using the if-converted method.

Our convertible senior notes due 2025 (the 2025 Notes) are convertible, based on the applicable conversion rate, into cash, shares of our common stock or a combination thereof, at our election. Our current intent is to settle the principal amount of the 2025 Notes in cash upon conversion. The impact of the assumed conversion premium to diluted net income per share is computed using the treasury stock method. As the average market price per share of our common stock as reported on The Nasdaq Global Select Market was lower than the initial conversion price of \$17.26 per share, there was no dilutive effect of the assumed conversion premium for the three months ended March 31, 2018.

The following table shows the computation of basic and diluted net income per share for the three months ended March 31, 2018 and 2017:

(In thousands except per share data)	Three Months Ended March 31,	
	2018	2017
Numerator:		
Net income attributable to Innoviva stockholders, basic	\$ 29,581	\$ 16,845
Add: interest expense on 2023 Notes	1,412	1,407
Net income attributable to Innoviva stockholders, diluted	\$ 30,993	\$ 18,252
Denominator:		
Weighted-average shares used to compute basic net income per share attributable to Innoviva stockholders	100,604	107,487

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Dilutive effect of 2023 Notes	12,189	12,189
Dilutive effect of options and awards granted under equity incentive plan and employee stock purchase plan	773	660
Weighted-average shares used to compute diluted net income per share attributable to Innoviva stockholders	113,566	120,336
Net income per share attributable to Innoviva stockholders		
Basic	\$ 0.29	\$ 0.16
Diluted	\$ 0.27	\$ 0.15

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Anti-Dilutive Securities

The following common stock equivalents were not included in the computation of diluted net income per share because their effect was anti-dilutive:

(In thousands)	Three Months Ended March 31,	
	2018	2017
Outstanding options and awards granted under equity incentive plan and e		